

# “The implementation of debt counselling: an exploratory study”

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## The implementation of debt counselling: an exploratory study

### Abstract

The South African working class is faced with the challenges of over-indebtedness. As a result of this phenomenon, measures were introduced to assist people (consumers) to manage and control over-indebtedness. One of the measures introduced is debt counselling to assist over-indebted people to approach debt counsellors to assist them to rearrange their debt obligations. This intervention is aimed at providing assistance to the consumers by way of budget advice, restructuring their payments, negotiating with credit providers on their behalf, monitoring their payments while providing after-care services. The purpose of the study is to explore and understand the challenges regarding the implementation of debt counselling. A qualitative approach was adopted for the study which is exploratory in nature. Data are collected from ten (10) debt counsellors through interviews. The findings of the study indicate that debt counselling is making strides in improving over-indebtedness of the consumers. It further emerged that the debt counsellors abide strictly to the guidelines and regulations provided by NCR. The debt counsellor also highlighted that there is no mechanism to monitor further indebtedness by the rehabilitees.

**Keywords:** consumers, debt counsellor, national credit regulator, over-indebtedness.

**JEL Classification:** H63.

### Introduction

South Africans are faced with the challenge of over-indebtedness. This however, is characterized by the fact that many people have taken credit that they cannot afford. Non-payments of credit obligations if not properly managed could hamper economic growth of the country since credit providers will realize a huge amount of bad debts. This is confirmed by the National Credit Regulator's (NCR) credit market report which indicates that the value of credit granted to consumers by the end of 2012 was R119.94 billion (NCR, 2013). The report further indicates that the outstanding gross debtors' book was R1.44 trillion during the same period.

Various reports indicated that consumer credit legislation needed an overview. These include the concern about over-indebtedness, fee structures in the banks' debit order system and the increase in micro-lending (DTI, 2003). The South African government expressed concern about credit markets and credit market legislation. Among the issues of concern were: consumer protection, particularly in relation to consumers in low income groups; increasing levels of indebtedness; and reckless behavior of credit providers, and the exploitation of consumers by micro-lenders, intermediaries, debt administrators and debt collectors (DTI, 2003).

To avoid the predicament of bad debts, the government introduced the National Credit Act (NCA) 34 of 2005, aimed at transforming the South African credit industry (South Africa, 2006). The NCA also aimed at putting forth a consistent regulatory and enforcement model which could ensure a fair and non-discriminatory market place for access to consumer credit (South Africa, 2006).

The main purpose of the NCA is to provide debt relief to the over-indebted consumer, and provide a

chance to survive the repercussion of his or her financial setback and to attain a manageable financial position (Roestoff, Haupt, Coetzee & Erasmus, 2009, p. 253). The implementation of the NCA brought the introduction of debt review restructuring, thus leading to the establishment of debt counselling.

According to the study conducted by Kim, Sorhaindo and Garman (2003), over-indebted consumers are likely to benefit from debt counselling services. Elliehausen, Landquist and Staten, (2007) concur with Kim et al. (2003) in their study by demonstrating that debt counselling process has a positive impact on consumer behavior.

The rest of the article proceeds as follows: section 1 provides the purpose of the study. Section 2 presents a theoretical background and analysis of debt counselling process. Section 3 discusses the methodology used in this study. Section 4 presents the findings obtained. The recommendations and suggestions for further research are provided in sections 5 and the conclusion is presented in final section.

### 1. Purpose of the study

There is a growing concern about lending patterns, debt enforcement procedures and practices, debt rehabilitation and consumer vulnerability in South Africa (Business Enterprises, 2012; & Daily Industry News, 2012). In addition, previous studies conducted on debt counselling focused on the legal impact of the National Credit Act No. 34 of 2005 (DTI, 2003; Roestoff et al., 2009). Very little, if any, research has been done on the evaluation of debt counselling from the debt counsellors' perspective.

It is against this background that the authors of this article aim to close this gap and contribute to the existing literature by investigating and describing the debt review programs, specific services rendered to

consumers, intervention and mechanisms offered to over-indebted and rehabilitated consumers.

The purpose of this study was therefore two-fold. Firstly, the study evaluated the debt counselling process from the debt counsellors' perspective. Secondly, the study evaluated the role that the NCR plays in terms of monitoring activities offered by debt counsellors to consumers.

## 2. Literature review

The expansion of consumer credit in South Africa started to be visible since 1968 and has been going on over the past years. Excessive interest rates paid by borrowers have caused heinous socio-economic hardships and sufferings for low-income individuals and communities (Du Plessis, 2007). A high percentage of personal income is used to service micro-lending debt, leaving very little of borrowers' personal income to pay for other household expenses (South Africa, 2006).

The South African consumer credit legislation had originally consisted of the Usury Act No. 73 of 1968 and the Credit Agreement Act No. 75 of 1980. The Usury Act revolved around the interest rates that credit providers could lawfully charge, whilst the Credit Agreement Act focused on the contracts drafted between credit providers and consumers (Barnard, 2010).

The Usury Act and the Credit Agreements Act provided a limit on interest rate charged by credit providers. This was circumvented when credit providers added costs such as credit life insurance, loan application fees, administration fees, club fees and various bank service charges. These Acts, according to Barnard (2010), did not protect consumers neither did they regulate credit providers. As a result, credit was recklessly extended to consumers. These anomalies led the South African government to institute various investigations, which led to the implementation of the National Credit Act (NCA) No. 34 of 2005. With the introduction of the NCA, the National Credit Regulator (NCR) was established in 2006, and the inception of debt counselling and debt review processes came into effect.

The NCR is tasked with carrying out education and creating awareness of the NCA, registration of credit providers, credit bureaus and debt counsellors (NCR, 2010). Furthermore, the NCR has to monitor the conduct of these parties and to investigate complaints from the parties and the consumers. The NCR must also ensure enforcement of the NCA and take action against contravening parties (NCR, 2010).

According to Davel (2010), despite the objectives and the provisions of the NCA, the economic recession in South Africa had a negative impact on

employment and ultimately reduced individuals' income. This resulted in a growing number of consumers falling into arrears on their debt repayments. Consumers are therefore resorting to debt counselling for protection (Davel, 2010).

Debt counselling is a process of assisting consumers who are experiencing debt related problems through budget advice, restructuring their payments, negotiating with credit providers on their behalf, monitoring their payments while providing after-care services. It is an educational program that aims to create awareness about credit-related services to consumers who borrow money and make use of credit facilities (Kelly-Louw, 2008). It also provides a consistent system of debt restructuring, enforcement and judgement, which places priority on the eventual satisfaction of the consumer's obligations under the credit agreements (De Wet, 2011, pp. 1-2).

The debt review procedure as stipulated in section 86 of the NCA, allows an over-indebted consumer to seek intervention from a registered debt counsellor who would evaluate the merit of the application tendered (Goslet, 2011). Section 79 of NCA prescribes that the consumer may be described as over-indebted if the debt counsellor is of the view that the consumer will probably not meet his or her financial commitments at the end of each month (South Africa, 2006). In the quest to assist the consumer, the debt counsellor should create debt restructuring agreement which is recommended by the NCR and acceptable to all credit providers (De Waal, 2013).

Consumers often turn to debt counsellors when their credit becomes unmanageable and their debt problems make it impossible to pay their financial obligations (Wang, 2010). A consumer who is experiencing debt repayment problems may seek debt restructuring assistance by applying for debt counselling service at any debt counsellor of his or her choice. The debt counsellor has to explain all the details pertaining to the debt counselling process to the consumer before he or she signs any debt counselling application and agreement forms (Debt Counselling Help South Africa, 2009). According to Wang (2010), debt counselling is often seen as a last resort to over-indebted consumers.

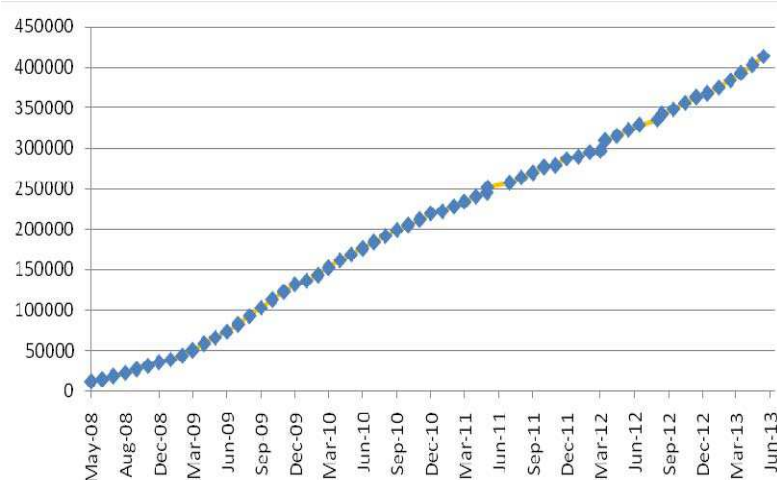
**2.1. Challenges facing debt counselling.** Although debt counselling service in South Africa has been a primary debt relief remedy for over-indebted consumers, it still needs to be standardized and accepted amongst credit providers and debt counsellors (Business Enterprises, 2012). Some credit providers have neither the capacity nor the understanding of appropriate policies and procedures to respond adequately to debt restructuring proposals

and as a result, backlogs in the debt counselling process are experienced (Davel, 2010).

According to Groenewald (2010), since the inception of the NCA, the debt counselling process has been plagued with challenges and obstacles. The levels of competencies of debt counsellors, education and experience in the debt review have been identified as some of the barriers hampering effective debt counselling process. In assessing the preparedness of the debt counsellors before they start with debt review process, Groenewald (2010) launched an intensive study to determine the competency requirements and skills needed for the debt counsellors. The findings revealed that some debt counsellors were incompetent, lacked integrity and knowledge of financial management as well as knowledge of credit legislation.

According to Business Enterprises (2012), a two-week course that debt counsellors undergo as a pre-requisite for their registration is only based on theoretical issues of debt counselling. Moreover, the course does not empower debt counsellors to deal with complex administrative tasks neither does it capacitates debt counsellors with financial management skills.

**2.2. Effectiveness of debt counselling.** At the time this study was undertaken (2013 to 2014), there was an ongoing increase in the number of consumers seeking debt counselling assistance. According to the NCR (2014), records indicate that in May 2008, there were 12 574 consumers who applied for debt counselling and this number had increased to 412 918 by the end of May 2013 as indicated in Figure 1.

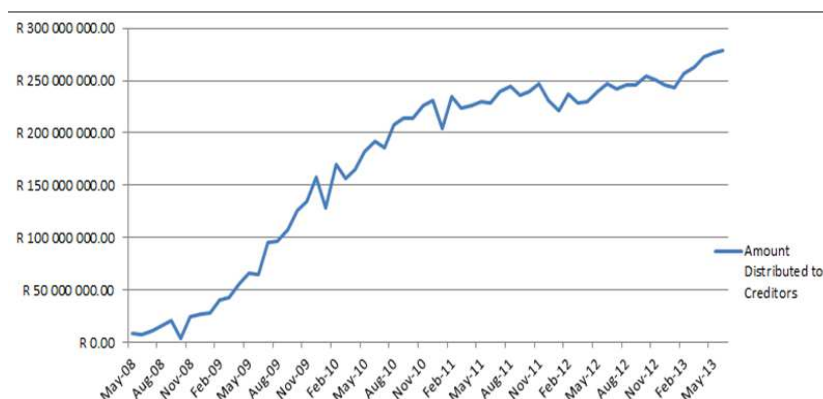


Source: adapted from NCR (2014).

**Fig. 1. Consumers who applied for debt counselling from May 2008 to May 2013**

The increase in demand for debt counselling indicates that consumers realize the importance and the effectiveness of debt counselling. Another indication of the effectiveness of debt counselling came from the relationship between the debt counsellors and the Payment Distribution Agencies (PDAs) (NCR, 2014). The PDAs provide an efficient mechanism for the payment of creditors. Debt counsellors were

succeeding in helping consumers pay their debts through the PDAs (NCR, 2014). In May 2008, the amount disbursed by the PDAs to creditors was R8 969 569.62, and this amount increased substantially to R276 696 485.68 by May 2013 as illustrated in Figure 2. Without debt counselling, these consumers would not have had any recourse to an independent mechanism to assist them.



Source: adapted from NCR (2014).

**Fig. 2. Payments distributed by PDAs to creditors from May 2008 to May 2013**

### 3. Research methodology

The study adopted the qualitative approach. With this type of approach, which is exploratory in nature, it was envisaged that the qualitative research method would provide an opportunity to unravel the debt counsellors' experiences on the debt counselling. The exploration enabled the researcher to obtain better understanding of challenges that they ordinarily experience in their endeavours (Creswell, 2009, p. 4). The study was conducted in Gauteng Province.

The sample consisted of debt counsellors ( $n = 10$ ) who were purposefully selected to be part of the study with the notion that the researchers regarded as appropriate typical units as they are likely going to benefit the study. The sampling technique used was informed by the fact that it is typically used when participants possess professional knowledge of the matter under study; hence debt counsellors were deemed appropriate in this regard.

Before data collection, the researchers made appointments with the debt counsellors to ensure that they would have time set aside for the interview. Interview guide was used to collect the data from the debt counsellors. Different questions were used, followed by probing questions to get a deeper understanding of the phenomenon.

Data were analyzed thematically by way of Tesch's data reduction method using the eight steps by Tesch (1990) namely: (1) get a sense of the whole by reading all the transcripts carefully; (2) pick one interview and go through it without thinking of the substance or essence thereof; (3) when all interviews have been completed, make a list of all topics; (4) take the list and go back to the data and abbreviate codes; (5) find the most descriptive wording of your topics as codes and turn them into codes; (6) make a final decision on the abbreviation for each category and alphabetize the codes; (7) assemble the data material belonging to each category in one place and perform a preliminary analysis and (8) in this last step, if necessary, recode existing data.

### 4. Research findings

In the analysis of the data, the following themes emerged: consumers' financial position, debt counselling process, effectiveness of debt counselling and NCR support. Results gathered from these themes are discussed in the next sub-section.

**4.1. Consumers' financial position.** Debt counsellors indicated that most of their clients are working and earning salaries. It emerged that most of the clients use their salaries for groceries, rent, school fees and transport. It was further noted that most of

the clients have personal loans as well as unsecured loans which increase their personal expenditure.

*'Almost all my clients are salaried. They have a lot of personal loans. They lack financial management. They are tempted to make lots of credit, they want instant gratification. Basically, they live lifestyles that they can't afford'.*

*'Yes, 100% of my clients are salaried, their salary ranges from R1 000 to R50 000. People have lifestyles that they don't afford'.*

*'Most of our clients are employed and they earn a salary. Most of them are uneducated. They become over-indebted because they try to maintain a lifestyle that they can't afford'.*

From the findings it can be deduced that consumers did not have the ability to prioritize their expenses as indicated by the debt counsellor. They lacked financial management knowledge and they live expensive lifestyles, which result in spending more than they earn. If this situation is not monitored, the consumers will remain deeply indebted.

**4.2. Debt counselling process.** The debt counsellors agreed that they were using the prescribed guidelines in conducting debt counselling process and were sticking to the stipulated maximum duration (60 months) for the debt counselling process. They further indicated that payslips, identity document, proof of residence and a three-month bank statement are the most important documents that they require from consumers who apply for debt counselling.

*'I stick to the rules. I require payslips, proof of residence, IDs just to make sure they are telling me the truth. The whole process lasts 5 years.'*

*'NCR has prescribed rules that guide us, and we have to follow. Documents that we need are three-month bank statement, IDs, payslips, proof of residence. Regarding how long it takes, I can say, at most 60 months or 5 years'.*

*'We follow NCR guidelines. Okay, they bring IDs, payslips, proof of residence. Some finish paying soon, but the maximum duration expected is 60 months'.*

It can be noted that debt counsellors abide to the guidelines for debt counselling process as prescribed and regulated by the NCR. The abidance by the debt counsellors in the debt counselling process is due to strict monitoring provided by NCR.

**4.3. After-care service.** After-care service and moral support were indicated as the only intervention methods that debt counsellors provide to their clients. In addition, debt counsellors agreed that they do not collect money from their clients instead; they engage

the services of the Payment Distribution Agency (PDA) to collect monthly payments.

*'Look, we do advice our clients here and there. I tell my clients that debt counselling fees are paid through the PDAs'.*

*'Normally I encourage them to come anytime when they feel like asking something. I give them moral support. Look, I collect R50 application fee only, the rest goes to the PDA'.*

*'I am a professional counsellor. I give my clients support they need. I provide after-care service. I don't collect any money from clients; they have to pay through the PDA'.*

It emerged that the intervention methods debt counsellors provide are moral support and after-care service. They also make referrals to the PDA for payments.

**4.4. Effectiveness of debt counselling.** Debt counsellors emphasized the importance of debt counselling and indicated that the process is indeed assisting the over-indebted consumers. They further indicated that they monitor their clients by offering moral support and after-care services during the debt review period only. They do not have mechanisms to monitor clients post-debt counselling service.

*'We do not provide any assistance in terms of following up those that have paid up their debts.'*

*'Mechanisms? No, I don't have.'*

*'No I do not have any mechanisms to give to clients who paid up their debts. Maybe your research will help.'*

It is evident that the debt counselling has made some strides in helping over-indebted people. It can however be deduced that though there is progress in debt counselling, there should be a mechanism to monitor rehabilitees.

**4.5. NCR support.** Debt counsellors were discontent with the support they receive from the NCR. They authenticated their discontent according to their perceived importance, by providing the following reasons:

*'NCR staff is not handling my queries efficiently, I had problems of cooperation with some of the credit providers, I reported to NCR, nothing is been done.'*

*'NCR is taking time to implement transfers of consumers from one debt counsellor to another.'*

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*'Some debt counsellors had to close business because of a lack of support from the NCR.'*

*'NCR is not involving us when making decisions that affect us'.*

Debt counsellors indicated their frustration about the support provided by NCR. Some of the frustrations experienced are lack of assistance from NCR; NCR not involving them in making decisions that affect them; and delays in the transfer of clients from one debt counsellor to another.

## 5. Recommendations

Based on the findings of the research, the following recommendations are suggested.

First, debt counsellors should be subjected to formal training and assessment on business-related matters and on financial management education. Second, debt counsellors should include personal financial management training as an intervention method to their clients. Third, NCR should reconsider the educational level of the prospective debt counsellors. Fourth, NCR should improve on monitoring and supporting debt counsellors. Fifth, both debt counsellors and the National Credit Regulators should monitor the financial performance of consumers after being rehabilitated.

## Conclusion

The study has investigated implementation of debt counselling focusing on the debt counsellors. Whilst there are challenges facing the debt counsellors in South Africa, the research findings indicated how effective debt counselling can be. However, relevant debt counselling training, more intervention methods to help over-indebted consumers as well as mechanisms that can monitor rehabilitated consumers are still lacking. NCR has to improve the support that they provide to debt counsellors to ensure that they are effective in their practices.

One of the limitations of this study is the nature of the sample. The sampled debt counsellors were from Gauteng province only.

To conclude, this study has provided vital information on how participants view the implementation of debt counselling. Though empirical evidence suggests that there is effective implementation of debt counselling, some challenges were highlighted that no monitoring mechanism is in place to assess rehabilitees. This study confirms that there is a need to train debt counsellors to ensure that they are effective in their respective roles.

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