Lending to your staff? Some pitfalls

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The National Credit Regulator, which is the statutory body responsible for implementation and enforcing the NCA, considers employee loans to fall within the ambit of the NCA.

An employer must register as a credit provider if:

1. it provides at least 100 employee loans
2. the total principal debt owed under all outstanding employee loans exceeds R500,000

Employers who don't fall into either of the above categories and therefore don't need to register as credit providers MUST STILL COMPLY with the provisions of the NCA where it applies to employee loans.

Downside of providing in-house loans:

NCA compliance issues

To ensure that employee loans meet the requirements of the NCA, employers must then, at the very least:

1. - The financial means and obligations of the borrower
   - The borrower's propensity to pay by analysing their previous debt repayment history
   - The borrower's general understanding of the risks, costs rights and obligations under the agreement

BEFORE entering into the agreement, conduct an assessment of

2. - Information that is clear, concise and in plain language
   - Particulars of the total cost of the credit
   - A credit agreement in an official language

WHEN entering into the agreement, provide the employee with

Other provisions may include those pertaining to maximum interest, fees and charges; prevention of reckless credit granting; agreements in the prescribed form; statements of account; pre-agreement statements and quotations and debt recovery procedures.

SARS taxation issues

The employer also has certain obligations to SARS as prescribed by the Income Tax Act. Paragraph 18 states that the employer must declare that all taxable benefits enjoyed by their employees are included in the employees' tax certificate issued to employees.

A taxable benefit is deemed to have been granted by the employer if the employee receives a low or interest free loan. The value of the benefit is the amount of interest on the loan at the official rate less any interest actually incurred by the employee.

Employees' tax is payable on this amount and the value of the benefit must be reflected on the IRP5 certificate.

Note that the benefit has no value in the event of casual loans (short-term loans made at irregular intervals) granted which do not exceed R3,000 and the granting of loans for study purposes.

Working Capital drain

Cash that would normally be available to the business for stock replenishment, marketing, repairs and maintenance etc is no longer available.

Some businesses do not have the cash flow to fund staff loans.
They need every cent to be spent in the production of income.
There is also the interest cost of this capital.

Over indebtedness

Businesses do not have access to the National Loan Register. The credit history, payment record, adverse credit and judgements of all credit active consumers are listed here.

Employers rely on the truthfulness and honesty of details provided by applicants but these may not be 100% complete and accurate. Applicants may have omitted to disclose certain information.

This may lead to an incorrect affordability assessment and over-indebtedness may result.

A credit check is necessary to validate information provided.

Declined loans lead to poor morale and productivity

That's what happens when there's an element of subjectivity in the loan approval process. Employees talk and this inevitably leads to upset amongst those who feel compromised.

Time and resources spent on handling staff loan issues

The time spent by Human Resources and Payroll on staff loan issues could be allocated elsewhere much more productively. (eg areas such as staff training and financial wellness programs etc.).

Also the applicant sees the loan as immediate and urgent. The timing may not be suitable for the HR / Payroll personnel and is a distraction from other pressing functions and routines.

Conflict then prevails!

Solution

Outsource this activity to a reputable credit provider.

There are employers who prefer to provide in-house loans to their staff. They see the upside as fostering good staff relations.

They also have a paternalistic instinct to protect their employees from unscrupulous lenders.