

THE STATUTORY SECURITY RIGHT IN SECTION 118(3) OF THE LOCAL GOVERNMENT: MUNICIPAL SYSTEMS ACT 32 OF 2000 – DOES IT SURVIVE TRANSFER OF THE LAND?

[DISCUSSION OF *CITY OF TSHWANE METROPOLITAN MUNICIPALITY V MATHABATHE* 2013 4 SA 319 (SCA)]

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1 Introduction

Section 118 of the Local Government: Municipal Systems Act 32 of 2000 (“LGMS Act”) provides for two interrelated but also seemingly independent mechanisms that secure a municipality’s claim for the payment of “municipal service fees, surcharges on fees, property rates and other municipal taxes, levies and duties” that are overdue with respect to immovable property (henceforth referred to as “municipal debts”). Hence, the section seemingly establishes statutory real security rights in favour of municipalities. The recent decision of the Supreme Court of Appeal (“SCA”) in *City of Tshwane Metropolitan Municipality v Mathabathe*¹ (“*Mathabathe*”) calls for a closer look at especially section 118(3).

Section 118(1) contains an “embargo” or “veto” provision in terms of which the municipality will refuse to issue a so-called clearance certificate unless all municipal debts for the preceding two years have been settled in full. If the certificate is not issued, the registrar of deeds may not register the transfer of the property concerned. This rule is confirmed by section 92(1) of the Deeds Registries Act 47 of 1937. Therefore, as the title of section 118 indicates, the municipality’s security involves a restraint on the transfer of the property until such time as the amounts due for the previous two years have been paid. The payment of this “two-year debt” is effectively secured in this manner and naturally it is preferent to all other claims that might have to be paid from the proceeds of the sale of the property, except for certain qualifications in insolvency law.²

* Thank you to Chantelle Gladwin, André van der Walt, Gerhard Brits and the two anonymous referees for their valuable comments

¹ 2013 4 SA 319 (SCA)

² S 118(2) of the LGMS Act states that the section is subject to s 89 of the Insolvency Act 24 of 1936

Even though section 118(1) has been the subject of controversy as well,³ the focus of this contribution is on the real security right established by section 118(3). The subsection provides that an amount due for municipal debts “is a charge upon the property in connection with which the amount is owing”. Notably this subsection, unlike section 118(1), involves no time limit and therefore the charge secures the payment of all outstanding municipal debts, and not only of the debts for the previous two years.⁴ Even more strikingly, the charge “enjoys preference over any mortgage bond registered against the property”, and the fact that the bond was registered before the charge came into existence, or before the Act came into force, makes no difference.⁵

These provisions have been a source of disquiet over the last couple of years and the SCA has had the opportunity to pronounce on their interpretation a number of times.⁶ The latest important case on section 118 is the one under discussion. Although the decision apparently provides clarity as to the nature of a municipality’s rights, it raises some questions as well. The purpose of this contribution is to expose one particular issue surrounding the statutory security measure in section 118(3) that is in need of further contemplation, namely its possible enforcement against successors in title. A subsequent unreported judgment of the high court⁷ seems to provide some direction in this respect, but because *Mathabathe* was decided by the SCA, only that court (or the Constitutional Court) can authoritatively clarify the legal position. It is important that there should be more clarity regarding the functioning and consequences of section 118(3), since it may have significant implications in the context of transfers of ownership of land and sectional title units, as well as the registration, enforcement and the security value of mortgage bonds. This contribution is not a comprehensive analysis of the matter, but it highlights some of the issues and provides brief comments as to the way section 118 should be interpreted on this point.

³ See for example *Mkontwana v Nelson Mandela Metropolitan Municipality*; *Bissett v Buffalo City Municipality*; *Transfer Rights Action Campaign v Member of the Executive Council for Local Government and Housing, Gauteng* 2005 1 SA 530 (CC). For a discussion, see especially AJ van der Walt “Retreating from the FNB Arbitrariness Test Already? *Mkontwana v Nelson Mandela Metropolitan Municipality*; *Bissett v Buffalo City Municipality*; *Transfer Rights Action Campaign v MEC for Local Government and Housing, Gauteng*” (2005) 122 *SALJ* 75

⁴ *BOE Bank Ltd v City of Tshwane Metropolitan Municipality* 2005 4 SA 336 (SCA) para 11; *City of Johannesburg v Kaplan NO* 2006 5 SA 10 (SCA) paras 13, 20; *City of Tshwane Metropolitan Municipality v Mathabathe* 2013 4 SA 319 (SCA) para 9. For present purposes I do not consider the role of prescription

⁵ *BOE Bank Ltd v City of Tshwane Metropolitan Municipality* 2005 4 SA 336 (SCA) paras 13-14

⁶ Notable examples with regard to s 118(3) include *BOE Bank Ltd v City of Tshwane Metropolitan Municipality* 2005 4 SA 336 (SCA); *City of Johannesburg v Kaplan NO* 2006 5 SA 10 (SCA); *City of Cape Town v Real People Housing (Pty) Ltd* 2010 5 SA 196 (SCA). For discussions, see M Kelly-Louw “Selling or Leasing Property? Beware of Municipal Debts! A Note in Two Parts (Part I)” (2005) 122 *SALJ* 557; M Kelly-Louw “Selling or Leasing Property? Beware of Municipal Debts! A Note in Two Parts (Part II)” (2005) 122 *SALJ* 778

⁷ *Perregine Joseph Mitchell v City of Tshwane Metropolitan Municipal Authority* NGP 08-09-2014 case no 50816/14 (judgment on file with author), discussed in part 3.2 below

2 The *Mathabathe* case

2.1 Factual background and decision

After the first respondent's immovable property was sold at a public auction, his agent (and mortgage creditor) instructed its attorney to see to the registration of the transfer of ownership. The attorney applied to the City of Tshwane Metropolitan Municipality ("the Municipality") to issue the clearance certificate that is required in order for transfer to take place. Section 118(1) of the LGMS Act provides as follows:

- "(1) A registrar of deeds may not register the transfer of property except on production to that registrar of deeds of a prescribed certificate –
- (a) issued by the municipality or municipalities in which that property is situated; and
 - (b) which certifies that all amounts that become due in connection with that property for municipal service fees, surcharges on fees, property rates and other municipal taxes, levies and duties during the two years preceding the date of application of the certificate have been fully paid."

The certificate that the Municipality issued indicated a total outstanding amount of R162,722.26, which included an amount of R151,324.22 – the so-called "historical debt".⁸ The historical debt is that part of the total that is due for rates and services rendered prior to the two-year period. In other words, section 118 distinguishes between two parts of the total municipal debt, namely the part owing for rates and services rendered within the two years preceding the application for a clearance certificate and the part owing for services rendered before the two years. Section 118(3) secures both parts, whereas section 118(1) restrains transfer only with regard to the former. It is useful to refer to these parts as the "two-year debt" and the "historical debt".

After an unsuccessful attempt to persuade the Municipality to furnish the certificate without taking account of the historical debt, the attorney applied to the North Gauteng High Court, seeking an order compelling the Municipality to issue a statement indicating only the amounts that became due during the preceding two years. Furthermore, she requested an order that the Municipality issue a clearance certificate in terms of section 118(1) as soon as the two-year debt is paid, and that the Municipality be ordered to adhere strictly to section 118(1).⁹ The Municipality opposed the relief sought and initiated a counter application for an order that R87,440.17 (apparently the two-year debt) must be paid before it issues the clearance certificate, which would enable registration of the transfer. Secondly, the Municipality wanted the court to order the respondents to provide it with an undertaking that the arrear amount of R87,743.64 (the historical debt) will be paid to the Municipality on the date of registration or within a reasonable time thereafter, in accordance with section 118(3) of the Act.¹⁰

In the court *a quo* Goddey AJ granted the relief sought by the respondent and dismissed the Municipality's counter application. The case under

⁸ *City of Tshwane Metropolitan Municipality v Mathabathe* 2013 4 SA 319 (SCA) para 3

⁹ Para 4

¹⁰ Para 5 Nowhere in the judgment is there any explanation as to the discrepancy between the amounts indicated on the initial certificate and the amounts claimed by the municipality

discussion concerns the Municipality's appeal against the high court's decision. The Municipality indicated that it did not appeal against the order that granted the relief sought by the attorney but only against the rejection of its counter application. The Municipality explained that it initially believed that it could withhold the clearance certificate unless it had an undertaking that the historical debt would be paid subsequent to registration. Yet, it now conceded that the respondents were entitled to the clearance certificate if the two-year debt was paid. Accordingly, the Municipality only appealed against the high court's rejection of its claim for an undertaking that the historical debt be paid upon registration.¹¹

The Municipality contended that the respondents' attorney failed to have regard to section 118(3) of the Act, which provides as follows:

"(3) An amount due for municipal service fees, surcharges on fees, property rates and other municipal taxes, levies and duties is a charge upon the property in connection with which the amount is owing and enjoys preference over any mortgage bond registered against the property."

Therefore, the Municipality based its counter application on the "*lien (hypothec)*" that section 118(3) grants it over the property and the preference that it enjoys over registered mortgage bonds by virtue of this security.¹² It appears that the reason why the Municipality insisted on an undertaking for the payment of the historical debt is that, without it and upon registration, the conveyancer would pay the outstanding moneys to the mortgagee and therefore that the Municipality would lose its rights under section 118(3). By virtue of the "*lien*" that section 118(3) provides the Municipality for the historical debt, it claimed that it is only obliged to issue the clearance certificate when it receives an undertaking from the transferring attorney that it will receive the amount of the historical debt upon registration or within a reasonable time thereafter.¹³

Consequently, it seems that the Municipality understood the nature of its right under section 118(3) to be that it is entitled to an undertaking for the amount of that debt. However, as the SCA's analysis indicates, the Municipality was labouring under a misconception as to nature of the real security right it enjoys in terms of section 118(3) of the Act. Indeed, the undertaking that the Municipality was seeking turned out to be superfluous, because the security right, contrary to the Municipality's previous assumptions, does not fall away when the property is transferred.

2 2 The Supreme Court of Appeal's analysis

The court explained that municipalities are assisted to enforce their debts in two ways – by being granted a charge upon the property (section 118(3)) and by being afforded an ability to prevent transfer of ownership until the two-year debt has been paid (section 118(1)).¹⁴ Therefore, the Act provides

¹¹ Paras 6-7

¹² Para 8

¹³ Para 8

¹⁴ Para 9, citing *City of Cape Town v Real People Housing (Pty) Ltd* 2010 5 SA 196 (SCA) para 2

municipalities with a right of veto or embargo (with a time limit) as well as a security (without a time limit).¹⁵ Although both aspects are aimed at ensuring payment of municipal debts, they involve different mechanisms.¹⁶

Section 118(3) is “an independent, self-containing provision”,¹⁷ and the security it provides amounts to a lien that has the effect of a tacit statutory hypothec.¹⁸ The court moreover explained that no limit is placed on the duration of the security, save for insolvency.¹⁹ The effect of this tacit statutory hypothec is to create a security for the payment of municipal debts so that the Municipality will enjoy a preference over a registered mortgage bond.²⁰ It should be pointed out that the description of the right as a “lien” that has the effect of a “tacit statutory hypothec” is unnecessarily strained. Since this security right is created by statute and therefore *sui generis*, one should not try to fit it into the traditional categories of real security rights. Instead, it should be referred to by the name it is given in the statute, namely a “charge”, or more generally as a statutory security right.

The SCA further emphasised that the section 118(3) security is a charge upon the property and, for the definition of a “charge”, it referred to the decision in *Irwin v Davies*.²¹ Based on a legal dictionary, that court held that a charge on property is security for payment of a debt or performance of an obligation.²² The SCA also quoted the explanation given in *City of Johannesburg v Kaplan NO*:²³

“Any amount due for municipal debts (ie not limited by the aforesaid period of two years) that have not prescribed is secured by the property and, if not paid and an appropriate order of court is obtained, the property may be sold in execution and the proceeds applied in payment of the debts. In such event, the proceeds will be applied to payment of the municipal debts in full. Only after satisfaction of such debts will the remainder, if any, be available for payment of the debt secured by a mortgage bond over the property.”²⁴

The SCA explained that section 118(3), unlike section 118(1), is not an embargo provision, but self-evidently a security provision. According to the court this point was misunderstood by the Municipality in that it did not distinguish between the two remedies available to it. Based on this misconstrued understanding of section 118(3), the Municipality therefore claimed, in addition to its security, an undertaking for payment of the historical

¹⁵ *City of Tshwane Metropolitan Municipality v Mathabathe* 2013 4 SA 319 (SCA) para 9, citing *City of Johannesburg v Kaplan NO* 2006 5 SA 10 (SCA) para 13

¹⁶ *City of Tshwane Metropolitan Municipality v Mathabathe* 2013 4 SA 319 (SCA) para 9, citing *BOE Bank Ltd v City of Tshwane Metropolitan Municipality* 2005 4 SA 336 (SCA) para 7

¹⁷ *City of Tshwane Metropolitan Municipality v Mathabathe* 2013 4 SA 319 (SCA) para 10, citing *BOE Bank Ltd v City of Tshwane Metropolitan Municipality* 2005 4 SA 336 (SCA) para 8

¹⁸ *City of Tshwane Metropolitan Municipality v Mathabathe* 2013 4 SA 319 (SCA) para 10, citing *Stadsraad van Pretoria v Letabakop Farming Operations (Pty) Ltd* 1981 4 SA 911 (T) 917; *BOE Bank Ltd v City of Tshwane Metropolitan Municipality* 2005 4 SA 336 (SCA) para 7

¹⁹ *City of Tshwane Metropolitan Municipality v Mathabathe* 2013 4 SA 319 (SCA) para 10, citing *City of Johannesburg v Kaplan NO* 2006 5 SA 10 (SCA) para 20

²⁰ *City of Tshwane Metropolitan Municipality v Mathabathe* 2013 4 SA 319 (SCA) para 10, citing *City of Johannesburg v Kaplan NO* 2006 5 SA 10 (SCA) para 16

²¹ 1937 CPD 442

²² 447

²³ 2006 5 SA 10 (SCA)

²⁴ Para 26, quoted at *City of Tshwane Metropolitan Municipality v Mathabathe* 2013 4 SA 319 (SCA) para 11

debt. This claim for an undertaking (effectively an additional security) hence had to fail and the SCA dismissed the appeal. Therefore, the Municipality was “plainly wrong” when it asserted that it would “lose its rights” in terms of section 118(3) when transfer is registered.²⁵ This statement by the court is the crux of the matter, since it implies that the charge remains intact and hence that the Municipality will not lose its rights to the property when it is transferred. Therefore, the charge seems to be enforceable against successors in title. But is this conclusion as simple as it seems?

3 Discussion

3.1 Main inference from *Mathabathe*

The apparent implication of *Mathabathe* (although one could argue this to be *obiter*) is that a municipality’s security right under section 118(3) survives a transfer of the property – the charge, if not enforced, is carried over to subsequent owners. As Cloete puts it:

“A purchaser of immovable property, not bought from an insolvent estate, can no longer accept that, on registration of transfer, he or she acquires the property free of any municipal debt.”²⁶

Cloete further explains that this state of affairs creates a problem for financial institutions that grant loans on the security of registered mortgage bonds.²⁷ He is also concerned about what would happen if a municipality only discovers the existence of historical debt after the property has been transferred.²⁸ Therefore, it is important to obtain clarity regarding the exact nature of the municipality’s real security right and to establish distinct rules for the enforcement of this right. Many practitioners might now be uncertain as to the effect of section 118(3) on property transactions and, to play it safe, many probably share Cloete’s assumption. However, in my view the conclusion reached by Cloete – although a logical inference from *Mathabathe* – is, all things considered, not an acceptable interpretation of section 118(3).

3.2 Impact of the *Mitchell* case

Before continuing with a discussion of the interpretation of section 118(3) in view of the *Mathabathe* case, it is necessary to briefly consider the implications of the subsequent unreported high court case of *Perregine Joseph Mitchell v City of Tshwane Metropolitan Municipal Authority*²⁹ (“*Mitchell*”). Regarding the nature of the section 118(3) charge, the court confirmed that it is “a real right of security created by statute in favour of the municipality”.³⁰ The court moreover stated that there is, generally speaking, no reason why transfer in the normal course of business should terminate the real right while the

²⁵ *City of Tshwane Metropolitan Municipality v Mathabathe* 2013 4 SA 319 (SCA) para 12

²⁶ B Cloete “Clearance Certificates: Does the Municipality’s Lien Survive the Transfer?” (2013) 534 *De Rebus* 46 46

²⁷ 46

²⁸ 47

²⁹ NGP 08-09-2014 case no 50816/14

³⁰ Para 9

principal debt is still outstanding.³¹ However, the court realised that “there is more to this than meets the eye”.³² With reliance on Voet,³³ the court held that, although the point of departure is that immovable property is transferred subject to all real burdens (such as real security rights), an exception in this regard is when the property is sold in execution, since the new owner receives a so-called “clean title”.³⁴ Yet, although the security right falls away, this does not impact the personal obligation that remains on the previous owner to pay the outstanding debt.³⁵

Therefore, the court’s conclusion was that, at least when it comes to sales in execution, the section 118(3) charge will not survive transfer of the land, despite the contrary conclusion that could be drawn from the SCA’s comments in *Mathabathe*. However, it is important to appreciate that, even if the *ratio* and conclusion reached in *Mitchell* on this point are correct,³⁶ it only applies to sales in execution and not to normal sales. In the discussion below, I express my agreement with the prospect that the section 118(3) charge does not survive transfer of the land, but I rely on different reasoning, which can apply to both sales in execution and normal sales. The *Mitchell* case (decided by the high court) does not overrule and probably will not be enough to resolve the uncertainties caused by the SCA in *Mathabathe*. Consequently, one can expect that the SCA itself – and perhaps even the Constitutional Court – will be called upon to clarify this matter in due course.

3 3 Interpretation of section 118(3)

The fact that section 118(3) describes the municipal debt as a “charge upon the property” is important because it reveals the intended legal nature of the preference – at least on face value. In this regard it seems like the charge is not enforceable against the owner in his personal capacity, but rather in his capacity as owner of the property to which the debt relates. Because the debt constitutes a charge upon the land, it is of a real nature; it grants the municipality a right *in rem* and accordingly it is enforceable against successors in title. The Act classifies the municipal debt as serving the property itself and not the owner or occupier. Therefore, it seems correct that a “charge upon the property” is enforceable against whoever is the owner of the property, notwithstanding that a previous owner or occupier might have incurred the debt. Of course, the “charge upon the property” is irrespective of any personal claims that the municipality might have against previous owners or other occupiers, but the municipality obviously has a better chance of recouping the debts by relying on the charge (which is a real right) than by suing the

³¹ Para 9, quoting from *City of Tshwane Metropolitan Municipality v Mathabathe* 2013 4 SA 319 (SCA) para 12

³² *Perregine Joseph Mitchell v City of Tshwane Metropolitan Municipal Authority* NGP 08-09-2014 case no 50816/14 para 10

³³ Voet 20 1 13

³⁴ *Perregine Joseph Mitchell v City of Tshwane Metropolitan Municipal Authority* NGP 08-09-2014 case no 50816/14 paras 12-14; and also the other sources cited there

³⁵ Para 15

³⁶ For instance, it is not clear whether Voet 20 1 13 (referring to hypothec, hence mortgage) can without more apply to a security right such as the *sui generis* charge created in s 118(3) of the Act

previous owner based on a personal claim. It appears that the only recourse for the new owner, if he is held liable, may be to sue the previous owner based on unjustified enrichment, but this will mostly not be a realistic solution and, even if possible, the existence of such a remedy does not in itself justify the alleged wide interpretation of section 118(3). Therefore, the interpretation that the “charge” stays with the land despite being sold and transferred is something that needs re-consideration, because the consequences could be too inhibiting for property owners and mortgagees.

Although there is a general principle that limited real rights are enforceable against successors in title, it is actually not the normal course of events in the law of real security. For example, it is usually intended that a mortgage bond should be cancelled when the property is sold and that the claim of the mortgagee (and other right holders) must be satisfied from the proceeds of the sale. This is trite practice and, in fact, it is not possible to transfer immovable property without cancelling the mortgage bond.³⁷ Therefore, it would be strange if there were widespread occurrences of unpublicised charges upon property that survive transfers of the land, so that subsequent owners might be held liable for the debt.³⁸

Another normal feature of conventional real security rights is the principle that the burden on the property is publicised, in the case of land, through registration. This is not the case with section 118(3), since the Act provides no way to afford publicity to the municipality’s charge.³⁹ Consequently, the disputed wide interpretation of section 118(3) does not fit into the system of real security rights very well, since it contradicts not only the publicity principle but also the normal expectations with regard to the operation of real security rights over land. This notwithstanding, a literal reading of the section could lead to a conclusion that the charge follows the property regardless of what the consequences might be.

It is, however, argued that it could never have been the legislature’s intention to grant a municipality a real security right, the enforcement of which could be postponed until any arbitrary time in future. The strongest indication of this is the rule that the charge enjoys a security in preference to the rights of a mortgagee. Therefore, when land is sold and transferred in the normal course of events or through a sale in execution, the municipality’s claim must be satisfied in full before a mortgagee may receive payment.⁴⁰ It would not make sense to violate this order of preference by paying the mortgagee only and thus to allow the municipality’s charge to remain “upon the property” until

³⁷ S 56(1) of the Deeds Registries Act; PJ Badenhorst, JM Pienaar & H Mostert *Silberberg and Schoeman’s The Law of Property* 5 ed (2006) 364-365

³⁸ Although an enrichment lien might have this effect as well, this is controversial in itself and in any event might be more justifiable because of the value that the lien holder added to the land in question and because his physical possession/occupation creates some publicity

³⁹ Compare s 31 of the Land and Agricultural Development Bank Act 15 of 2002, which also entails a statutory “charge” upon land, but in that case a form of publicity is provided by means of a note that the registrar must make against the records of the land in question. However, it is otherwise not uncommon for statutory security rights to be vested without fulfilment of the publicity principle

⁴⁰ In the case under discussion this was clearly also the municipality’s expectation – hence its insistence on an undertaking that the debts would be paid from the proceeds of the sale before the mortgagee is paid

such time in future when the municipality wishes to enforce it or discovers old unpaid debts. In effect, the municipality's charge logically precludes any payment to a mortgagee before the charge has been satisfied.

Therefore, reading the section as a whole, there is – in my view – no option but for the municipality's debt to be settled before the mortgagee is paid.⁴¹ Practically, nothing else makes sense. A secured creditor cannot forego its place in the order of preference, only to resume it again at some arbitrary later stage – even if the creditor is the state. Section 118(3) should have incorporated a distinct rule regarding the satisfaction of the charge at the time that the property is alienated and the proceeds are distributed. Although this is not expressly stipulated in the section, one could read it in as a logical implication, especially if the municipality's secured position in preference to mortgagees is to have practical effect.

A comparable interpretation of section 118(3) is supported by Gladwin, who suggests that the municipality's security right is only intact until the property is transferred.⁴² The implication of this argument is that, if the municipality does not receive (or claim) payment in terms of section 118(3) when the property is realised, it loses its "charge" and cannot rely on it at a later stage against subsequent owners and mortgagees.

3 4 Constitutional perspective

Another aspect of section 118(3) that one must consider is the important principle that the effects of statutory security rights must comply with the Constitution of the Republic of South Africa, 1996 ("the Constitution"). In recent years statutory security rights and execution measures have been the subject of quite a number of key Constitutional Court judgments.⁴³ Except for brief remarks, a full analysis of these cases and how the principles developed in them could apply to the carry-over of section 118(3)'s "charge" to subsequent owners and mortgagees falls outside the scope of this contribution. However, if an instance should come up where an owner of land is held liable (by virtue of the charge upon his land) for the municipal debts incurred by a previous owner, the current owner might want to challenge the constitutionality of the application of the "charge" to him. The same goes for a subsequent mortgagee

⁴¹ This is also why the court held that no undertaking for the payment of the debts was necessary in the present case, since s 118(3) guarantees payment

⁴² C Gladwin "Historical Municipal Debt" (23-01-2014) *GhostDigest* <<http://www.ghostdigest.co.za/articles/historical-municipal-debt/54489>> (accessed 15-09-2014)

⁴³ See for example *First National Bank of SA Ltd t/a Wesbank v Commissioner, South African Revenue Service*; *First National Bank of SA Ltd t/a Wesbank v Minister of Finance* 2002 4 SA 768 (CC) (s 114 of the Customs and Excise Act 91 of 1964); *Mkontwana v Nelson Mandela Metropolitan Municipality*; *Bissett v Buffalo City Municipality*; *Transfer Rights Action Campaign v Member of the Executive Council for Local Government and Housing, Gauteng* 2005 1 SA 530 (CC) (s 118(1) of the LGMS Act); *Chief Lesapo v North West Agricultural Bank* 2000 1 SA 409 (CC) (s 38(2) of the North West Agricultural Bank Act 14 of 1981); *First National Bank of South Africa Ltd v Land and Agricultural Bank of South Africa*; *Sheard v Land and Agricultural Bank of South Africa* 2000 3 SA 626 (CC) (s 34 of the Land Bank Act 13 of 1944, in the meantime replaced with Act 15 of 2002)

whose claim, by virtue of this interpretation of section 118(3), is ranked below the claim of a municipality for debts owed by a previous owner.⁴⁴

Section 25(1) of the Constitution provides that no law (including the LGMS Act) may permit arbitrary deprivation of property.⁴⁵ Without going into any details, the decisions in both *First National Bank of SA Ltd t/a Wesbank v Commissioner, South African Revenue Service; First National Bank of SA Ltd t/a Wesbank v Minister of Finance*⁴⁶ (“FNB”) and *Mkontwana v Nelson Mandela Metropolitan Municipality; Bissett v Buffalo City Municipality; Transfer Rights Action Campaign v Member of the Executive Council for Local Government and Housing, Gauteng*⁴⁷ (“Mkontwana”) are authority for the proposition that statutory security rights involve deprivation of property. The cases show that statutory security rights generally are constitutionally acceptable ways for state institutions to enforce payment of their debts. However, it is also clear that there may be situations where the burden imposed on the property goes too far or has an effect on the owner that is disproportionate to the purpose of the security right. Therefore it is not a given that section 118(3) should be allowed to have an unqualified effect on successors in title and subsequent mortgagees. As was found in *FNB*,⁴⁸ a deprivation of property will be arbitrary if the law in question provides insufficient reason for the deprivation. As the outcome of *FNB* also shows, a very good reason will probably have to be provided if the deprivation has the effect of holding someone other than the actual debtor liable for the payment of a debt to the state. In *Mkontwana*⁴⁹ the court held that it is justifiable for an owner to be held liable for municipal debts incurred by occupiers of his land (even unlawful ones). The explanation for this decision, put briefly, was that owners have a responsibility to ensure that people do not unlawfully occupy their land and incur debts; and furthermore that the debts benefit the land itself, rendering owners liable even though they did not personally make use of the services for which the debts were incurred. The reasoning of the case has been criticised⁵⁰ but even if one accepts it for present purposes, the same reasoning cannot be applied to a subsequent owner who has absolutely no control over the occupation of the land or over the debts that were run up with regard to municipal services before he became owner.

To argue that the purchaser should have checked whether there were outstanding historical debts, or that he should have provided for this eventually in the contract of sale, is not convincing either. For example, information

⁴⁴ Compare for example the analysis by L du Plessis “Observations on the (Un-)constitutionality of Section 118(3) of the Local Government: Municipal Systems Act 32 of 2000” (2006) 17 *Stell LR* 505 520-526

⁴⁵ In general, see AJ van der Walt *Constitutional Property Law* 3 ed (2011) ch 4

⁴⁶ 2002 4 SA 768 (CC), particularly paras 57-60

⁴⁷ 2005 1 SA 530 (CC), particularly paras 31-33

⁴⁸ *First National Bank of SA Ltd t/a Wesbank v Commissioner, South African Revenue Service; First National Bank of SA Ltd t/a Wesbank v Minister of Finance* 2002 4 SA 768 (CC) para 100

⁴⁹ *Mkontwana v Nelson Mandela Metropolitan Municipality; Bissett v Buffalo City Municipality; Transfer Rights Action Campaign v Member of the Executive Council for Local Government and Housing, Gauteng* 2005 1 SA 530 (CC) paras 44-54

⁵⁰ See especially Van der Walt (2005) *SALJ*; and also C Gladwin *The Constitutionality of Municipal Policy Regarding the Opening of Municipal Service Accounts with Specific Reference to Mkontwana v Nelson Mandela Metropolitan Municipality* 2005 1 SA 530 (CC) LLM dissertation Unisa (2013)

regarding outstanding municipal debts is not freely available to the public so as to create some sort of publicity that purchasers can rely on. Moreover, why should the responsibility to ensure that prior debts are not charged to a subsequent owner be on him? An argument that a purchaser should exercise a degree of due diligence is perhaps not without merit, but it is not strong enough justification for the imposition of a real burden on his property.

What is more, due to the operation of section 118(1), any charge in terms of section 118(3) will in almost all instances only be a charge with regard to debts older than the two years before the property has been sold, since the two-year debt would have had to be paid before the property was sold. This factor means that the charge (for historical debts) is even further removed from the new owner's ability to control the debt or enjoy the services, because it relates to debts and services of more than two years before he acquired the land. Similar reasoning applies to a subsequent mortgagee, who obviously has no control over or knowledge of the debts incurred by previous owners, and who enjoys no (or minimal) benefits from municipal debts incurred years before.⁵¹

Consequently, section 118 must be interpreted and applied in a way that does not authorise arbitrary deprivation of property. A charge upon one's property imposed by legislation so as to secure a debt that one did not incur is certainly suspect and must be scrutinised in view of section 25. From a subsequent mortgagee's perspective the matter is just as serious, if not more so. The fact that the municipality's charge has priority over a current mortgagee's claim (despite the fact that the mortgage might have been registered before the charge came into being) is already an extraordinary arrangement that raises questions of its own.⁵² But, the doubts one can raise are even more serious if the charge enjoys priority over a subsequent mortgagee's rights, for example, in a sale in execution. Consequently, the wide application of section 118(3) cannot be accepted without more, because – if interpreted to be enforceable against successors in title – it clearly has the potential to interfere unjustifiably with the property rights of subsequent owners and bondholders.

Although the state is permitted to use legislation to create exceptional rights of preference for the enforcement of debts, it is important to consider that such measures are subject to constitutional control. As with all areas of state regulation, the impact of these measures can be tested for constitutional compliance. A more comprehensive analysis than the comments I made here can probably be undertaken,⁵³ but the basic point is that the charge provided in section 118(3) must be treated with care because, taken to its logical extreme, the results could be unacceptable.

It can be mentioned in passing that, as the conclusion of Du Plessis's article suggests,⁵⁴ it may also be time to revisit the current approach of section

⁵¹ See Du Plessis (2006) *Stell LR* 520-526

⁵² See for example M Kelly-Louw "Municipalities Versus Bondholders – Who Won?" (2006) 20 *Speculum Juris* 160; M Kelly-Louw "Municipal Debts – Are They Killing Mortgage Bonds?" (2005) 13 *Juta's Business Law* 121; M Kelly-Louw "The Preferential Right of the Local Government or the Body Corporate Above that of the Mortgage Bondholder during Insolvency Proceedings" (2004) 2 *Speculum Juris* 169

⁵³ For example, with reference to the type of arguments made by Du Plessis (2006) *Stell LR* 520-526

⁵⁴ 529-530

118(3)'s charge being unlimited in time when it comes to the debt that it secures. If section 118(3) – like section 118(1) – was made subject to a two-year limit, the question that *Mathabathe* has created would not have been an issue. If the charge only secured the payment of the “two-year debt” in the event of a sale in execution of the property, there would have been no question of the charge surviving a transfer of the property. The reason for this is that, in the event of normal sales, the two year debt would have been paid before the clearance certificate was issued and there would be no charge upon the property when the new owner receives transfer. However, because the topic of this note is not the time-limit issue as such, nothing further needs to be said in this regard, except that it is certainly a factor to keep in mind when a broader analysis of section 118 is undertaken.

4 Conclusion

Read as a whole, section 118(1) and (3) should, in my view, be interpreted as follows. This interpretation makes practical sense and avoids the constitutional difficulties pointed out above: In terms of section 118(1), if any debts for the previous two years are outstanding (the “two-year debt”), the property cannot be transferred to a purchaser. Conversely, if the two-year debt is paid, the property can be transferred. Section 118(3) should then preferably kick in at this stage when the property is sold and transferred, and it is at this time when the municipality should enforce its charge as security for payment of the remaining (historical or pre-two year) debt.

The claim that the municipality has in preference to the mortgagee should be settled and paid from the proceeds of the sale at the time of transfer, or alternative security should be given to the municipality for full payment of the historical debt from the proceeds of the sale.⁵⁵ In other words, the municipality must rely on its charge in some way or another at or before the point of transfer (and at no stage after this). Practically speaking it would be the conveyancer's duty to ensure that the municipality is paid before the mortgage debt is settled. It may even be that, if the conveyancer fails to attend to the municipality's claim, he might face liability.⁵⁶

To interpret section 118(3) so that the municipality can simply elect to not enforce its claim before or at the point of transfer, but rather at some uncertain, later stage and against a subsequent owner and in priority to a subsequent mortgagee, would contravene any sense of rationality or justice. In my view, it cannot be interpreted to give the municipality the power to postpone enforcement of the historical debt until some arbitrary point in time when it deems fit. Statutory security rights (and related powers) granted to the state must, because of the extraordinary burdens they impose, be interpreted strictly – especially if the principle of publicity is bypassed. Another interpretation that indeed allows the municipality to enjoy a charge against a subsequent

⁵⁵ The seller can also give the municipality an acknowledgment of debt and make arrangements regarding payment of the historical debt, in which case the municipality is necessarily waiving its right to rely on the property as security for the debt

⁵⁶ See H Jackson “Not Much Comfort for Conveyancers” (2013) 13 *Without Prejudice* 45

owner or mortgagee, which it can impose when it wants to, would in all likelihood be unconstitutional. However, as suggested here, it is possible to interpret the section to avoid such unconstitutionality.

SUMMARY

The Supreme Court of Appeal's decision in *City of Tshwane Metropolitan Municipality v Mathabathe* 2013 4 SA 319 (SCA) may have some implications for the interpretation of section 118(3) of the Local Government: Municipal Systems Act 32 of 2000. This subsection provides that municipal debts constitute a "charge" upon the immovable property to which the debts relate. In other words, municipalities are afforded a type of statutory real security right that secures payment of the debt. A potential problem with the decision is that one could read it to mean that the municipality's security right is enforceable against successors in title, hence that it continues to exist even after the property has been transferred to a new owner. This prospect is controversial because it could have the effect that a later owner is held liable for the municipal debts incurred by a previous owner. Just as problematic, the municipality's charge would enjoy preference above the claims of mortgagees. This contribution discusses the case and briefly considers whether the supposed interpretation is sustainable. A suggestion is made regarding the way in which section 118(3) should be interpreted so that it makes practical sense, has fair consequences and is in line with section 25(1) of the Constitution of the Republic of South Africa, 1996. The conclusion is that the municipality's charge is not enforceable against successors in title, but that it must be enforced before or at transfer of the property.