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REAL ESTATE ALERT

IN THIS **ISSUE**

HISTORICAL DEBT AND CLEARANCE CERTIFICATES: ARE WE ALL (UN)CLEAR?

Does s118(3) of the Local Government: Municipal Systems Act survive the transfer of property?

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The recent case of City of Tshwane Metropolitan Municipality v PJ Mitchell [2015] ZASCA 1 (29 January 2016) (Mitchell) has been the fodder for discussion among legal minds and the general public alike as to whether or not the rights of the local municipality, more specifically with regards to s118(3) of the Local Government: Municipal Systems Act, No 32 of 2000 (Act) have been limited.

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Does s118(3) of the Local Government: Municipal Systems Act survive the transfer of property?

The recent case of City of Tshwane Metropolitan Municipality v PJ Mitchell [2015] ZASCA 1 (29 January 2016) (Mitchell) has been the fodder for discussion among legal minds and the general public alike as to whether or not the rights of the local municipality, more specifically with regards to s118(3) of the Local Government: Municipal Systems Act, No 32 of 2000 (Act) have been limited.

The Act provides municipalities with two distinct remedies to claim monies in respect of arrear rates, namely:

- the municipality could either prohibit the transfer of property altogether by not issuing a clearance certificate until all debts for the past 24 months have been settled [as per s118(1)];
- or it could submit a claim as a secured and preferred creditor, which claim ranks in priority to that of any bondholder over the property [as per s118(3)].

The municipality's right in terms of s118(3) has been described as a "charge upon the property" in terms of the Act and has commonly been referred to as a lien or tacit hypothec. It is generally accepted that the right over the property by the municipality is unique in nature and cannot truly be compared to the legal concepts of charge, lien or tacit hypothec as commonly understood.

The Mitchell case was first heard in the High Court and subsequently taken on appeal to the Supreme Court of Appeal.

The facts of the matter in summary are that Mr Mitchell purchased fixed property at a sale in execution. When taking transfer of the property, he obtained a rates clearance certificate which was issued in respect of a period of two years prior to the date on which the application for which such a certificate was made. A historical debt of R106 219.75 remained due and outstanding. Mr Mitchell subsequently sold the property to Ms Prinsloo, who before taking transfer, tried to open municipal services accounts. Ms Prinsloo was advised that the municipality would not open an account in her name, until the historical debt was settled. Ms Prinsloo advised the transferring attorneys to stop the transfer process until the historical debt issue was resolved. Mr Mitchell then approached the High Court for relief.

In the High Court

The matter before the court was whether the local municipality could claim the historical debt (ie debt incurred in respect of a property, for a period greater than 24 months preceding the date of application for a rates clearance certificate) from the new owner and his/her successors in title. The property was acquired by Mr Mitchell at a sale in execution and the court, in delivering judgement, ensured that its response was limited to this context. The court held that where a sale in execution has taken place, the local municipality loses its rights in terms of s118(3) of the Act to claim the

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CONTINUED

The consequence of this ruling is that there is no "clean" transfer of title, and purchasers will now have to seek indemnities from sellers in relation to rates payments.

historical debt from anyone other than the previous owner of the property due to the common law principles pertaining to immoveable property subject to a special hypothec. Simply put, s118(3) does not survive transfer where there has been a sale in execution.

In the Supreme Court of Appeal:

The municipality challenged the ruling handed down by the High Court and, in its majority decision, the SCA held that there should not be a distinction drawn between property sold at a sale in execution or in a private sale. According to the majority, the hypothec does survive the transfer (regardless of the originating cause for such transfer) as it is a hypothec created by statute and therefore there is no limitation on its duration. The consequence of this ruling is that the municipality's tacit hypothec survives transfer and that it can perfect its security over the property, should it wish to do so, in order to settle the debt.

How is security perfected:

In order for the municipality to perfect its security, it would have to:

1. Obtain a court order allowing it to attach the property;
2. Sell the property in execution; and
3. Apply the proceeds from the sale to settle any historical debt.

The SCA however further advises that before perfecting its security, the municipality must comply with its own by-laws. In this case, the municipality, (if it were looking to perfect its security) would have had to have shown that:

1. There was no occupier of the property; and
2. The person who has entered into the contract to receive the services:
   - 2.1 cannot be traced; or
   - 2.2 has absconded; or
   - 2.3 is unable to pay; or
   - 2.4 does not exist.

So what does this mean?

1. A municipality's rights in terms of s118(3) does survive transfer, regardless of the reason for the transfer;
2. An owner of property could be responsible for its historical debt. It is important to note that the court did in passing mention that the constitutionality of s118(3) was not in question before the court. The consequence of this ruling is that there is no "clean" transfer of title, and purchasers will now have to seek indemnities from sellers in relation to rates payments. Similarly financial institutions may insist on an "audit" of the rates and taxes in respect of properties they choose to finance; and
3. In order to perfect its security a municipality must first show that it has complied with its by-laws before seeking a court order to attach property.

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