

DISPUTE RESOLUTION AND REAL ESTATE ALERT



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HISTORICAL DEBTS ARE JUST THAT – HISTORICAL!

In the eagerly anticipated judgment of *Jordaan and Others vs City of Tshwane Metropolitan Municipality and Others* [2017] ZACC 31, the Constitutional Court upheld the constitutional validity of s118(3) of the Local Government: Municipal Systems Act, 2000 (Act) but declared that upon transfer of a property, a new owner is not liable for the historical debts of the previous owners arising before transfer from the charge upon the property under s118(3).

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New owners could not be sure of their tenure, despite the municipalities having issued a rates clearance certificate in respect of the transfer, and bondholders (who had financed the new owner) could not be certain that their security would remain intact for very long, if it all.

The municipalities conceded that nothing prevented them from claiming payment of the historical debt from the party who had incurred such debt.



In the eagerly anticipated judgment of *Jordaan and Others vs City of Tshwane Metropolitan Municipality and Others* [2017] ZACC 31, the Constitutional Court upheld the constitutional validity of s118(3) of the Local Government: Municipal Systems Act, 2000 (Act) but declared that upon transfer of a property, a new owner is not liable for the historical debts of the previous owners arising before transfer from the charge upon the property under s118(3).

Section 118(3) created for the benefit of municipalities, "a charge" in respect of properties. The municipalities argued that this "charge", which ranked in priority to any bondholder rights over the property, survived transfer of ownership, thus allowing municipalities to look to the new owner for compensation for debt that had been incurred by the prior owner. This interpretation by the municipalities created uncertainty in the marketplace as it meant that new owners could not be sure of their tenure, despite the municipalities having issued a rates clearance certificate in respect of the transfer, and bondholders (who had financed the new owner) could not be certain that their security would remain intact for very long, if it all.

The High Court in Pretoria ruled that the "charge on the property" created by s118(3) was constitutionally invalid to the extent that the security provision survives transfer of ownership into the name of the new owner. The applicants (*Jordaan et al*) sought confirmation of the finding of invalidity, and the municipalities appealed against the decision of the High Court's order of invalidity in the Constitutional Court.

TUHF Limited, a social housing organisation, and the Banking Association South Africa (BASA), which has 32 member banks,

including the largest banks in South Africa, joined the proceedings as "friends of the court" and both associated themselves with the applicants in challenging the municipalities' interpretation of s118(3). TUHF advanced arguments that showed municipalities had distinct remedies at their disposal to reclaim historical debts, while BASA argued that the section's arbitrary deprivation of rights extended to the new bondholder as well and should be declared unconstitutional.

The municipalities argued that in order to meet their constitutional duties of service delivery, they needed "extra-ordinary" debt collecting measures. The municipalities, however, conceded that nothing prevented them from claiming payment of the historical debt from the party who had incurred such debt and that they further had at their disposal the ability to interdict a transfer until such time that the debts were settled by the old owner.

The Constitutional Court delivered a unanimous decision, and in doing so confirmed that the interpretation and application of the legislation, and the development and application of the common law falls squarely within its jurisdiction. It therefore put to rest the argument that this matter should not be heard before the Constitutional Court.

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The judgment provides landowners and finance houses with the comfort of knowing that historical debts will remain squarely in the past.



In handing down its judgment, the Constitutional Court focused squarely on the following question: whether the charge created by s118 (3) survives transfer, so as to burden succeeding owners with the prior owner's historical debt?

In unpacking what was meant by "charge", the Court arrived at the conclusion that it allows municipalities to bypass some debt collection enforcement procedures, thus providing the municipalities with preference and allowing for an efficient execution of the property, subject to a court order.

The Court further explained that a real right in the property of another is a right which has long been recognised by our law and by definition, includes a "charge". However, the transferability of this real right is subject to the condition that this real right must be publically known and acknowledged. Municipalities are not required to note their charges against a property at the Deeds Registry Office, nor is there any accompanying act of formality to give effect to transfer of this charge from the present owner to the new owner. The charge therefore cannot be inferred or transferred to another and is only enforceable against the party responsible for incurring such debt. The fact that the municipality's real right is contained in the Act does not fulfil the requirement of "public knowledge" as the value of the debt remains unknown.

The Court emphasised that municipalities have an obligation to create a culture of payment and to take appropriate steps to collect outstanding monies, including

its right to attach the property where the property is still registered in the name of the owner that incurred such debt. The municipality's prior ranking right to bondholders in this situation was not contested. Coupled with this is the practical requirement that all conveyancers are obliged to notify municipalities of every transfer, thus ensuring that municipalities have every opportunity to claim the outstanding debt from the existing owner, prior to transfer. How the new owner acquires transfer of the property (ie through a sale in execution, private treaty or any other means) was of little consequence to the Court in its interpretation of s118(3).

Finally, the Bill of Rights prevents the "arbitrary deprivation of property". Deprivation is said to have taken place where there is a "substantial" interference with a property right. In this instance, the new owner could have the property attached so as to settle the debts of the old owner. The lack of connection between the new owner and the debts incurred on the property, being the epitome of arbitrariness, is plain to see. To therefore allow the charge to survive post transfer would clearly arbitrarily deprive both the new owner and its bondholder of any substantial rights in the property.

The judgment therefore reaffirms the roles and responsibilities of municipalities in relation to the collection of debt and provides landowners and finance houses with the comfort of knowing that historical debts will remain squarely in the past.

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