

Can a new owner be liable for old owner's municipal debts?

 By [Chantelle Gladwin](#)

10 Feb 2016

A judgement by the Supreme Court of Appeal in *City of Tshwane Metropolitan Municipality v PJ Mitchell*, on 29 January 2016, has opened the way for municipalities to take legal action against a present owner of a property for debts owed to it by former owners.



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Findings

The Supreme Court of Appeal held that the hypothec (sometimes referred to as a lien) that exists in favour of the local municipality, to secure amounts owing by the owner of a property to that municipality for rates and services, is not extinguished by transfer of the property from the owner who incurred the debts to a third party. This is the case regardless of whether the sale that led to the transfer took place as a sale in execution, or in any other fashion. This finding was based on the court's interpretation of section 118(3) of the Local Government: Municipal Systems Act 32 of 2000, as interpreted against the backdrop of the South African common law relating to hypothecs.

Implications for property owners

1. A municipality can, if it chooses, take legal action against the present owner of a property, not only for any amounts owing by that owner to the municipality in respect of the property, but for any other amounts owing by any prior owner of that property to the municipality in connection with the property as well, provided that those amounts have not prescribed (become unclaimable in law as a result of the passage of time).

2. The legal action that can be taken against the new owner can range from suing the new owner for the old owner's debts in court, and attaching and selling the property itself (which according to section 118(3) stands as security for the debts owed to the municipality, regardless of who owns it and even if the debts were incurred by a person other than the present owner). The municipality would then take the proceeds of the sale of the property to settle whatever is owing, and anything remaining after that would then be paid to the bondholder (if there is one), and thereafter to the owner.
3. This applies even if the amounts that the municipality claims that the prior owner is liable for, were not levied to the prior owner's account at the date of transfer. For example, a municipality might discover some time (months or years) after transfer that it accidentally under billed the prior owner for electricity or for rates (or for any other service). When it discovers this, it can then add the applicable charges to the old owner's account and send the corrected bill to the prior owner, or it can send the corrected bill to the new owner. If the old owner does not pay, the municipality can sue the old owner. However, if the new owner does not pay, the municipality can apply to court to attach the new owner's property and to sell it to satisfy the old owner's debts, because the property serves as security under section 118(3) for all debts owed to the municipality in connection with the property, regardless of who incurred the debt.
4. If this were to happen, the municipality could hold the new owner liable for (and attach and sell the property for) the debts of the old owner (or owners, as there is no limit to how many prior owners might not have paid their debts), for debts incurred as far back as 30 years ago (in respect of rates, refuse and sewer) and 3 years ago (in respect of electricity and water).
5. If a new owner was presented with an invoice for charges incurred by prior owners, the new owner would be able to raise any defences to that debt that the old owner would have been able to – however, how is the new owner supposed to know what those defences might possibly be? The new owner would not have been privy to the goings on of the old owner, and will (realistically) never be able to ascertain what defences the old owner might have raised to that debt. The new owner would have absolutely no records of how the old owner conducted the account. Imagine what would happen if it transpired that the old owner disputed R2 million of charges on the basis that the meter that those charges were allegedly incurred in relation to, never existed at the property. There would be no "proof" that the meter was never at the property, other than the actual physical absence of the meter at the property, but a site inspection done now would not assist because the period in respect of which the dispute pertained to, was several years ago. The same problem exists in relation to any dispute pertaining to broken meters, and meters that are supplying incorrect properties, as well as to illegal electricity and water connections, and meter tampering.

Imagine further what would happen if the prior owner were disputing rates charged to him based on an incorrect valuation, and five or six years after selling the property, the result of a review of the property valuation (that applied to the prior roll) was that it was undervalued by several million. This would result in the new owner receiving a rates bill of several hundred thousand rand, for rates that should have been billed to the old owner before transfer. There is very little (if anything) that the new owner can do, other than contact the old owner (who may be dead, have left the country, have ceased to exist if a juristic person, have not kept any records, or simply have destroyed records older than a few years) for assistance in either of the two examples given above.

6. Furthermore, depending on how long ago the charges were incurred, the municipality may not have any records relating to the account at all, or its records may be inadequate, or incorrect. There is virtually no way whatsoever that any new owner would ever be able to disprove the municipality's claim that amounts were owing by the old owner in these circumstances.

7. Basically, no property owner can ever sleep soundly again, as no matter how much homework you do before purchasing a property, you can never be 100% sure that someone else's debt will not appear out of the woodwork to haunt you.

Implications for banks (and other bondholders)

1. A municipality's right to claim the proceeds of the sale of a property from the new owner, trumps the bank's right to claim what it is owed in terms of a mortgage bond. This means that no bank can ever really assess the risk of lending money to a purchaser properly – because it cannot realistically assess the risk that the purchaser will be called upon to settle an old owner's debts. This means that (unless something radical changes) many fewer bonds will likely be granted. This will, in turn, impact on the property market as a whole (as sales will drop) and the economy as a whole (as if the situation weren't bad enough already).

Implications for occupants of properties affected by section 118(3)

1. In many municipal jurisdictions, municipalities have by-laws that enable them to hold tenants and other occupiers of properties liable for charges billed to (and not paid) by the owners of those properties. This means that even tenants, who have never been the owners of the property, may be held liable for debts incurred (and not paid) by prior owners of the property that they reside in. Again, there is no way for a tenant to "vette" a prospective property to ensure that this will not happen, because the passage of time, the failure of the human memory, and the destruction of records usually renders any investigation impossible (or at the very least, largely inaccurate) after a period of 5 – 6 years.

Analysis of the implications

The implications are catastrophic for all stakeholders – owners, bondholders, tenants, professionals in the property industry, and generally anyone relying on the South African economy to make a living.

The only upside to this judgment is that the court has declared that municipalities have greater security for outstanding debts, which should (in theory) lead to greater collections by these entities, better service delivery, and better performance overall by these municipalities. In the author's opinion it is doubtful that this will occur.

Seeing that municipalities have had this security right for many years (the present case not conferring this right, but merely confirming its existence and scope) but exercise it only very rarely, and seeing that (in my opinion, which is supported by the present judgment and other Constitutional Court judgments) municipalities are still under an obligation to first try and claim debt from the person who incurred it, the effectiveness of this ruling as a debt collection mechanism will be far less beneficial to the fiscus than anticipated, and the harm and prejudice caused by its operation will, by far, outweigh the marginal benefit obtained.

Short-term solution?

There is not one – property owners, bondholders, and tenants needs to be aware of the problem, and do as thorough an investigation as they can into the chances of any old debt popping up, and investigate the possibility of taking out insurance to cover the risk. Purchasers need to insist that sellers pay all amounts owing to the municipality when passing transfer (which most of them do already). However, none of these actions is guaranteed to protect a person from being held liable for another person's debt, and even losing their property to satisfy that debt.

Where to from here?

There is a possibility that the matter will be referred to the Constitutional Court, which may still overturn the judgment on constitutional grounds (which were not considered by the Supreme Court of Appeal). This is pretty much the only hope for the industry. I for one hope that this happens urgently, and if given the opportunity I will be the first to apply to the Constitutional Court to be admitted to the proceedings as an amicus (a "friend of the court") to put forward my submissions

on why the judgment should be overturned.

ABOUT CHANTELLE GLADWIN

Chantelle Gladwin (@chantellegladwi) is a partner at Schindlers Attorneys specialising in all areas of commercial and residential property practice and litigation, including sectional title body corporate management, eviction, general property management and property-owning enterprise management, as well as corporate restructurings and corporate taxations matters.

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