WERKSMANS
ATTORNEYS

REAL ESTATE

Obligation of liquidators to pay rates, taxes and utilities in order to give effect to the transfer of immovable property

3 February 2021 *8 min read*

by Vivienne Hosiosky, Director and Khathu Neluheni, Senior Associate

The COVID 19 pandemic has had a devastating effect on the South African economy not least of all, the residential, commercial and industrial property markets. Property owning companies and individuals are falling victim to loss of income and there has been an upsurge in liquidations and insolvencies as a result. Property auctions have become the order of the day in an attempt to realise some return and minimise losses to creditors.

Upon the liquidation of a juristic person or the sequestration of a natural person, a question that arose recently was, as to how much the relevant municipality is entitled to claim from the insolvent estate for rates, taxes and utilities owing on a property, in order to issue and to provide the conveyancers attending to the transfer of the property, with the required rates clearance certificate ("**Certificate**").

As a general rule, section 118(1) of the Local Government: Municipal Systems Act No 32 of 2000 ("**Municipal Systems Act**") provides that the Registrar of Deeds may not register the transfer of immovable property except on the production of a prescribed certificate issued by the relevant municipality, certifying all amounts that became due in connection with that property during the two years preceding the date of application for the certificate, have been fully paid. These amounts relate to municipal service fees, surcharges on fees, property rates and other municipal taxes, levies and duties (hereinafter collectively referred to as, "**Municipal Charges**").

In addition, section 118(2) of the Municipal Systems Act provides that in the case of the transfer of property by a trustee of an insolvent estate, the provisions of section 118 of the Municipal Systems Act shall be subject to section 89 of the Insolvency Act No 24 of 1936 ("**Insolvency Act**"). Although section 118(2) of the Municipal Systems Act refers to the transfer of property by a "trustee of an insolvent estate", the Supreme Court of Appeal in the *City of Johannesburg v Kaplan No and Another* 2006 (5) SA 10 (SCA) (hereinafter referred to as, the "**Kaplan Judgment**") found that a liquidator of a company or a close corporation are equally as liable to pay the charges referred to in section 118(1) as natural persons are. In this regard, the municipality's need for protection is no more or less in one case than in the other. Accordingly, the court held that there is no rational ground for applying section 89 of the Insolvency Act to section 118 of the Municipal Systems Act in the context of the sequestration of an individual, but excluding it from the liquidation of a juristic person and to do so would "lead to an absurdity so glaring that the legislature could not have contemplated it".

Section 89(1) of the Insolvency Act provides, *inter alia*, that all "taxes" form part of the costs of realisation. For purposes of interpreting this section, "tax" is defined in section 89(5) of the Insolvency Act as meaning "*any amount payable periodically in respect of that property to the State or for the benefit of a provincial administration or to a body established by or under the authority of any law in discharge of a liability to make such periodical payments, if that liability is an incident of the ownership of that property*". In this regard, any "tax" which is or will become due on the immovable property being sold in respect of any period not exceeding two years immediately preceding the date of the sequestration of the estate in question and in respect of the period from that date to the date of the transfer of that property by the trustee of that estate, with any interest or penalty which may be due on the said tax in respect of any such period, shall form part of the costs of realisation.

The two-year period provided for in section 89(1) of the Insolvency Act differs from that provided for in section 118(1) of the Municipal Systems Act in that (i) the former relates to the relevant municipality's secured claim for the payment of "taxes" for a **period of two years prior to the date of liquidation**; and (ii) the latter relates to the payment of Municipal Charges for **a period of two years prior to the**

submission of an application for a Certificate required to be lodged in the deeds office as part of the conveyancing process giving effect to the transfer of immovable property.

The Supreme Court of Appeal in the Kaplan Judgment found that once a debtor has been liquidated, the position is as follows, provided the municipal debts are "taxes" as defined in the Insolvency Act:

(i) no property may be transferred unless the Certificate certifies full payment of municipal debts that have become due during a period of two years before the date of application for the Certificate;
(ii) the preference accorded by section 118(3) of the Municipal Systems Act in favour of the municipality over that of a holder of a mortgage bond is limited to claims which fell due during the period laid down in section 89(1) of the Insolvency Act (i.e. two years prior to the date of liquidation up to the date of transfer);
(iii) interest charged on the secured claim of the municipality is secured as if it were part of the municipality's claim.

In the matter of *Barnard NO v Regspersoon van Aminie en 'n Ander* 2001 (3) SA 973 (SCA) (hereinafter referred to as, the "**Barnard Judgment**"), the court held, *inter alia*, the starting point is to determine whether the municipality's claim is for a "tax" in its ordinary sense and, only if the answer is positive, to apply the restrictive provisions of section 89 of the Insolvency Act. In this regard, the court stated it was of the view that property rates are "taxes" within the definition provided for in the Insolvency Act, and service charges which are a *quid pro quo* for a measured consumption are probably not. This principle should be used as a guideline and consideration should also be given to the applicable by-laws which govern the relevant municipality.

Consumption of water and electricity

Although utility charges fall within the definition of Municipal Charges as it relates to the provision of services by the municipality, the consumption thereof falls outside of the definition of "taxes" as provided for in the Insolvency Act as stated in the Barnard Judgment. Accordingly, it will be necessary to comply with the provisions of section 118 of the Municipal Systems Act in respect of all service charges levied by a municipality relative to the provision of water and electricity, but excluding the **actual** consumption thereof.

Section 10(1) as read together with section 11(d) of the Prescription Act No 68 of 1969 ("**Prescription Act**") provides, *inter alia*, a debt shall be extinguished by prescription after the lapse of a period of three years. In order to determine whether such a period has lapsed, consideration must be made as to when the debt became due for purposes of calculating when prescription started running. In this regard, section 12 of the Prescription Act provides that:

(i) prescription shall commence to run as soon as the debt is due;
(ii) if the debtor willfully prevents the creditor from coming to know of the existence of the debt, prescription shall not commence to run until the creditor becomes aware of the existence of the debt; and
(iii) a debt shall not be deemed to be due until the creditor has knowledge of the identity of the debtor and of the facts from which the debt arises, provided a creditor shall be deemed to have such knowledge if he could have acquired it by exercising reasonable care.

In the matter of *Argent Industrial Investment (Pty) Ltd v Ekurhuleni Metropolitan Municipality* 2017 (3) SA 146 (GJ), the facts were such that the municipality made a submission that a debt in respect of the consumption of water only became due after the municipality's reading of the installed meter and the subsequent issuing by the said municipality of an invoice to the debtor. The court rejected this argument as this would "entitle the respondent to ignore its constitutional duties, which include debt collection, indefinitely". Furthermore, the court emphasised it is the municipality's duty to take reasonable steps to collect what is due to it. In this regard, the court held that any obligation to pay charges for the actual consumption of water and electricity older than three years from the date of invoice had extinguished by prescription due to the municipality's failure to take reasonable steps to collect what was due to it.

In conclusion, the municipalities are:

(i) entitled to claim payment of all rates, taxes and property charges which fall within the definition of Municipal Charges for a period of two years preceding the date of application for the Certificate as contemplated in section 118(1) of the Municipal Systems Act, together with all interest accrued on such amounts regardless of the solvency status of the relevant person; and
(ii) secured for the payment of "taxes", as defined in section 89(5) of the Insolvency Act, for a period of two years prior to the date of liquidation, together with all interest accrued on such amounts, in preference to any holder of a mortgage bond.

Insofar as charges relative to actual consumption of water and electricity are concerned, municipalities have a claim in relation thereto provided the amounts have become due and the debtor has been requested to make payment thereof. Any failure on the part of the

municipality to take reasonable steps to collect these amounts, may result in the municipality's claim being extinguished by prescription, after the lapse of a period of three years.



Khathu Neluheni

Director

View Profile