



SHOULD A CREDITOR BE ABLE TO
ATTACH A MUNICIPALITY'S ASSETS?

The new State Liability Bill

Photo: TFM Conversions, East London

Attaching the assets of bad debtors is one of the few remedies that creditors can rely on when approaching a court to enforce their rights. Municipalities, in as much as they vary in needs and efficiency of service delivery, also have varying credit records. While some battle with credit control and debt-collection from their constituents, others have developed reputations for being notoriously bad debtors.

These municipalities, like all bad debtors, have to face the legal consequences of their debt. The MFMA and case law has made it clear that the assets of a municipality can be attached by creditors to satisfy judgment debts (i.e. court orders requiring the municipality to pay money). This is in contrast to the law that prohibits the attachment of the assets of national and provincial government, namely section three of the State Liability Act of 1957. The Constitutional Court, however, has invalidated this section.

Two new bills, the State Liability Bill and the accompanying Constitution Eighteenth Amendment Bill propose to remedy the situation. The State Liability Bill proposes to exclude the assets of the national, provincial and municipal government from attachment. This article critically assesses the Bill and the

proposed constitutional amendment, particularly in respect of their impact on local government. In so-doing, it will examine the case law and legislative developments that preceded these bills.

Local government and the State Liability Act of 1957

In *Mateis v Ngwathe Plaaslike Munisipaliteit* the Supreme Court of Appeal held that a municipality was not protected by the State Liability Act of 1957. The Court held that because the Act only referred to national and provincial governments, local government was not included. Consequently their assets could be attached in a sale of execution.

The MFMA of 2003 and the liquidations of assets

The Municipal Finance Management Act was adopted after the *Mateis* judgment. The general principle is that if a municipality cannot meet its financial commitments, its non-core assets may be liquidated in order to pay creditors. 'Non-core assets' are defined as assets not reasonably necessary to sustain effective administration or to provide the minimum level of basic municipal services'. The principle is clear: it is not feasible to liquidate the core assets of a municipality as it is an essential organ of state that must continue the delivery of basic municipal services.

There are thus limits to realising a monetary claim by liquidating municipal assets.

Nyathi v MEC for Department of Health, Gauteng

In *Nyathi v MEC for Department of Health, Gauteng* the Constitutional Court declared section 3 of the State Liability Act unconstitutional.

Denying judgment creditors the remedy of attachment violated their right to be treated as equal before the law and the right to equal protection and benefit of the law guaranteed by section 9(1) of the Constitution. It also violated creditors' section 34 rights of access to courts. Turning to the question of whether section 3 is a reasonable and justifiable limitation of these rights, the Court saw the purpose of the section as being 'to protect the state interests by disallowing attachment as it has the potential to disrupt service delivery and interfere with the state's accounting procedures'.

However, the Court observed:

I agree that the attachment of certain state assets, for example ambulances and dialysis machines, would severely disrupt service delivery and would also unjustifiably limit the rights of many other individuals. There are few countries which allow such attachment and even if it is allowed, there is very specific legislation which prescribes the assets which can be attached, such assets being deemed to be non-essential to the proper functioning of the state.

A distinction is thus to be drawn between assets that are essential for the functioning of the state and public well-being which should not be subject to attachment and other, non-essential ones, that could. This is precisely the approach adopted in the MFMA. The general principle evident is that in the event of a municipality being unable to meet its financial commitments, non-core assets of a municipality may be liquidated in order to pay creditors.

Constitution Eighteenth Amendment Bill

The Bill proposes adding section 173A to the Constitution, providing that an Act of Parliament must prescribe reasonable procedural requirements for the institution of legal proceedings against the state and measures for enforcing the execution of final court orders against the state. Two comments need to be made.

- Section 173A(1) opens with the phrase: 'Despite any other provision of the Constitution, an Act of Parliament must prescribe reasonable ... measures for enforcing the execution of final court orders against the state, including payments'. What can the words 'any other provision of the Constitution' refer to? The only answer can be that they refer to other provisions of the Constitution which may be applicable to the execution of court judgments. In particular, the Constitutional Court held that sections 9 and 34 were applicable. The Bill is thus an

attempt to insulate the State Liability Bill from scrutiny in terms of the Bill of Rights. It defeats the entire purpose of having a constitution as the foundation of all law if certain types of laws can be excluded from constitutional scrutiny. This is also in violation of one of the founding values of the Constitution, namely 'supremacy of the Constitution and the rule of law'. Amending the Constitution to say that it is no longer supreme amounts to removing this foundational value. Such a proposition cannot even be contemplated, let alone considered, as it goes to the heart of our constitutional state.

- There is no suggestion that the envisaged legislation would exclude local government. Indeed, section 173A(3) establishes the important principle that there can be differentiation between the three spheres of government. Unfortunately, there is little attempt to do so in the accompanying Bill with respect to local government.

State Liability Bill

Clause 7(1) of the Bill establishes the rule that no execution or attachment of state property is allowed. 'State property' includes municipal property. ('State' is defined as including an organ of state, and the latter includes a municipality or municipal entity.) If a municipality cannot make payment within 30 days of a final court order because of a lack of funds, the following steps must be taken:

- (a) the accounting officer of an organ of state must submit 'such motivated reason ... to the court and, where applicable, to the National or provincial treasury concerned, as the case may be, ... applying for the necessary funds in the manner prescribed'.
- (b) If the National or provincial treasury is satisfied that the organ of state has funds available, it must as soon as possible direct, in writing, the accounting officer to make the payment.
- (c) If the National or provincial treasury is satisfied that there are no or insufficient funds available (or the accounting officer has failed to comply with earlier steps), it must intervene. In the case of a municipality it (the National or provincial treasury) must reduce 'any equitable share, allocation or other transfer from the relevant Revenue Fund to which the municipality is entitled by an amount equal to the judgment debt' and pay the debt.
- (d) The National Treasury must intervene only if there are no or insufficient funds in the Provincial Revenue Fund to which the municipality is entitled, or the provincial treasury fails to intervene.
- (e) The National or provincial treasury may deduct the amount from any equitable share or transfer from revenue raised

key points

- Local government did not enjoy the protection of the State Liability Act of 1957.
- The MFMA establishes the principle that any asset not necessary for the provision of basic municipal services or administration may be liquidated.
- The Constitution Eighteenth Amendment Bill and the State Liability Bill of 2009 propose to include local government in the procedures that apply when court orders require an organ of state to pay money (a judgment debt). These Bills include municipalities in their protection against the attachment of assets to satisfy court orders.
- The attempt by the Constitution Eighteenth Amendment Bill to insulate the State Liability Bill from constitutional scrutiny runs counter to the entire constitutional enterprise of the South African constitutional state.
- In principle it is correct to include municipalities in a general law governing the payment of court orders requiring money to be paid to satisfy a judgment debt, but it is wrong to exclude all municipal property from attachment for this purpose.
- The Bill does not provide a separate and clear procedure for municipalities to pay court orders.

nationally, in that financial year or any ensuing financial years or years.

- (f) The enforcement mechanism for compliance by the accounting officer is that failure to comply with a directive of the National or provincial treasury opens the accounting officer to a charge of financial misconduct in terms of the MFMA which must be pursued.

Comment

The first objection to the Bill is that it conflicts with the principle developed in the MFMA that where a municipality cannot pay its debts, non-essential assets must be liquidated. There are very good reasons for incorporating this principle into the management of payment by municipalities.

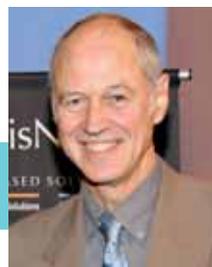
First, the attachment of non-essential assets is a strong inducement to effect payment promptly. It imposes a strict discipline on municipalities not to waste money on non-essential assets as they are open to attachment.

Second, the potential attachment of luxuries is a strong incentive for quick action from the political executive.

Third, the Bill allows a municipality to compromise its future by having final court orders deducted from its equitable share or other transfers. Those transfers are designed for specific purposes, such as free basic services.

The second objection, flowing from the first, is that there is no dedicated procedure for municipalities. While many of the provisions regarding notice requirements should be the same, the reporting obligations should be differentiated. The result is a confusing set of provisions. First, it is not clear how the municipalities must report to the provincial treasury and/or the National Treasury. Second, the Bill provides that National Treasury may intervene only if there are insufficient funds in the Provincial Revenue Fund or the provincial treasury fails to intervene. From this it seems that the first port of call is the provincial treasury and it should pay the claim from its Provincial Revenue Fund. However, there are usually very limited funds earmarked for local government lying in the provincial coffers. None of the equitable share of a municipality goes through the Provincial Revenue Fund. There are also very limited other funds that the province passes on to municipalities, aside from transfers for housing. If the province then subsidises court order payments from the housing grant, the municipality will be short on that score, which exposes it to further claims by building contractors when they are not paid from budgeted funds. This looks like a case of stealing from Peter to pay Paul.

Deducting court order payments from the current and future equitable share and other transfers also flies in the face of the principle that municipalities must stand on their own financial feet. In *MEC Mpumalanga v IMATU*, the Supreme Court of Appeal held that the provincial government did not stand surety for the debts of a municipality. Only the equitable share can be regarded as funds a municipality is entitled to. The other funds are conditional grants to be used for dedicated purposes. If debtors cannot seek to liquidate non-essential assets, they will look to national and provincial governments to settle debts from conditional grants. This does not make for self-reliance and good financial management.



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