

## SECTIONAL TITLE UNIT OWNERS' LIABILITY FOR PAYMENT OF BODY CORPORATE'S DEBTS

### 1 Introduction

In 1972 the authors of a commentary on the Sectional Titles Act 66 of 1971 concluded their analysis of the Act by stating:

“In hierdie oorsig het ons maar liggies op die gebreke van die Wet gewys ... Die Wet moes nooit gemaak gewees het nie. Die man wat 'n seksie koop, koop moeilikheid.”

(De Wet and Tatham “Die Wet op Deeltitels” 1972 *De Rebus Procuratoriis* 205).

What troubled the authors, amongst others, was the fact that section 35 of the Act empowered creditors of the body corporate of a sectional title scheme to hold unit owners personally liable for payment of the body corporate's judgment debts. They expressed their views on this as follows:

“Op die ou end moet die 'eienaars' van seksies vir (die regspersoon se) skulde instaan, behalwe vir sover die aanspreeklikheid deur versekering gedek is ... Maar dit is nie die einde van die 'seksie-eenaar' se aanspreeklikheid nie. Hy kan as vonnisskuldenaar gevoeg word vir enige vonnisskuld van die regspersoon, en eksekusie kan teen hom gehef word vir 'n deel van die vonnisskuld, in verhouding met sy kwota, en selfs al het hy al sy bydraes tot op datum betaal. Dit is waar dat hy verhaal het op die regspersoon, maar sodanige verhaal kan 'n skrale troos wees as die sake van die regspersoon so deurmekaar is dat die regspersoon nie eens sy skulde kan betaal nie ...”

Other sectional title experts gave section 35 scant attention. Most merely mentioned its existence, coupled with a statement that the extent of each owner's liability was determined by reference to the respective participation quotas. The Sectional Titles Act 95 of 1986 replaced the 1971 Act, but section 35 of the latter Act remained intact and was taken over in the new Act as section 47(1). As was the case with its predecessor, section 47(1) also escaped detailed academic evaluation when the 1986 Act became law. Presumably this lack of concern was based on the belief that the provisions of section 47(1) would rarely be applied in practice because one could hardly imagine a situation where creditors of a sectional title body corporate would be compelled to turn to individual owners to foot the bill. Few commentators took serious notice of a growing problem in sectional title schemes: the culture of non-payment of levies. Over the years the problem escalated rapidly, and today the harsh reality is that many sectional title bodies corporate in South Africa find themselves in grave financial distress because unit owners simply do not pay levies. Some owners don't pay because they did not know at the time they bought their units that they would have to pay

levies to the body corporate over and above their monthly bond repayments to the bank. They never budgeted for levy payments and cannot afford to pay (see the remarks made by Hartzenberg J in *Body Corporate, Geovy Villa v Sheriff, Pretoria Central Magistrate's Court* 2003 1 SA 69 (T) 73D). Others initially pay their levies but later stop doing so for financial reasons. In some instances even affluent owners refuse to pay because they are disillusioned with the way in which the sectional title complex is being managed by the trustees (see, eg, *Body Corporate of Fish Eagle v Group Twelve Investments (Pty) Ltd* 2003 5 SA 414 (W)). A further group argue that they do not see a reason to pay if their neighbours are not paying.

When levies are not paid a body corporate obviously has to cut its spending to the bone in an attempt to make ends meet. However, there are certain liabilities over which a body corporate has no or little control, notably monthly rates and service charges payable to municipalities. Where reserves and monthly income are insufficient to meet these commitments, the body corporate inevitably defaults on payment. At that point creditors have no choice but to pursue whatever remedies they have in order to obtain payment. Turning to the unit owners individually then becomes an attractive option.

This note focuses on the scope and application of section 47(1) of the Sectional Titles Act 95 of 1986. The section must be viewed in the context of certain key provisions of the Act. These are discussed briefly. Attention is also given to the changes made to the section by the Sectional Titles Amendment Act 7 of 2005. It is argued that although the Amendment Act has absolved some unit owners from liability for payment of the body corporate's debts, it has introduced an uncertainty as to whether owners can be held liable for body corporate debts incurred *before* they became members of the body corporate.

## 2 Section 47 in context

Section 47 must be seen against the background of the following key provisions of the Sectional Titles Act:

- (a) Every sectional title scheme is managed by a body corporate established with effect from the date on which any person other than the developer becomes an owner of a unit in the scheme (s 36(1)). Membership of the body corporate is automatic upon obtaining transfer of a unit. It terminates when an owner ceases to be the owner of a unit (s 36(2)). Cessation of ownership of a unit is the only way in which membership can be brought to an end. No member can resign from the body corporate while remaining the owner of a unit in the scheme.
- (b) The functions of a body corporate are to control and manage the sectional title scheme to which it relates (s 36(4)). In order to meet management expenses a body corporate may impose a levy on each unit owner in proportion to the unit's participation quota. Levies are due and payable on the passing of a resolution to this effect by the body corporate's trustees. They must be paid by the persons who were the owners of units at the time that the trustees passed their resolution (s

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37(2)). Special levies may be imposed by the trustees from time to time, when necessary (rule 31(4) of the management rules contained in annexure 8 to the regulations promulgated under the Act).

- (c) Levies may be recovered by a body corporate by action in court (s 37(2)). Levy defaulters may not exercise a vote in respect of ordinary resolutions at general meetings of the body corporate (rule 64(a) of the management rules), but no unit owner may be expelled from the scheme or the body corporate by reason of non-payment of levies. Unit owners aggrieved by other owners not paying levies cannot resign their membership of the body corporate, nor can they withhold payment of their own levies in protest (see *Body Corporate of Fish Eagle v Group Twelve Investments (Pty) Ltd* 2003 5 SA 414 (W)).
- (d) A body corporate, though a legal entity, does not fall under the Companies Act 61 of 1973 (s 36(5)). It is not required to have any assets on its establishment and it is not required to maintain any capital reserves, other than a reasonable reserve to cover future maintenance and repairs. There is no specific penalty if for any reason the latter reserve is inadequate or, for that matter, not kept at all.
- (e) It is an open question whether a body corporate can be wound-up on the ground that it is insolvent (*Ex parte Body Corporate of Caroline Court* 2001 4 SA 1230 (SCA)). It has been held that a body corporate is not a "debtor" as defined in the Insolvency Act 24 of 1936, meaning that it cannot be sequestrated under the provisions of that Act (*Reddy v Body Corporate of Croftdene Mall* 2002 5 SA 640 (D)).

It is clear from the above provisions of the Act that the success or failure of a sectional title scheme is by and large in the hands of the unit owners themselves. The unit owners control the body corporate which, in turn, controls the scheme. As members of the body corporate the unit owners elect trustees who are in day to day control of the scheme's operations. The unit owners, through the body corporate, determine the amount payable in respect of levies. The system can work perfectly, provided all role players play their part. Everything hinges on proper management. When management is not up to scratch, however, problems will and do occur, particularly if management fails to take its levy collection responsibility seriously. A scheme can end up facing serious financial problems if levies are not paid consistently and on time. In this respect *all* unit owners must cooperate. If some pay levies and others not, those that pay may soon discover that their contributions are not enough to keep the scheme afloat. When that stage is reached none of the owners can simply walk away from the problem. They are locked into the body corporate's woes as long as they remain unit owners.

Owners aggrieved by the body corporate's failure to take action against levy defaulters may invoke the provisions of section 41(1) which empowers an owner to apply to court for an order appointing a curator for the body corporate to institute and conduct proceedings on the body corporate's behalf. In extreme cases application may also be made to the court for the

appointment of an administrator (s 46(1); *Bouraimis v Body Corporate of the Towers* 1995 4 SA 106 (D)). However, in practice few unit owners are keen to pursue these remedies. Most prefer the easy way out, namely to sell their units. This requires a closer look at the buyer's position. In terms of the Act (s 15B(3)(a)(i)(aa)) ownership in a unit cannot be transferred from a seller to a buyer unless the Registrar of Deeds is furnished with a certificate stating that at the date of registration all moneys due to the body corporate by the transferor in respect of the unit have been paid or that satisfactory arrangements for payment have been made. In other words, what the buyer will know on registration of transfer is that the seller has paid his levies, or that satisfactory arrangements for payments have been made. However, he will not necessarily know whether all the *other* unit owners are also up to date with their levy payments. There is no provision in the Act imposing a duty on a seller, the trustees or the scheme's managing agent to furnish a buyer with details of the scheme's financial position. In terms of rule 32(2) of the prescribed management rules the trustees must make a copy of the *rules* available to a prospective purchaser of a unit, but there is no rule obliging the trustees to make available a copy of the scheme's latest financial statements. A buyer who discovers that he has bought into a financially distressed sectional title scheme may in appropriate instances have a contractual claim against the seller based on misrepresentation, but the fact remains that unless the sale is set aside and the transfer is cancelled the buyer has no choice but to accept what he has inherited from the seller, that is, a scheme beset by financial problems. This raises the question whether the buyer can be held liable for payment of the body corporate's debts incurred at a time *before* he obtained transfer of his unit. The answer requires a closer look at section 47.

### 3 Analysis of section 47

Prior to its amendment by the Sectional Titles Amendment Act 7 of 2005 section 47(1) read as follows:

"Recovery from owners of unsatisfied judgment against bodies corporate, and non-liability of bodies corporate for debts and obligations of developers.

- (1) If a creditor of a body corporate has obtained judgment against the body corporate, and such judgment, notwithstanding the issue of a writ, remains unsatisfied, the judgment creditor may, without prejudice to any other remedy he may have, apply to the court which gave the judgment, for the joinder of the members of the body corporate in their personal capacities as joint judgment debtors in respect of the judgment and, upon such joinder, the judgment creditor may recover the amount of the judgment debt still outstanding from the said members on a *pro rata* basis in proportion to their respective quotas or a determination made in terms of s 32(4): Provided that any member who is so required to make a payment to a judgment creditor after he has paid to the body corporate any contribution which he was required to pay to that body corporate in respect of the same debt, shall be entitled to obtain a refund from the body corporate of the amount of the payment so made to the said creditor.
- (2) ..."

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The following are key features of section 47(1):

- (a) A body corporate creditor cannot simply demand payment from individual unit owners the moment the body corporate fails or refuses to settle its debt. Judgment must first be obtained against the body corporate and such judgment must remain unsatisfied notwithstanding the issue of a writ. The judgment creditor must then apply to the court which gave the judgment for the joinder of the body corporate members in their personal capacities as joint judgment debtors. Upon such joinder the judgment creditor may recover the amount of the judgment debt from the members on a *pro rata* basis.
- (b) Members of a body corporate are not jointly and severally liable for the body corporate's debts. A unit owner's liability for payment of the judgment debt is limited to a percentage of the debt based on his unit's participation quota, or a determination made in terms of section 32(4). (The latter section empowers the developer or a body corporate by special resolution to modify an owner's liability for the judgment debts of a body corporate. It is not discussed further in this Note).
- (c) A judgment creditor is not empowered to join only *some* members of the body corporate in their personal capacities as joint judgment debtors. *All* members must be joined, but nothing prohibits the judgment creditor from recovering *pro rata* payments from some members only.
- (d) The judgment creditor is empowered to join those persons who are members of the body corporate at the time when the application for joinder is made to court. Persons who were members of the body corporate at the time when the debt was incurred but are no longer members at the time when the application for joinder is made, cannot be joined as joint judgment debtors. Conversely, persons who were *not* members of the body corporate at the time when the debt was incurred but who became members in the meantime *can* be joined as joint judgment debtors. In other words, the question is not whether a person was a body corporate member at the time when the debt was incurred; the question is whether a person is a member at the time when the application for joinder is made.
- (e) Section 47(1) draws no distinction between levy paying members and levy defaulters. In other words, persons who had consistently paid their levies from the date that they became members of the body corporate can be joined as joint judgment debtors. The judgment creditor may elect to recover a *pro rata* payment from them only, and not from the levy defaulters (even though the latter may have been joined as judgment debtors).

Section 47(1), in its original form, clearly had far-reaching consequences for both current and prospective members of a body corporate. In *Reddy v Body Corporate of Croftdene Mall* 2002 5 SA 640 (D&CLD) the court had the following to say in this regard (644I):

"This is a most significant subsection. In the first place it brings about an important deviation from the principle that a corporate entity is liable for its own debts. Here the Legislature has indicated that if the levying of execution does not result in a judgment being satisfied or if a *nulla bona* return is issued,

the judgment creditor applies to court and joins members of the body corporate as joint judgment debtors who are obliged to satisfy the judgment in proportion to their participation quotas in the scheme. In my view, this indicates clearly that the Legislature did not intend that the law of insolvency or of winding-up of companies as a means to enforce payment of a debt would apply to bodies corporate. The creditor's remedy is against all members of the body corporate and is not limited only to those who are members at the time when the debt was incurred. Any person who takes transfer of a section ought to apprise him/herself of the financial position of the body corporate. Certainly the trustees ought not to allow a situation to come about where the liabilities of the body corporate exceed its assets and it is unable to discharge its ordinary day-to-day liabilities to its service providers and others ..."

#### 4 Section 47(1) as amended by the Sectional Titles Amendment Act 7 of 2005

A Sectional Titles Amendment Bill was published in *Government Gazette* 27047 on 10 December 2004. One of the proposals contained in the Bill was that the proviso to section 47(1) be amended as follows (words in bold type in square brackets indicating omissions and words underlined indicating insertions):

“:Provided that any member who **[is so required to make a payment to a judgment creditor after he has paid to the body corporate any contribution which he was required to pay to that body corporate in respect of the same debt, shall be entitled to obtain a refund from the body corporate of the amount of the payment so made to the said creditor]** has paid the contributions due by him or her in terms of section 37(1) to the body corporate prior to the judgment against the body corporate, may not be joined as a joint judgment debtor in respect of the judgment debt.”

If the Bill became law the effect would have been that no member of a body corporate who has paid his levies may be joined as a joint judgment debtor in respect of a judgment obtained against the body corporate. It would have made no difference whether or not the debt in question was incurred before or after a unit owner became a member of the body corporate. The only question would have been: had the member paid his levies? If the answer was affirmative, the member would have been absolved from liability for payment of the body corporate's debts, and he could not be joined as a joint judgment debtor.

The proposed amendment of section 47(1) did find its way into the Amendment Act, but in somewhat different form. There is a subtle difference between the wording of the Bill and the Act. In the Act the amended section 47(1) reads as follows:

“:Provided that any member who **[is so required to make a payment to a judgment creditor after he has paid to the body corporate any contribution which he was required to pay to that body corporate in respect of the same debt, shall be entitled to obtain a refund from the body corporate of the amount of the payment so made to the said creditor]** has paid the contributions due by him or her in terms of section 37(1) to the body corporate *in respect of the same debt* prior to the judgment against the body corporate, may not be joined as a joint judgment debtor in respect of the judgment debt” (my italics).

The words “in respect of the same debt” did not appear in the original Bill.

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They were obviously inserted in the Amendment Act with a specific purpose, but the problem is that it is not entirely clear how the amended section 47(1) should now be interpreted. It is submitted that the position is as follows:

- (a) A unit owner who has paid his levies cannot be joined as a joint judgment debtor in respect of the body corporate's unpaid accounts, provided the levies were raised by the body corporate with the intention that they should cover payment of the accounts in question. The unit owner cannot be joined as a joint judgment debtor because by having paid his levy he has already made payment "in respect of the same debt". For example, if a body corporate member has paid his levies for the full year but the body corporate failed to pay the municipal accounts for that year, such member cannot be held liable by the municipality to make any further payment in respect of those accounts.
- (b) If a *special levy* has been imposed to cover extraordinary expenditure, a member who has paid his ordinary levy but not the special levy can be joined as a joint judgment debtor if judgment is obtained against the body corporate in respect of such extraordinary expenditure. Conversely, a unit owner who has paid the special levy cannot be joined as a judgment debtor in respect of the expenditure in question because he has already made payment "in respect of the same debt". An owner who has paid the special levy but not his normal levy cannot be held liable as a joint judgment debtor in respect of the special expenditure, but can be joined as a judgment debtor in respect of other "ordinary" debts of the body corporate.
- (c) The real difficulty is whether an owner can be joined as a judgment debtor in respect of debts incurred by the body corporate *before* such owner became a member of the body corporate. That was the position prior to the Amendment Act. Has this now been changed? On the one hand it may be argued that if the levies paid by an owner relate to expenses incurred (or to be incurred) by the body corporate *after* the owner became a member, a creditor claiming payment of debts incurred *before* such owner became a member may join the owner as a joint judgment debtor in respect of those debts because the owner cannot say that his levies were paid *in respect of the same debt*. On this approach the amendment of section 47(1) has brought some relief for sectional title owners who pay their levies, but has not removed the risk of investing in a development where the body corporate has unpaid debts. If this is correct the anomaly would arise that a buyer of a sectional title unit can always be joined as a joint judgment debtor in respect of debts incurred by the body corporate before he took transfer, even though the seller of the unit could not be so joined because he had paid the levies in respect of those debts.

A contrary argument may be that by amending section 47(1) the legislature clearly intended to rectify the situation where owners who pay their levies can be held liable for payment of body corporate debts. It could never have been the legislature's intention to grant relief to levy paying owners but no relief to persons (*ie*, buyers) who were never even responsible for payment of levies. Accordingly, section 47(1) must be interpreted to mean that unit owners can be joined as judgment debtors

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only if during the period of their membership of the body corporate  
(i) they were liable to pay levies in respect of the debt in question, and  
(ii) they failed to pay the required levies.

## 5 Conclusion

The Sectional Titles Amendment Act 7 of 2005 did not remove all the problems associated with section 47(1) of the principal Act. The Amendment Act does make it clear that a unit owner who has paid all his levies cannot be joined as a joint judgment debtor in respect of body corporate debts incurred after such owner became a member of the body corporate. What is uncertain, however, is whether a member of a body corporate may, as in the past, be joined as a joint judgment debtor in respect of debts incurred by the body corporate *before* such member obtained his membership of the body corporate. There is much to be said in favour of the view that the legislature intended to absolve a member from liability for the body corporate's debts, provided the member has paid all the levies which he was liable to pay. Unfortunately, however, the matter will remain shrouded in uncertainty until cleared up by the courts or the legislature. An acceptable solution would be to amend section 47(1) to the effect that if an owner has paid his levies neither he nor his successor in title may be joined as judgment debtors for payment of the body corporate's debts, provided the latter also keeps up his levy payments.

Until the matter is resolved by the courts or cleared up by a further amendment to section 47(1), prospective buyers of sectional title units would be well advised to continue exercising caution. The fact that the seller has paid his levies does not mean that the buyer runs no risk of being joined as a joint judgment debtor in respect of debts incurred by the body corporate prior to the buyer obtaining transfer of the unit he bought. To protect his interests the buyer should obtain from the seller a copy of the latest financial statements of the sectional title scheme. Those financial statements must be closely examined to determine the scheme's financial position. Ideally a statement should be obtained from the trustees to the effect that no material change has occurred in respect of the scheme's financial affairs from the date of the financial statements. If the financial statements and/or such declaration from the trustees cannot be obtained, a clause should be inserted in the relevant sale agreement whereby the seller indemnifies the buyer in respect of any payment for which the buyer may be held liable under section 47(1) relating to debts incurred by the body corporate before the buyer took transfer.

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