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THE ROLE OF THE RULE OF LAW IN GOVERNMENT BUSINESS TRANSACTIONS

Are you doing business with the government? Take precautionary measures.

The government and all organs of the state within each sphere of government can only act if they are empowered by law (not by the Minister, MEC or the Council) to conduct state commercial activities. Therefore, if an organ of the state conduct commercial activities with the private companies, there must be a law that authorizes them to do so and if there is a prescribed procedure that must be followed when entering into a business transaction, that procedure must to be adhered to. To do otherwise would render the transaction unlawful and liable to be set aside by the court of law on judicial review.

Recently, the KZN High Court, in the case of *Umgungundlovu District Municipality v Amaraka Investment 37 (Pty) Ltd and others*, declared unconstitutional and unlawful and set aside an agreement between a District Municipality and a private company (the company). As part of its development plan to build a private hospital, the company applied to the Municipality for water works infrastructure since this is a responsibility of the Municipality. This was granted and the Municipality agreed to install the necessary water infrastructure. However, by the time the development was completed in 2014, the Municipality had not erected the required infrastructure. There was an agreement that the company construct a temporary infrastructure (conservancy tank and other water works) to get the hospital running. The Municipality and the company then entered into an agreement in terms of which the company agreed to empty and transport the affluent from the conservancy tank to the nearby Waste Water Treatment Works, and the Municipality agreed to pay the company for this service. The full Council passed the resolution for the Municipality to enter into this transaction. The company then started to transport the affluent to the agreed destination and submitted their invoices to the Municipality monthly as per the agreement. The Municipality failed to pay the invoices and after several months, decided to terminate the agreement. The dispute ensued. The Municipality lodged a court application to have the agreement declared invalid because there was no tender process followed before the conclusion of the agreement as demanded by the Constitution, the Municipal Finance Management Act and the Municipal Systems

Act. The company disagreed and opposed this application. The Court agreed with the Municipality and declared the agreement unconstitutional and unlawful, and therefore invalid.

The court's decision was based on the following considerations:

1. District Municipalities are constitutionally and legislatively obliged to provide clean water, water works and sanitation services. Simply put, it is their responsibility to make sure that there is clean water and water infrastructure in their areas of jurisdiction. They are also water services authorities in terms of Water Services Act.

2. Section 217(1) of the constitution and Section 111 of the Municipal Finance Management Act oblige the Municipalities and other organs of state to adopt and follow a Supply Chain Management Policy for the appointment of service providers to provide goods and services, with few certain exceptions.

3. Section 76 of the Systems Act authorizes the Municipalities to either internally provide the water infrastructure services or engage external service providers to provide this service. In terms of Section 78 of the Systems Act if the Municipality choses to engage external service provider it must follow a certain procedure. The procedure includes (a) engaging the community, (b) doing feasibility study, (c) assessing different service delivery options, and (d) - most importantly - complying with any applicable legislation relating to the appointment of service providers. Section 80 of the Systems Act authorizes the Municipalities to provide services through service delivery agreements with external service providers. Section 83 provides that if the service delivery is to be done by a private person a competitive bidding process must be followed.

The reading of the above legislation appears to suggest that the Municipality was indeed authorized to engage a private company to provide the services but not in a manner in which it did so. The legal issue is that the procedure of securing the services of this private company was never adhered to by the Municipality. There was no community consultation, no feasibility study conducted, no comparison of available service delivery options, and no public procurement process undertaken. The Municipality clearly flouted several provisions of the Constitution and legislation (MFMA and Systems Act). Our courts have pronounced on several occasions that the exercise of public power is only legitimate if (a) authorized by law, (b) exercised within the set boundaries, and (c) a prescribed procedure has been followed. Therefore, an agreement entered into without authority is invalid.

It is important to note that authority to act must come from the law, not from any individual or structure having a high position in government.

Therefore, before you sign on that dotted line please ensure that (a) the transaction is authorized by law, (b) prescribed procedures (if any) were followed, and (c) the person signing on behalf of the government is authorized to sign.

For more clarity and information on the above, feel free consult our attorneys on the contact details below or visit our website: www.tmj.co.za

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