Accountability, Estoppel and Bypassing of the Municipal Finance Management Act: A Note on *Merifon (Pty) Ltd v Greater Letaba Municipality* Trilogy

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Abstract

Accountability and transparency reinforce the constitutional principles of governance, which constitute equality before the law, separation of powers, legality and the rule of law, which are central to the conception of modern constitutional order. The trilogy of *Merifon (Pty) Ltd v Greater Letaba Municipality Limpopo Division*, Case No 01/2014 (18 July 2019), *Merifon (Pty) Ltd v Greater Letaba Municipality* [2021] ZASCA 50 and *Merifon (Pty) Ltd v Greater Letaba Municipality* [2022] ZACC 25 poses fundamental questions regarding the failure of a municipal manager and incompetent council to comply with statutory prescripts. Although the narrow issue for determination concerned the seller's reliance on estoppel and the Turquand Rule to hold a municipality to the unlawful and inflated sale of land agreement, the *Merifon* litigation invites consideration of the practical reality of malfeasance in the local government sphere. In this note the litigation history and the analytical framework as well as the Municipal Finance Management Act 56 of 2003 (MFMA) are examined. The critical aspects of the three judgments regarding the problematic reliance on estoppel and the Turquand Rule in the face of peremptory prescripts of MFMA are subsequently examined.

Keywords: Accountability; corruption; estoppel; legality; malfeasance in public office; ostensible authority; representation and capacity

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Introduction*

At first blush, the *Merifon*[1] trilogy narrowly focuses on a specific performance claim by an aggrieved seller relying on estoppel and the Turquand Rule (or alternatively known as the 'indoor management rule') to circumvent peremptory provisions of the Local Government: Municipal Finance Management Act 56 of 2003 (MFMA). However, a closer look at the case reveals that the protracted litigation was firmly anchored in the tension between accountability and malfeasance in public office. Against the backdrop of the release of the State Capture Report Recommendations,[2] *Merifon* affords an opportunity to interrogate the extent to which accountability together with other normative value systems[3] (that serve as keystones to the constitutional framework) such as transparency and openness are observed, fulfilled and respected. It should be noted that an analysis of public accountability inevitably leads to the heart of constitutional law as it implicates legality, which draws its strength from the rule of law. Besides an in-depth scrutiny of section 19 of the MFMA, this note proceeds to examine the application of estoppel and the Turquand Rule in transactions entered between private parties and state organisations.

While this note focuses on *Merifon*, it remains crucial to look into public accountability, particularly the meaning and its objective within the public sector as the core feature of the Constitution, as it forms the central argument in the *Merifon* cases. It should be kept in mind that the proper management and monitoring of public accountability demand a

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1 *Merifon (Pty) Ltd v Greater Letaba Municipality* (unreported judgment of the High Court, Limpopo Division, Polokwane) Case No 01/2014 (18 July 2019) (*Merifon I*); *Merifon (Pty) Ltd v Greater Letaba Municipality* [2021] ZASCA 50 (*Merifon II*) and *Merifon (Pty) Ltd v Greater Letaba Municipality* [2022] ZACC 25 (*Merofon III*).

2 The Judicial Commission of Inquiry Report (2021) Part 1, Vol 1 – procurement 715. Further, see generally, Daily Maverick 'Here You Go: The Final State Capture Report Recommendations – At Last' <https://www.dailymaverick.co.za/article/2022-06-22-here-you-go-the-final-state-capture-report-recommendations-at-last/> accessed 22 June 2022.

3 In *Nyathi v MEC: Department of Health Gauteng* 2008 (5) SA 94 (CC) paras 80–1 (*Nyathi*). Madala J was satisfied that: 'Certain values in the Constitution have been designated as foundational to the democracy. This in turn means that as pillar-stones of this democracy, they must be observed scrupulously. If these values are not observed and their precepts are not carried out conscientiously, we have a recipe for the constitutional crisis of great magnitude. In a state predicated on a desire to maintain the rule of law, it is imperative that one and all should be driven by a moral obligation to ensure the continued survival of the South African democracy.' See generally, Tumo Maloka, **'**Recent Developments Regarding Costs Awards in Constitutional and Public Interest Litigation' (2019) 34 SAPL 1 and '*Biowatch* Shield, Costs Liability for Abuse of Process and Crossfire Litigation' (2020) 41 Obiter 186; Tumo Maloka and Nokukhanya Jili, 'The Role of the Judiciary in Promoting Accountability, Responsiveness and Openness: Lessons From *Life Esidimeni Arbitration* and *Black Sash/SASSA* Litigation' (2019) 54 Journal of Public Administration 105.

better understanding of public accountability and how it complements the system of public management.[4] It must also be emphasised that scholars' views about the meaning of public accountability may differ.[5] For this reason, Haidt posits that public accountability is essential when strangers have to cooperate with each other,[6] based on the premise that people who are trustworthy and able to trust each other will do what is expected of them.[7] Moreover, Rashid is of the view that public accountability in instances where team(s) of people work together in pursuit of common goal(s) resembles and explains inter-personal and reciprocal relationships.[8] This he titled 'mutual accountability' which means that team members need to evaluate one another's conduct.[9] Flowing from *Merifon* and considering public accountability in the municipal government sphere, it turns out that public accountability could mean different accountabilities between individuals or groups in diverse contexts.[10] Public accountability could have different objectives. For instance, in the municipal sphere, a central objective of the accountability of a municipality is to ensure proper services for its communities whereas another might be the proper usage of fiscal resources.

Legal Framework

The objective of the MFMA is the modernisation of the budget and the accounting and financial management practices by placing local government finances on a sustainable footing in order to maximise the capacity of municipalities to deliver services to communities.[11] A relevant part, section 19 of the MFMA which is headed 'Capital projects,' reads as follows:

> (1) A municipality may spend money on a capital project only if–

4 'Public Accountability: A Matter of Trust and Confidence, A Discussion Paper <https://oag.parliament.nz/2019/public-accountability/docs/public-accountability.pdf> accessed 20 February 2023.

5 See Dwight Frink and Richard Klimoski, 'Advancing Accountability Theory and Practice: Introduction to the Human Resource Management Review' (special edn 2004) 14 Human Resource Management Review 1–17. Further see Philip Tetlock, The Impact of Accountability on Judgment and Choice. Toward a Social Contingency Model' in M Zanna (ed), *Advances in experimental social psychology* ((New York, Academic Press 1992).

6 Jonathan Haidt, *The Righteous Mind: Why Good People are Divided by Politics and Religion* (UK, Penguin 2012) 87.

7 Haidt (n 6).

8 Faaiza Rashid, Mutual Accountability and its Influence on Team Performance (PhD thesis, Harvard University 2015) 3, 8, 9.

9 Rashid (n 8).

10 Public accountability (n 4).

11 See National Treasury <http://mfma.treasury.gov.za/> accessed 19 October 2022.

(a) the money for the project, excluding the cost of feasibility studies conducted by or on behalf of the municipality, has been appropriated in the capital budget referred to in section 17(2);

(b) the project, including the total cost, has been approved by the council;

(c) section 33 has been complied with, to the extent that that section may be applicable to the project;[12] and

(d) the sources of funding have been considered, are available and have not been committed for other purposes.

(2) Before approving a capital project in terms of subsection (1)(b), the council of a municipality must consider–

(a) the projected cost covering all financial years until the project is operational; and

(b) the future operational costs and revenue on the project, including municipal tax and tariff implications.

(3) A municipal council may in terms of subsection (1)(b) approve capital projects below a prescribed value either individually or as part of a consolidated capital programme.

Section 19 and the interplay between estoppel and the Turquand Rule are at the heart of the issues in *Merifon*. This section provides the circumstances under which the municipality may or may not spend money on a capital project.

Drawing from this section, the factual question, however, is whether section 19 of the MFMA finds application in the trilogy of litigation under discussion. The Supreme Court of Appeal (SCA) categorically stated that the foremost objective of the pertinent provision of section 19 is to preclude municipal disbursements from capital projects that lack an ample budget to do so, to safeguard and foster transparency and accountability,

12 Section 33 (1) (a) (i) and (ii) of the MFMA provides that: 'a municipality may enter into a contractwhich will impose financial obligations on the municipality beyond a financial year, but if the contract will impose financial obligations on the municipality beyond the three years covered in the annual budget for that financial year, it may do so only if – the municipal manager, at least 60 days before the meeting of the municipal council at which the contract is to be approved – has in accordance with section 21A of the Municipal Systems Act – made public the draft contract and an information statement summarising the municipality 's obligations in terms of the proposed contract; and invited the local community and other interested persons to submit to the municipality comments or representations in respect of the proposed contract; and has solicited the views and recommendations of – the National Treasury and the relevant provincial treasury; the national department responsible for local government; and if the contacts involves the provision of water, sanitation, electricity or any other service as may be prescribed, the responsible national department… .'

which includes fiscal and financial discipline.[13] This has also been accentuated by the Constitutional Court (CC) when determining the applicability of section 19 on the *Merifon* case. In this regard, the CC pronounced that

> sight ought not to be lost of the central factor which affirms application of section 19, being the fact that following the terms of the contract, it remained the municipality that incurred the obligation to pay as opposed to CoGHSTA, hence the summons were issued against the municipality and not CoGHSTA. [14]

Undoubtedly, the responsibility to honour the contract was possible only if the municipality had provided the required funds which would have had to be authorised by the municipal council through a resolution. For this reason, the court held that 'there can be no question of compliance with section 19 on account of the commitments made by CoGHSTA.'[15]

Case Facts

The *Merifon* litigation concerns an amount of ZAR52 million claimed by Merifon (Pty) Ltd from the Greater Letaba Municipality for a breach of sale agreement. The case has its origins in the latter's need of suitable land for low-cost housing. For several years the municipality has not had a budget to acquire land for human settlement and it had lost out on the provincial allocation of funds to municipalities to build low-cost houses.[16] In an attempt to remedy this situation, the then executive mayor sought the intervention of the provincial member of the executive council (MEC) of the Department of Cooperative Governance, Human Settlements and Traditional Affairs (CoGHSTA). In turn, the department engaged the Housing Development Agency (HDA) to assist the municipality, which led to the identification of suitable land.[17] Thereafter, negotiations commenced with the representatives of the seller, Merifon. On 6 March 2013, the head of the department formally confirmed the availability of funds for the purchase of the identified land as follows:

> We refer to the above mentioned transaction and hereby [confirm] that the Department in the current financial year ending 31 March 2013 has budgeted the required R52 Million excluding VAT required to acquire the above mentioned property required for human settlements development. The funds will be paid into the trust account of the transferring Attorneys after the Deed of Sale between the Municipality and the Seller has been concluded. The Department will furthermore pay the applicable transfer and registration costs amounting to R209 892.90.[18]

13 *Merifon II* (n 1) para 21.
14 *Merifon III* (n 1) para 39.
15 ibid.
16 *Merifon II* (n 1) para 5.
17 ibid para 23.
18 Merifon I (n 1) para 16

The letter was then presented to the municipal council for adoption at its special meeting held on 22 March 2013. Among the resolutions adopted at this sitting was the Council Resolution A. 1038/ 22/03/2013 / Acquisition of Remaining Extent and Portion 5 and 6 of the Farm Mooiplaats 434-LT. The resolution adopted by the council read 'that the commitment letter from CoGHSTA to purchase portion 5 and 6 of the farm Mooiplaats 434-LT is approved.'[19]

The adoption of the Council Resolution seemingly cleared the path for the conclusion of a contract of purchase and sale between Merifon (Pty) Ltd (Merifon) and the municipality. It transpired that prior to committing itself to pay the purchase price, including the transfer costs for the identified piece of land on behalf of the municipality, CoGHSTA had requested authorisation from the Provincial Treasury to disburse the amounts as reflected on its letter dated 6 March 2013. However, on 27 March 2013, the provincial treasury declined the department's request on the grounds that the purchase price for the property was inflated. The upshot of the provincial treasury's *volte-face* was the failure of the department to fulfil its undertaking to pay the purchase price. However, Merifon remained resolute in holding the municipality bound to the sale agreement. The municipality disclaimed the sale agreement despite threats of legal proceedings. Merifon then approached the High Court for relief.[20]

The Parties Submissions

The crux of the *Merifon* case was that the municipal manager was duly authorised, and acted with ostensible authority in entering into the agreement with Merifon.[21] This was a submission of real and wide substance. Cognisant of the difficulty posed by section 19 of the MFMA, Merifon contended that the relevant provision was inoperative and the agreement was valid. In the alternative, it pleaded persuasively that 'in the event it was found that section 19 was applicable, the municipality had considered the availability of funds before concluding the agreement and these funds were not committed for any other purpose.'[22]

The municipality resisted by advancing several grounds to counter Merifon's claim. First, it contended that its municipal manager lacked the requisite authority—whether actual, ostensible or otherwise to enter into a contract with Merifon.[23] Second, it pointed out that the sale agreement constituted a capital project, rendering it null and void for non-compliance because of the clear wording of section 19 of the MFMA.[24] Specifically, the purchase price for the property had never been budgeted for. Third, the municipality argued that council never approved the acquisition of land for human

19 *Merifoni II* (n 1) para 7 and *Merifoni III* (n 1) para 11.
20 ibid para 8.
21 ibid para 10.
22 *Merifon III* (n 1) para 4.
23 *Merifon II* (n 1) para 16
24 *Merifon I (*n 1) para 11.

settlement, including the total costs thereof.[25] Fourth, it was asserted that the municipality was prohibited from incurring expenditure other than that in line with 'an approved budget and within the limits of the amounts appropriated … in the budget,'[26]

In a counter-claim, the municipality sought an order declaring the contract null and void, and thus unenforceable. Alternatively, if the first counter-claim failed, the municipality sought to extricate itself by invoking the remedy of rectification.[27] Otherwise expressed, rectification of the contract was permissible because it was commonly understood by the parties that the purchase price was not to be paid by the municipality but by CoGHSTA.[28]

The High Court Proceedings

In dismissing Merifon's claim and granting the judgment in favour of the municipality, Ledwaba AJ found that the municipal manager had no authority to sign the contract on behalf of the municipality. At no stage had the municipality resolved to acquire the property, for it lacked the appropriate funds for such acquisition as its 2012/2013 annual approved budget or adjusted budget did not make provisions for such. Turning to Merifon's reliance on estoppel, the High Court (HC) held that

> failure by a statutory body to comply with the provisions which the legislature has prescribed for the validity of a specified transaction cannot be remedied by estoppel because that would give validity to a transaction which is unlawful and therefore *ultra vires*.[29]

The Supreme Court of Appeal Proceedings

Before the Supreme Court of Appeal (SCA), Merifon persisted with its argument that the sale agreement was valid as the municipality had, for all intents and purposes complied with section 19. After all, the department had confirmed the availability of the required funds (in its letter dated 6 March 2013) and pursuant to that, the municipality had adopted a resolution to acquire the property in question.[30] The question for determination was whether it was appropriate, given the factual context, for the court to grant an order of specific performance, together with consequential relief, bearing in mind section 19 of the MFMA.

25 *Merifon II* (n 1) para 19.
26 *Merifon I* (n 1) para 11.
27 See *Voltex (Pty) Ltd v First Strut (RF) Ltd* [2021] ZGPJHC 630 (5 October 2021) paras 7–12; *Tesven CC v SA Bank of Athens* 2000 (1) SA 268 (SCA) para 6.
28 *Merifon II* (n 1) para 12.
29 ibid para 13.
30 ibid para 23.

By considering the law and the facts, the SCA began by restating the ubiquitous role of the doctrine of legality and the rule of law in a nascent constitutional democracy,[31] expounded in *Fedsure Life*,[32] *Affordable Medicines Trust*[33] and *Nyathi.*[34] It stressed that state organs and public officials can never act beyond or contrary to their powers as prescribed by law. Once again section 19 of the MFMA had the practical bite. The agreement Merifon sought to enforce was plainly unenforceable for non-compliance with the prescripts of section 19.[35] Petse AP reasoned that:

> the fundamental purpose of section 19 is to prevent municipalities from spending money on capital projects that have not been budgeted for so as to safeguard that transparency, accountability as well as fiscal and financial discipline are fostered.[36]

Merifon's quest to invoke estoppel to enforce the contract also failed. Since the performance undertaken by the municipality under the impugned contract would have been unlawful, it could not be sanctioned through the remedy of specific performance.[37] It was further argued that the application of estoppel must be considered in the light of the *RPM Bricks* case.[38] Merifon also pleaded that as an innocent third party, it was entitled to assume that the municipality had complied with its internal formalities. Put differently, as an outsider it was not its responsibility to enquire whether the municipality had complied with the necessary internal processes. According to the SCA, reliance on *RPM Bricks* was misconceived. This case confirmed that

> failure by a statutory body to comply with provisions which the legislature has prescribed for the validity of a specified transaction cannot be remedied by estoppel because that would give validity to a transaction which is unlawful and therefore ultra vires.[39]

It follows that reliance on estoppel was not permissible because the requisite provisions of the MFMA were not complied with.[40] The rejection of an estoppel submission made it unnecessary for the SCA to determine the issue relating to whether the municipal manager was authorised to conclude the contract on behalf of the municipality, since

31 See generally, Chuks Okpaluba, 'The Constitutional Principle of Accountability: A Study of Contemporary South African Case Law' (2018) 33 SAPL 1 and 'Contemporary Perspectives on Constitutionalism and the Rule of Law: Reflections on South Africa's Contributions to Commonwealth Constitutional Jurisprudence' in Patrick Osode and Graham Glover, *Law & Transformative Justice in Post-Apartheid South Africa* (2010) 390–428.

32 1999 (1) SA 374 (CC) (*Fedsure*).

33 *Affordable Medicines Trust v Minister of Health* 2006 (3) SA 247 (CC) para 49 and paras 75–77.

34 *Nyathi* (n 3) para 80.

35 *Merifon II (*n 1) para 19.

36 ibid para 21.

37 ibid para 25.

38 *City of Tshwane Metropolitan Municipality v RPM Bricks (Pty*) *Ltd* 2008 (3) SA 1 (SCA).

39 *RPM Bricks* para 13.

40 *Merifon II* (n 1) paras 25 and 27.

that issue was hit by non-compliance with section 19 of the MFMA.[41] In short, the court dismissed the appeal with costs.[42]

The Reasoning of the Constitutional Court

Undeterred, Merifon appealed to the Constitutional Court (CC). At the apex court, Merifon premised its submissions on the interpretation and application of the MFMA and in particular sections 19 and 15, including the constitutional principle of legality.[43] It was submitted that the SCA erred by ruling that failure by the municipality to comply with section 19 of the MFMA rendered the contract null and void and, therefore, unenforceable. Merifon further argued that given the context and manner in which the acquisition of the enterprise was structured between the parties, sections 15 and 19 of the MFMA were inapplicable. According to Merifon, sight must never be lost that CoGHSTA was the purchaser of the property and not the municipality. The import of this submission is that the municipality would not in any way incur the expenditure for the acquisition of the land. Merifon also pointed out that section 19 was inoperative because there was no capital project under consideration. Consequently, 'there was no need for the approval of the acquisition of the property by means of a council resolution.'[44]

In the event that the CC was to rule that the operative statutory provisions were applicable, Merifon urged for an interpretive approach that would find that failure by the municipality and the department to comply with their prescripts would not invalidate the agreement entered into with an innocent third party.[45] It was emphasised that innocent parties in a similar position as Merifon are often disadvantaged when concluding contracts with municipalities, owing to a lack of knowledge of the internal applicable processes.[46] With regard to sections 26, 27, 171, 174, and 176 of the MFMA, Merifon sought to render section 19 less effective by arguing that the relevant provisions do not render a contract between a municipality and a bona fide third party unenforceable. Properly understood, 'section 19 does not place the responsibility on the bona fide third party to investigate whether the public authority in question has complied with the provisions which regulate it.'[47] The logic of this point is that innocent private actors dealing with organs of state and municipalities will be placed in jeopardy.

41 ibid para 28.
42 ibid para 30.
43 Section 15 provides that a municipality may, except where otherwise provided in the MFMA, incur expenditure only (i) in terms of an approved budget; and (ii) within the limits of the amounts appropriated for the different votes in an approved budget.
44 *Merifon III* (n 1) para 23.
45 ibid para 25.
46 ibid para 26.
47 ibid para 24.

In emphasising the basis of its principal submission, Merifon contended that the SCA should have invoked the Turquand Rule,[48] and that innocent third parties contracting with a statutory body or its agents and dealing in good faith are entitled to assume that internal formalities and procedures have been properly complied with and duly performed.[49] In addition, Merifon argued that the overriding objective of MFMA is to 'enforce internal, financial and fiscal discipline and proper financial management within the municipality' with particular penal consequences being visited upon any non-compliant functionaries.[50]

In opposing the application for leave to appeal, the municipality pointed out that the matter did not engage the CC's constitutional or generic jurisdiction. Reinforcing its principal submission, the municipality maintained that the peremptory empowering provision—section 19 dictated that it cannot act beyond its circumscribed powers.[51]

In deciding that the court's constitutional jurisdiction was engaged,[52] Mlambo AJ noted that Merifon was appealing the decision of the SCA which ruled that 'no court can compel a party to flout the law and more fundamentally, the principle of legality which is the cornerstone of our constitutional democracy.'[53]

Having said that, the CC observed that Merifon's objective was primarily to assert a specific performance claim located in a contract.[54] In finding that the interests of justice militates against granting leave to appeal, the court was dismissive of Merifon's prospects of success.[55] There was no persuasive argument why the judgment of the SCA had to be overturned. The rationale for the unanimous decision is found in para 39 where Mlambo AJ explains:

> Regarding Merifon's submissions based on the commitment letter and council resolution, one should not lose sight of another factor that testifies to the applicability of section 19, ie, that in terms of the agreement, it was the municipality that incurred the obligation to pay, not CoGHSTA. This is why Merifon issued summons against the municipality. Clearly the contractual obligation to pay was possible only if the municipality had made provision for the required budget and which, importantly, would have had to be authorised by its council through a proper resolution. There can therefore

48 The Turquand Rule was enunciated in the case of *Royal British Bank v Turquand* (1856) 6 E & B 327 and protects persons from being affected by a company's non-compliance with an internal formality pertaining to the authority of its representatives. The statutory indoor management rule is enshrined in section 20(7) and (8) of the Companies Act 71 of 2008. See also Farouk Cassim, 'Corporate Capacity, Agency and the Turquand Rule' in Farouk Cassim and others, (eds) *The Law of Business Structures* (Juta 2012) 148.

49 *Merifon III* (n 1) para 26.

50 ibid para 28

51 ibid para 24.

52 ibid para 35.

53 ibid paragraph 1.

54 ibid para 47.

55 ibid para 46.

be no question of section 19 having been complied with based on the commitments made by CoGHSTA.[56]

Commentary

Accountability, the Rule of Law and Legality

Section 1 of the Constitution of the Republic of South Africa, 1996 (the Constitution) establishes the founding values of the state. These includes as part of those values 'a multi-party system of democratic government, to ensure accountability, responsiveness and openness.'[57] Accountability is embedded in every facet of the Constitution and imposed on all holders of public office. Moreover, it bears emphasis that 'society has always been concerned about the accountability of persons or institutions who operate the levers of power.'[58] After all, 'constitutionalism, accountability and the rule of law constitute the sharp and mighty sword that stands ready to chop the ugly head of impunity off its stiffened neck.'[59]

There is an inter-connectedness between public accountability, corruption and maladministration. Public accountability reassures the citizenry of the government's protection of their rights and personal security; it is, therefore, the antithesis of corruption. Public accountability requires that persons in position of authority take responsibility for their conduct even if the action or decision taken, turns out to be wrong or unlawful. In constitutional democracies such as South Africa's public administrator and state institutions in every sphere of government, organs of state and public enterprises are guardians of the members of the public. Bearing in mind the apparent weaknesses of the human being, the founders of the Constitution thought it wise to establish such offices as that of the Public Protector ostensibly to keep a watchful eye over those same administrators and institutions entrusted with the responsibility of guarding the welfare, wellbeing and security of citizens.[60]

Constitutionalism and the rule of law remain the salient points of constitutional law. The phrase 'rule of law' is subject to contention. More important, the framers of the 1996 Constitution conceived the rule of law as an essential safety-net with larger landmarks. They envisaged a modern constitutional polity with entrenched standards of good governance and democracy. One commentator has compiled a Rosetta stone-like guide to the rule of law which includes, but is not exclusive to the following:

56 ibid para 39.
57 The Constitution s 1(d).
58 *Speaker of the National Assembly v Public Protector* 2022 (3) SA 1 (CC) para 1.
59 *Economic Freedom Fighters v Speaker, National Assembly* 2016 (3) SA 580 (CC) para 1. For a helpful analysis, see Mtendeweka Mhango and Ntombizozuko Dyani-Mhango, 'The Powers of the Public Protector: A Note on the *Economic Freedom Fighters v Speaker of the National Assembly*' 2020 AJLS 1–20.
60 Okpaluba (n 31) 3.

- that governmental powers can only be exercised in accordance with the law, not arbitrarily or capriciously. This means that every act of government or its officials must have a valid foundation in the law and that its actions, the government or authority must not exceed its powers or act without constitutional authority;

- that the exercise of governmental acts must be subject to review by the courts of law, so that, it is not in the spirit of the rule of law for the legislature to enact laws that take away the ordinary jurisdiction of the courts; there must be access to the court for the ventilation of disputes and grievances;

- that each organ of state must treat the other with respect, especially, the executive must not only respect the due process of law but must also treat the judgments of courts of competent jurisdiction with uttermost respect. This entails the absence of resort to the use of brute force or self-help as against using the judicial process to settle disputes;

- that as a consequence of the foregoing, the constitutional state must ensure the independence and impartiality of the judiciary, the organ of government with which the settlement of disputes between the government and its citizens is entrusted;

- that the law should conform to certain minimum standards of justice, both substantively and procedurally;

- that every person including public functionaries and officials are equal before the law, so that public officials are subject to effective legal sanctions, like other citizens; and that government officials, except with the express authorisation of the law, must not discriminate against citizens in respect of public privileges and rights; and

- that the state itself is subject to law. For instance, it is beyond the state to purport by way of a policy decision to alter the right that a citizen has acquired by virtue of the Constitution, nor could the legislature give effect to such policy by way of legislation without following the due process of amending the Constitution.[61]

The norm of accountability is further underscored by the ubiquitous principle of legality. Legality is instrumental in ensuring that the exercise of all public power is subject to constitutional control.[62] It behoves the courts if called upon to do so to determine whether or not power has been exercised consistently with the requirements of the

61 Chuks Okpaluba, 'Constitutionality of Legislation Relating to the Distribution of Governmental Powers in Namibia: A Comparative Approach' in Manfred Hinz, Sam Amoo & Dawid van Wyk (eds), *The Constitution at Work: Ten Years of Namibian Nationhood* (VerLoren van Themaat Centre for Public Law Studies, University of South Africa 2003)116–118.

62 *Pharmaceutical Manufacturers Association of South Africa: In re Ex parte President of the RSA* 2000 (2) SA 674 (CC) para 79. *Minister of Health v New Clicks SA (Pty) Ltd* 2006 (2) SA 311 (CC) para 313 (*New Clicks SA*).

Constitution and the law.[63] Crucially, however, legality occupies front benches in the appellate courts.[64]

The *Merifon* judgments demonstrate that accountability and legality play a decisive role in the judicial scrutiny of exercises of public power. Mlambo J at the outset of his judgment underlined the settled proposition that

> an important foundation of our constitutional democracy is the doctrine of legality, a subset of the rule of law.…The exercise of public power must strictly comply with ordained prescripts, and that failure to observe this contravenes the doctrine of legality.'[65] That principle is vouched by the opening statement of Petse AP that 'the doctrine of legality and the rule of law lie at the heart of the Constitution.'[66] It is accepted that 'a local government may only act within the powers lawfully conferred upon it by a legislation.[67]

Legality constituted a material consideration in obliterating Merifon's prospects of success, when bearing in mind that it was simply impermissible for the municipality to enter into an agreement involving a capital project in contravention of explicit prescripts of section 19 of the MFMA.

Estoppel and the Turquand Rule

The correlation between the doctrine of estoppel and the Turquand Rule is recognisable. It has been said that estoppel and the indoor management rule are opposite sides of the same coin.[68] Although estoppel is entrenched in South African law,[69] the concept originated in English law. The essence of 'untechnical,' the defence of estoppel,[70] is that the party resorting to estoppel must prove that, by reliance on the other's conduct, he or she has suffered prejudice, and that he or she acted reasonably in relying on the representation.[71] The converse is true, in that a party who knows the true state of affairs of a business partner cannot aver that they were induced to act according to their

63 *New Clicks SA* para 313; *National Director of Public Prosecutions v Zuma* 2009 (2) SA 277 (SCA) paras 15-16.

64 See generally, *Buffalo City Metropolitan v Asla Construction (Pty) Ltd* 2019 (4) SA 331 (CC); *State Information Technology Agency Soc Ltd v Gijima Holdings (Pty) Ltd* 2017 (2) SA 63 (SCA); *Merafong City Local Municipal v AngloGold Ashanti Ltd* 2017 (2) SA 211 (CC).

65 *Merifon III* (n 1) para 1.

66 *Merifon II* (n 1) para 1.

67 *Fedsure Life* para 56.

68 See *One Stop Services (Pty) Ltd v Neffesaan Ontwikkelings (Pty) Ltd* 2015 (4) SA 623 (WCC) paras 23–29.

69 Richard Christie and Graham Bradfield, *Christie's The Law of Contract in South Africa* (6th edn, Lexis Nexis 2011) 28. See also *Makate v Vodacom (Pty) Ltd* 2016 (4) SA 121 CC) paras 49–50. See also Tumo Maloka, 'The Turquand Rule, Irregular Appointments and Bypassing the Disciplinary Process' (2017) SA Merc LJ 533.

70 Jean Sonnekus, *The Law of Estoppel in South Africa* (2nd edn, Lexis Nexis 2012) 171.

71 See *Captick-Dale v Fibre Solutions (Pty) Ltd* (2013) 34 ILJ 129 (LC) para 17.

prejudice, based on a representation.[72] If the defence of estoppel prevails, it has the effect that the incorrect impression is maintained as if it were correct.[73] It should be appreciated that the person who has been misled may raise estoppel only if the other party has raised the correct facts.[74] To sum up, a reliance on estoppel is thwarted by the proposition that estoppel cannot operate in a way which brings about a result not permitted by law.[75]

The indoor management rule postulates that bona fide third parties should not be prejudiced by a company's non-compliance with its internal formalities and procedures, because to inquire into the company's arcane internal affairs is impractical, if not risky.[76] To drive the point home,

> … persons contracting with a company and dealing in good faith may assume that acts within its constitution and powers have been properly and duly performed and are not bound to inquire whether acts of internal management have been regular.[77]

The rule is intended for the protection of outsiders who have no means of establishing whether the necessary formalities and procedures in terms of the company's constitution have been satisfied.[78]

It must be remembered that at the core of Merifon's estoppel and Turquand submissions was that private actors acting in good faith when negotiating with state organs were entitled to presume that internal formalities and statutory prescripts have been followed. More importantly, Merifon stressed that as an innocent private party it was not incumbent on it to investigate whether the municipality had complied with the necessary internal processes. Their argument was that it was thus patently unfair to invalidate an agreement concluded with an innocent third party because of the municipality's failure to obtain proper, fitting and effective council approval for a capital project as mandated by section 19 of the MFMA. Broadly stated, fulfilment of executive obligations in terms of the Constitution.[79]

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72 See eg *Blue IQ Investment Holdings Ltd v Southgate* (2014) 35 ILJ 3326 (LAC); *Hudson v SA Airways* (2015) 36 ILJ 2574 (LAC).

73 Schalk Van der Merwe, *Contract: General Principles* (4th edn, Juta 2012) 29.

74 At para 45 in *Makate* Jafta J observes that 'estoppel is not a form of authority but a rule to the effect that if the principal had conducted herself in a manner that misled the third party into believing that the agent has authority, the principal is precluded from denying that the agent had authority.'

75 See *HNR Properties CC v Standard Bank of SA Ltd* 2004 (4) SA 471 (SCA) 480A.

76 See for eg *East Asia Co Ltd v PT Satria Tirtata Energindo (Bermuda)* [2019] UKPC 30 para 62–65.

77 *Halsbury's Laws of England* (2nd edn), vol V, 423, cited in *Morris* 474.

78 The Companies Act 71 2008 s 20(7). See also Farouk Cassim and others (n 48) 183; Rehana Cassim, 'Corporate Capacity, Agency and the Turquand Rule' in Cassim and others (eds), *The Law of Business Structures* (Juta 2012) 136.

79 *Premier, Gauteng v DA* 2022 (1) SA 16 (CC) paras 65–69 *New Clicks SA* (n 62) para 613; *Pharmaceutical Manufacturers Association of SA: In Re Ex Parte President of the RSA* 2000 (2) SA 674 (CC) para 33.

The common thread running through the three judgments is that a reliance on estoppel and the indoor management rules is highly constrained by the proposition that they cannot operate in a way which brings about a result not permitted by law.[80] The judgment at first instance found that reliance on estoppel to bypass legislative prescripts was misconceived. The municipality's non-compliance with statutory prescripts cannot be remedied by estoppel. To do otherwise, would be to accord validity to a transaction which is unlawful and therefore *ultra vires*.'[81]

In rejecting Merifon's substantive submissions, Petse AP observed and noted that sight must never be lost that:[82]

> [I]t was plainly impermissible for the municipality to enter into an agreement involving a capital project contrary to the prescripts of s 19. This being the case, it must ineluctably follow that this Court cannot grant the order for specific performance sought by *Merifon* in this litigation. To do so in the face of the clear provisions of s 19 would, as Innes CJ said in *Schierhout v Minister of Justice* 1926 AD 99 at 109, be tantamount to granting the court's imprimatur to something proscribed by the law. The reason for this principle is self-evident: no court can compel a party to flout the law and, more fundamentally, the principle of legality which is the cornerstone of our constitutional democracy. And sight should never be lost of the fact that in exercising their judicial functions, courts are themselves constrained by the principle of legality.[83]

Given the context-specific circumstances of the present case, reliance on estoppel as articulated in *RPM Bricks* was flawed. In any event, validating irregular acquisition of land through the instrument of estoppel would have undermined the applicable provisions.[84] In this respect 'the principle of legality was manifestly implicated in the action of the municipality and was at odds with the dictates of section 19.'[85] Having regard to the above considerations, the SCA emphasised that the usage of estoppel would have negated the underlying purpose of the MFMA, which is to promote transparency, accountability and good governance within the local sphere of government.

The CC endorsed the decisions of the HC and SCA unanimously. The doctrine of legality completely eclipsed Merifon's contention which was predicated on estoppel and Turquand. At para 43 Mlambo AJ referred to the fact that

> the conclusions of the SCA regarding the applicability of section 19, and the force of the principle of legality, are based on settled jurisprudence … Simply put, the transaction for the acquisition of the property entailed a capital project as it implicates the

80 See *HNR Properties CC v Standard Bank of SA Ltd* 2004 (4) SA 471 (SCA) 480A.
81 *Merifon II* (n 1) para 13.
82 ibid para 29.
83 *National Director of Public Prosecutions v Zuma* 2009 (2) SA 277 (SCA) paras 15-16.
84 *RPM Bricks* para 13.
85 *Merifon II* (n 1) para 27.

> acquisition of a capital asset. The MFMA's provisions, in particular sections 15 and 19, are peremptory and they required that the Municipality comply with them before concluding the agreement with *Merifon*.

As to the last contention raised by Merifon regarding the failure of the municipality to review its conduct after concluding an invalid agreement relying on *Merafong*[86] and *Tasima*,[87] Mlambo AJ was persuaded that a reactive challenge was available to the municipality. Authorities have made it clear that a reactive challenge 'should be available where justice requires it to be.'[88] Thus it follows that an organ of state is 'not disqualified from raising a reactive challenge merely because it is an organ of state.'[89] The approach was most conveniently summarised in *Qaukeni*,[90] where it was held that

> [i]f the second respondent's procurement of municipal services through its contract with the respondent was unlawful, it is invalid, and this is a case in which the appellants were duty bound not to submit to an unlawful contract but to oppose the respondent's attempt to enforce it. This it did by way of its opposition to the main application and by seeking a declaration of unlawfulness in the counterapplication. In doing so it raised the question of the legality of the contract fairly and squarely, just as it would have done in a formal review. In these circumstances, substance must triumph over form. [91]

Conclusion

Beyond the narrow issue of whether estoppel or the Turquand Rule can be invoked to override the mandatory provisions of section 19 of the MFMA, *Merifon* underscores accountability as a transcendental constitutional norm. There can be no criticism about the factual findings or the re-affirmation of the constitutionally embedded norm of accountability and the all-encompassing principle of legality by the HC, SCA and CC. The conduct of the municipal manager and council was at variance with the normative value system reinforcing the constitutional order. It is significant that the case illustrates that the prejudice does not lie with the harm suffered by the municipality or *Merifon*, but in the continued lack of provision of low-cost housing to the people and communities the municipality is supposed to serve. Ironically, the people who may suffer the real harm are often not party to the proceedings.[92]

It cannot be stressed enough that neither estoppel nor the Turquand Rule can be raised by innocent private actors to enforce agreement that were concluded in breach of statutory prescripts. Given the suffocating grip of pathological deficiencies of

86 *Merafong City v AngloGold Ashanti Ltd* 2017 (2) SA 211 (CC).
87 *Department of Transport v Tasima (Pty) Ltd* 2017 (2) SA 622 (CC).
88 *Merafong* (n 86) para 55. See also Okpaluba (n 31) 15–16.
89 *Tasima* (n 87) para 140.
90 *Municipal Manager Qaukeni Local Municipality v FV General Trading CC* 2010 (1) SA 356 (SCA).
91 ibid para 26.
92 *Ngaka Modiri Molema District Municipality v Chairperson, North West Provincial Executive Committee* 2015 (1) BCLR 72 (CC) para 9; *Premier, Gauteng* para 51.

governance in present-day South Africa, the *Merifon* case is neither the first, nor the last that the bench will have to grapple with regarding issues of malfeasance in public office.[93]

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93 See *Esorfranki Pipelines (Pty) Ltd v Mopani District Municipality* [2022] ZACC 41 (30 November 2022); *MEC Responsible for Local Government, Western Cape v Mtazikama Local Municipality* [2022] ZASCA 167 (30 November 2022); *Sekoko Mametja Incorporated Attorneys v Fetakgomo Tubatse Local Municipality* [2022] ZASCA 28 (18 March 2022).

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