

THE INTERPRETATION AND EFFECT OF SECTION 197 OF THE LABOUR RELATIONS ACT 66 OF 1995

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Declaration

I, the undersigned, hereby declare that the work contained in this thesis is my own original work and that I have not previously in its entirety or in part submitted it at any other university for a degree.

ABSTRACT

Section 197 of the Labour Relations Act 66 of 1995 ensures the transfer of a contract of employment from an old employer to a new employer on the transfer of a business as a going concern.

Although section 197 is mostly based on European and British statutes and regulations, one should not rely on foreign provisions when interpreting section 197 without careful consideration. It is only when we understand the inherent limitations of applying these provisions, that they can be of any help to formulate definitions for the terms “transfer”, “business” and “going concern”.

The two most important effects that section 197 has, is that it ensures the transfer of the contract of employment and that it protects the terms and conditions of employment when such a transfer takes place. Unfortunately, this section does not regulate dismissal on the transfer of a business. Section 197 also does not deal satisfactorily with the transfer of contracts of employment on the transfer of an insolvent business.

As a result of the above-mentioned and other shortcomings of the current section 197, it was decided to amend the Act. The Labour Relations Amendment Bill 2000 relies heavily on precedents from foreign law, but unfortunately it does not adequately address all the current problems.

OPSOMMING

Artikel 197 van die Wet op Arbeidsverhoudinge 66 van 1995 verseker die oordrag van 'n dienskontrak van 'n ou werkgewer na 'n nuwe werkgewer by die oordrag van 'n besigheid as 'n lopende onderneming.

Alhoewel artikel 197 gebaseer is op Europese en Britse wetgewing en regulasies, moet die leser versigtig wees om sulke bepalings sonder skroom aan te wend by die interpretasie van artikel 197. Wanneer ons die inherente beperkings daarvan begryp, mag die bepalings van hulp wees om definisies te vorm van die begrippe “oordrag”, “besigheid” en “lopende onderneming”.

Artikel 197 het hoofsaaklik twee uitwerkings: dit fasiliteer die oordrag van die dienskontrak en verseker dat die terme en voorwaardes van indiensneming onveranderd bly. Die artikel reguleer nie ontslag by die oordrag van 'n besigheid nie. Artikel 197 reguleer ook nie genoegsaam die oordrag van dienskontrakte waar 'n insolvente besigheid oorgedra word nie.

As gevolg van bogenoemde en ander tekortkominge is besluit om die Wet te wysig. Die Wysigingswetsontwerp op Arbeidverhoudinge 2000 steun op buitelandse presedente, maar spreek ongelukkig ook nie al die huidige probleme suksesvol aan nie.

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CHAPTER 1

THE INTERPRETATION AND EFFECT OF SECTION 197 OF THE LABOUR RELATIONS ACT 66 OF 1995

1 INTRODUCTION

What are the consequences for employees and their contracts of employment when the business is transferred? Why would the common law prevent the automatic transferral of the contracts of employment with the rest of the business? A simple answer to these questions would be that slavery was abolished in South Africa many years ago. Today, employers and employees are bound by a contract of employment – a private relationship between these two parties. Unfortunately the common law prevents the unilateral assignment of certain rights and all obligations flowing from this contract to anyone else.¹ The transferral of the business would therefore lead to the termination of the contracts of employment² and only the novation of the contract or an offer of re-employment from the new employer could ensure any continuity of employment.

This common law position is problematic for two reasons. Firstly, it is clearly incompatible with modern legal principles of employment protection. Secondly it fails to provide for an effective mechanism to encourage the restructuring of businesses, without which it is difficult to survive in the modern internationally competitive environment. As a result many nations have opted to alter their common law by passing legislation ensuring the automatic transfer of the contract of employment. In South Africa such legislation was passed in the form of section 197 of the Labour Relations Act.³

¹ *Eastern Rand Explorations Co v Nel* 1903 TS 53A

² Based on the redundancy of the employees.

³ 66 of 1995

2 THE WORKINGS OF SECTION 197

Section 197 provides the following:

"197 Transfer of contract of employment

(1) A contract of employment may not be transferred from one employer (referred to as 'the old employer') to another employer (referred to as 'the new employer') without the employee's consent, unless-

(a) the whole or any part of a business, trade or undertaking is transferred by the old employer as a going concern; or

(b) the whole or a part of a business, trade or undertaking is transferred as a going concern-

(i) if the old employer is insolvent and being wound up or is being sequestrated; or

(ii) because a scheme of arrangement or compromise is being entered into to avoid winding-up or sequestration for reasons of insolvency.

(2)(a) If a business, trade or undertaking is transferred in the circumstances referred to in subsection (1)(a), unless otherwise agreed, all the rights and obligations between the old employer and each employee at the time of the transfer continue in force as if they were rights and obligations between the new employer and each employee and, anything done before the transfer by or in relation to the old employer will be considered to have been done by or in relation to the new employer.

(b) If a business is transferred in the circumstances envisaged by subsection (1)(b), unless otherwise agreed, the contracts of all employees that were in existence immediately before the old employer's winding-up or sequestration transfer automatically to the new employer, but all the rights and obligations between the old employer and each employee at the time of the transfer remain rights and obligations between the old employer and each employee, and anything done before the transfer by the old employer in respect of each employee will be considered to have been done by the old employer.

- (3) An agreement contemplated in subsection (2) must be concluded with the appropriate person or body referred to in section 189 (1).
- (4) A transfer referred to in subsection (1) does not interrupt the employee's continuity of employment. That employment continues with the new employer as if with the old employer.
- (5) The provisions of this section do not transfer or otherwise affect the liability of any person to be prosecuted for, convicted of, and sentenced for, any offence."

As a point of departure section 197 acknowledges the common law position requiring the consent of the employee before the contract of employment can be transferred. However, where a business is transferred *as a going concern*, the contracts of employment are automatically transferred along with the business, while the terms and conditions of the contract are also maintained, unless the parties agree otherwise. This provides for continuity of employment.

The section also makes a distinction between the normal transferral of a business and the transferral of the business as a result of insolvency or a rescue of undertakings procedure. In the case of the former, the new employer simply steps into the shoes of the old employer, taking over all his rights and obligations. In the latter cases, the new employer does not acquire the rights and obligations of the old employer at all.

While section 197 effectively provides for the automatic transfer and the maintenance of the terms⁴ of the contract of employment where a business is transferred as a going concern, ironically, this does not necessarily provide for greater job security in practice. Employees are still faced with retrenchment⁵ prior to such a transfer, simply because employers might prefer to avoid this section.⁶ Neither does the section cast the terms of the contract in stone – an employee might well find herself forced to oblige to reasonable changes.⁷

⁴ The terms of the contract may only be varied by agreement between the employer (most probably the new employer) and the parties listed in s189(1).

⁵ Based on operational requirement as defined in s213. The merit of such an approach will be considered in chapter 5.

⁶ Blackie & Horwitz "Transfer of Contracts of Employment as a result of Mergers and Acquisitions: A Study of Section 197 of the Labour Relations Act 66 of 1995" 1999 20 *ILJ* 1395

⁷ s196(3) of the Labour Relations Act states that an employee who unreasonably refuses to accept an offer of alternative employment with the current employer or another employer will not be entitled

Despite all this, the section does go a long way towards recognising the unique relationship that employees have with the business itself.⁸ The real success of section 197, lies in the effective mechanism that it provides for South African companies to restructure without being hampered by unnecessary costs and time-consuming procedures. The key objective is therefore to improve – or save – the competitive position of the business.

As restructuring is a modern reality in South Africa, be it in the form of privatisation, land reform, take-overs, mergers or out-sourcing, there is no doubt that the increased flexibility that section 197 brings to these processes would have a beneficial effect on the economy. It would follow that any attempts to increase the effectiveness and correct interpretation of such legislation should have the same result.

3 IDENTIFYING THE PROBLEM

From the above, it is clear that the section attempts to regulate a situation where the tension between commercial interests and social policy for the employee is often at its highest.⁹ Given the importance of such regulation, it is regrettable that this provision is so brief.¹⁰ When we consider just how new this provision is to South Africa in the first place, it seems inevitable that such brevity would result in problems.

Despite all its advantages, section 197, has therefore not escaped criticism, some of it well founded. Even before the Act was passed, Olivier pointed out several shortcomings of the clause 92 of the Draft Bill.¹¹ While most of his criticism was aimed at the uncertainty surrounding the interrelationship between the provision and section 38 of the Insolvency Act, he also noted correctly that there were no provisions ensuring information sharing, consultation or the transferral of collective rights. Strangely enough, these deficiencies were also not addressed in section 197; but while

to severance benefits.

⁸ The gist of s197 is that the contract of employment is preserved, irrespective of the change in employer, when the identity of the business stays the same. In fact, the section places such a strong emphasis on the business, which it might even be considered as a partial recognition of the business as the third party to the employment relationship.

⁹ *Schutte v Powerplus Performance (Pty) Ltd* 1999 ILJ 664A-C

¹⁰ This general lack of detail is also clearly illuminated when s197 is compared to foreign legislation that varies from 4 sections in the Industrial Relations Act of 1996 (New South Wales) (s 101–104) to separate and comprehensive attempts at codification, as is the case with the Transfer of Undertakings (Protection of Employment) Regulation of 1982 in the UK.

¹¹ Olivier “Transfer of Undertakings and Insolvent Employers: A Comparative Enquiry and Implications for South African Labour Law” 1995 *Tydskrif vir Suid Afrikaanse Reg* 746-750

this might seem serious, it is a problem that can quite easily be remedied by an amendment to the Act, as will happen in the near future.

On the 27th of July 2000 the Labour Relations Amendment Bill was published in the Government Gazette.¹² The proposed new section 197 is much more detailed and addresses many of the problems that currently exist. The interpretation of this extended piece of legislation and how it would affect the current status of section 197 if it were to be enacted within the next few years would necessarily form part of the subject of scrutiny in this thesis.

Despite any amendments, section 197 is by its very nature plagued by another serious and far more persistent problem: general uncertainty about the interpretation and extent thereof. Such uncertainty is unfortunately not necessarily an issue that the legislator can address, as Thompson points out:

"Even the most carefully articulated legislation cannot produce certainty. And language being what it is, the very attempt to write policy generates its own ambiguities."¹³

Instead of legislative intervention in this area, it would therefore clearly be more productive to rely on the courts to apply the law in an attempt to create more certainty. A lack of reported case law on section 197 has, however, delayed this process. As a result, certainty about its interpretation and application would for the time being have to be arrived at in some other way. It is the aim of this thesis to contribute to this process.

4 METHODOLOGY

To determine the point of departure for this study, it would be helpful to turn to Thompson once more.

"The Labour Relations Act grapples with the policy issues and makes choices. However, not all the issues are addressed, and those that are, are not always addressed clearly. The Act may be cagey or elliptic on an issue, but in practice of course it simply arises, and must then be dealt with. One then has to infer the answer from the basic design of the law [and] attempt to interpret the

¹² No 21407

¹³ Thompson "Bargaining, Business Restructuring and the Operational Requirements Dismissal" 1999 20 *ILJ* 756

statute's signs and silences to arrive at a coherent picture on the boundaries of power, prerogative and law."¹⁴

It seems obvious that if we are uncertain about the workings and interpretation of a provision of an act, the first course of action would be to turn to the act itself to provide an answer. There are several convincing arguments¹⁵ that suggest that section 3 of the Labour Relations Act also point us towards an analysis of foreign law. As section 197 was inspired by foreign legislation in the first place, this thesis will therefore contain an analysis of foreign jurisprudence. Since it appears from the Amendment Bill that future amendments to section 197 might be based largely on the European Directive, problems that have arisen in the European Community in this regard will also be closely scrutinised.

The following methodology will be applied in each chapter of the thesis.

Chapter 2 will contain a brief analysis of the statutory position before 1996. This will be followed by an analysis of the common law position, with specific reference to the problems that it created for the employer and employee. Finally, the origins of section 197 will be retraced. The value of the above will be to illustrate exactly how and why problems arose with regard to the interpretation of section 197.

Chapter 3 will describe the value of foreign jurisprudence in the South African context. The different provisions within the European Community that have inspired the South African model will be scrutinised and the differences and similarities between these and other models and section 197 will be studied in order to evaluate their relevance.

In Chapter 4 an attempt will be made to clarify the terms of section 197 by applying current South African labour and commercial law, keeping in mind the principles established in foreign jurisdictions. The current definitions of these terms will also be clarified and the thesis will attempt to show how the definitions advocated by the Amendment Bill would influence the current position.

The various effects of section 197 on the employment relationship will be discussed at length in chapter 5. To this end, the interaction between section 197 and current labour law issues and developments will be studied.

¹⁴ Thompson 1999 20 *ILJ* 756

¹⁵ Blackie and Horwitz 1999 20 *ILJ* 1388

Chapter 6 will contain a critical analysis of the insolvency and rescue operations provisions included in section 197. The shortcomings of these provisions will be identified. Also, this chapter will contain an analysis of how the Amendment Bill proposes to remedy this position. The merit of these propositions will be discussed. Finally, the most important findings of this thesis will be summarised in Chapter 7.

CHAPTER 2

THE ORIGINS OF SECTION 197 AND FUTURE AMENDMENTS

1 THE STATUTORY POSITION BEFORE 1995

Before 1995 there was no general statutory protection for employees at the time of the transfer of the employer's business. Limited continuity of employment was provided by section 22(5)(a) of the Manpower Training Act¹⁶ as well as section 12 of the Basic Conditions of Employment Act.¹⁷ The former provided for the automatic transfer of contracts of apprenticeship entered into with a partnership in the case of the partnership being dissolved and the business being transferred. The latter ensured the transferral of an employee's accrued leave benefits in the event of the transfer of a business provided that the new employer re-employed the employee.

1.1 COMMON LAW

At common law the automatic transferral of a contract of employment was impossible as the transferral of the contract necessitated the consent of the employee.

1.1.1 CONSENT OF THE EMPLOYEE

Different common law rights and obligations flow from the contract of employment. The employer, for example, has the right to demand the service of the employee, while the employee has the right to demand payment for these services rendered. While rights can usually be ceded at common law without the debtor's consent,¹⁸ there are some exceptions.¹⁹ One such exception necessitates the consent of the debtor in the case of the cession of a right of which it can fairly be inferred that the debtor, in conferring the right on the creditor, intended it to be exercised by him personally. This would be the case where the right is of such a personal nature that it can make a substantial or reasonable difference if the cedent or the cessionary enforces it.²⁰ The right of the employer to demand service from the employee falls into this category.

¹⁶ 56 of 1981

¹⁷ 3 of 1983

¹⁸ Eg an employee may freely cede her right to wages, subject to certain conditions – see Christie *The Law of Contract in South Africa* (1996) 517

¹⁹ For examples refer to Lubbe & Murray *Contracts: Cases, Materials and Commentary* (1988) 654 and Christie *supra* 515-516

²⁰ *Eastern Rand Explorations Co v Nel* 1903 TS 53

The cession of this right would thus require the consent of the employee, because the courts accept that the employee does “attach importance to the identity of the particular company with which they deal.”²¹ Furthermore, as the employee is subjecting herself to some extent to the control and authority of the employer, it is even more essential that she should be the one to decide who her employer should be.²²

But mere cession of the rights flowing from a contract of employment would not be enough to transfer it. As obligations are transferred by way of delegation²³, a combined process of session and delegation²⁴ -which is a form of novation - is called for.

1.1.2 NOVATION²⁵

The process of novation requires the consent of all the involved parties: the old employer, new employer and employee. By way of agreement, the old contract is brought to an end and replaced with a new contract. The consent of the employee is therefore needed for the substitution of the old employer with the new employer and for any changes made to the terms of the contract. Not surprisingly, this form of the transferral was almost never used in practice,²⁶ as employers elected to use a simpler process: the unilateral termination of the contract of employment.

1.1.3 UNILATERAL TERMINATION OF CONTRACT

The contract of employment was not automatically terminated at the time of the transfer of the business.²⁷ Instead, on the sale of the assets of the business, the employer could unilaterally terminate the contract²⁸ of employment due to the redundancy of the employee. In such a case, the normal procedures for the bona fide termination of the

²¹ *Nokes v Doncaster Amalgamated Collieries* 1940 AC 1014

²² *Eastern Rand Exploration Co v Nel supra* 53

²³ *Christie supra* 513-515

²⁴ 523-524

²⁵ 498

²⁶ There is only one reported case where the industrial court dealt with a transfer by way of novation: *Roshanlall v Design Three* 1989 ILJ 1162 (IC)

²⁷ Jordaan "Transfer, Closure and Insolvency of Undertakings" 1991 12 5 ILJ 947-948 argues convincingly that a contrary finding by the industrial court in *NUMSA v Metkor Industries* 1990 ILJ 1116 (IC) was based on an incorrect interpretation of *Ntuli v Hazelmores Group* 1988 ILJ 709 (IC).

²⁸ In *NUMSA v Metkor Industries supra* 1120C the industrial court did however find correctly that the termination of the contract did not effect collective agreements “in so far as any provisions for the termination [of employment] are concerned.”

contracts of employment would have to be followed in keeping with the guidelines provided by the industrial court at that time.²⁹

The procedures would also depend on the type of contract. In the case of an indefinite period contract, the unilateral termination of the contract would necessitate a notice of termination to provide the employee with “sufficient time in which to regulate his own affairs”.³⁰ In the case of a fixed period contract, however, it would not be possible to terminate the contract unilaterally, except in the case of a serious breach of contract. Lacking this, the unilateral termination would result in a repudiation of the contract, even in the case of an offer of re-employment.³¹

1.1.4 OFFER OF RE-EMPLOYMENT

On the transfer of a business, the termination of the contract of employment would usually be accompanied by an offer of re-employment from the new employer. The new employer was, however, not compelled to make such an offer, except in the case of an expressed undertaking or a created expectation.³² In the absence of such an offer, the employee would be redundant and would have to look to the old employer for compensation.

Although employees were not compelled to accept such an offer of re-employment, anyone who declined an offer of re-employment on the same terms³³ was not entitled to compensation, except where there was sound reason for such a refusal.³⁴ To provide for the informed consent of the employee in such cases, it was necessary to provide for a process of consultation.

²⁹ *NUTW v Braitex* 1987 ILJ 1127 (IC), *PPWAWU v Kaycraft* 1989 ILJ 272 (IC), *NUMSA v Metkor Industries* *supra* 1116.

³⁰ *Putco v Radio Guarantee Co* 1985 4 SA 809 (A)

³¹ *Isaacsohn v Walsh & Walsh* 1903 SC 569

³² In *Ntuli v Hazelmores Group* *supra* 719C-D the industrial court decided that a “reasonable expectation” for re-employment was created when the employer retained the services of an employee “sufficiently long to demonstrate that the employees may safely look to the transferee for security of tenure.”

³³ *Ntuli v Hazelmores Group* *supra* 709 (C.f. *Young v Lifegrow* 1990 ILJ 1127 (IC). In this case the industrial court decided that the termination of the contract of employment coupled with an offer of re-employment on the same terms *did not constitute retrenchment* and that employees who therefore refused the offer would not be entitled to compensation.)

³⁴ *Ntuli v Hazelmores Group* *supra* 719I

1.1.5 CONSULTATION

In *NUTW v Braitex*³⁵ the industrial court recommended that in order to minimise the negative effects that a transfer of business could have on employees, tripartite negotiations (involving the old employer, new employer and the employees) should be called for prior to the transfer being completed. In another instance³⁶ the court stated that the purpose of this process of consultation was "to discuss the measures which are to be taken to protect the interest of the employees and the preservation of the employment relationship notwithstanding the change of ownership of the business". On one occasion the court even went as far as to suggest that the purchaser also had a **duty** to consult with the employees by stating that

“[t]he transferee should also be involved in these consultations or at least consult separately with the employees and their unions”.³⁷

Despite all of this, Du Toit³⁸ rightly pointed out that the industrial court never went as far as to provide employees with a right to continued employment at the time of the transfer of a business.³⁹ The closest the industrial courts ever came to this was in *Kebeni*,⁴⁰ when it provided that the agreement of the assets of the old employer should incorporate some clause to safeguard the rights of the employees.

1.1.6 CONCLUSION

In the light of all the above, it is clear that there was always a close link between the transfer of a business at common law and the termination of the contract of employment resulting in the dismissal of employees. This was such an intimate relationship in fact, that the reason why the transfer of businesses was ever problematic in the first place – from the viewpoint of the employee - was due to the lack of statutory guidelines for dismissal. It is with this particular problem in mind that writers like Jordaan (1991: 964) called for statutory reform.

Their wish was granted in 1996 with the passing of the new Labour Relations Act.⁴¹

³⁵ 1987 ILJ 794 (IC)

³⁶ *Kebeni v. Cementile Products (Ciskei)* 1987 1LJ 442 (IC)

³⁷ *Ntuli v. Hazelmere Group supra* 719E

³⁸ Du Toit et al *Labour Relations Law: A Comprehensive Guide* (2000) 398

³⁹ The only remedy was an application in terms of s17(11)(a) of the Labour Relations Act 28 of 1956.

⁴⁰ *supra* 442

⁴¹ 66 of 1995

2 LABOUR RELATIONS ACT 66 OF 1995

The new Labour Relations Act sought to address many issues.⁴² Of most importance here, is chapter eight, which regulates the fairness of dismissals, and more particularly the last section of this chapter, section 197, which regulates the transfer of the contracts of employment on the transfer of a business.

On 9 August 1994 a Ministerial Legal Task Team was appointed to draft a new Labour Relations Act. This team produced a draft Labour Relations Bill, in the form of a negotiating document with an attached explanatory memorandum. On 10 February 1995 the Minister of Labour published this draft bill in a schedule to a General Notice in the Government Gazette.⁴³

Clause 92 of this schedule provided for the transfer of employment rights and obligations at the time of the transfer of an undertaking as a going concern - a major shift away from the common law position. The accompanying Explanatory Memorandum explained the reasoning behind this shift:

"The draft Bill explicitly deals with the employer's rights and obligations in the event of a transfer of undertaking. This resolves the common law requirement that existing contracts must be terminated and new ones entered into, which leads to the retrenching of employees, the paying of severance benefits etc and escalates costs in a way that inhibits these commercial transactions. Provision is made in the draft Bill for the automatic transfer of contracts of employment to the transferee provided the employees consent to the transfer. All rights and obligations arising from the contract of employment are transferred. In the case of insolvency, however, the transferee will be responsible for settling claims arising from the employment contracts up until the date of the transfer. The transferee takes over the contracts of employment, but is only responsible for wages and claims arising from date of transfer. The purpose of this proviso is to avoid what might otherwise be an adverse effect to the liquidator's ability to dispose of the undertaking."

⁴² s1 of the Act proclaims that the purpose of the act is to pursue economic development, social justice, labour peace and the democratisation of the workplace.

⁴³ 16259

While the provisions ensuring fair dismissal were clearly to be included in the Act to protect the rights of the employee, it seems that the provisions providing for the automatic transfer of the contracts of employment were to be included to promote business. As Froneman DJP explains in *Foodgro v Carol Keil*:⁴⁴

The ease or otherwise, with which businesses, trades or undertakings may be transferred, and the consequences flowing from these transfers for employers and employees alike may be very important for the economic well being of a country. There may indeed be very good economic reasons why the free and unrestricted transfers of businesses, trades and undertakings will promote commercial efficiency and thus ultimately promote economic development.⁴⁵

While the promotion of restructuring is laudable, it is inevitable that such a process would lead to the dismissal of employees. It is striking therefore, that the clause made no attempt to regulate such dismissals prior to a transfer, opting instead that the fairness of such dismissals be regulated under the wider auspices of operational requirements.

The Notice also included an invitation for all interested parties to submit written comment on the Draft Negotiating Document as soon as possible. Considering the published criticism⁴⁶ of the shortcomings of clause 92, however, it is quite surprising that it found its way into the new Labour Relations Act, mostly unchanged,⁴⁷ in the form of section 197.

3 LABOUR RELATIONS AMENDMENT BILL 2000

Following the initial confusion and general lack of interest about section 197, it became clear after only a few years that the section contained several shortcomings. Various articles in law journals as well as a few labour court judges called for the amendment of certain aspects of section 197, particularly in regard to the situation regulating a transfer on insolvency, the transfer of shares and the dismissal of employees. The Labour Relations Amendment Bill seeks to address these and various other problems.

⁴⁴ 1999 ILJ 2521 (LAC)

⁴⁵ 2524F

⁴⁶ Olivier "Transfer of Undertakings and Insolvent Employers: A Comparative Enquiry and Implications for South African Labour Law" 1995 *Tydskrif vir Suid Afrikaanse Reg* 737

⁴⁷ The only noteworthy addition was the inclusion of the rescue of undertakings proceedings under s197(1)(b).

In a statement released on the internet on 2000/07/27 the Department of Labour stated that it believes that the revamped provision will provide greater certainty and flexibility to local and foreign investors who may want to acquire local businesses thus will assist to reduce negative perceptions about our labour laws.

These aims are sought to be achieved by two new detailed sections: a completely new section 197 - based to a large extent on the European Directive discussed in chapter three- which regulates the transfer of the business as a going concern, and a section 197A which regulates separately the transfer of a business as a going concern in the case of insolvency. Certain amendments to the Insolvency Act -especially section 38 - are also proposed which are specifically made to work in conjunction with the amendments to section 197A in order to solve the conflict that existed previously between these two acts.

While these propositions make for interesting study, the question that remains is not whether the legislator will accept the changes, but rather if these changes are comprehensive enough and to what *degree* they will be accepted in the Amendment Act.

CHAPTER 3

AN ANALYSIS OF THE VALUE OF FOREIGN JURISPRUDENCE

1 INTRODUCTION

Most countries have provisions that ensure some sort of continuity of employment upon the transfer of the business and as a result there is no lack of foreign authorities on the subject. But does the LRA encourage the use of such foreign jurisprudence?

Section 3 of the LRA prescribes that any interpretation of the Act should -

- (a) give effect to the primary objects of the Act;
- (b) be in accordance with the Constitution;
- (c) be in accordance with public international law.

Blackie and Horwitz (1999: 1388-1389) argue that all three these subsections necessarily point us towards an analysis of foreign jurisprudence. Section 3(a) advocates a purposive approach to the interpretation of the Act, necessitating a look at the factors and (foreign) influences that led to the design of the Act. Section 3(b) refers to section 23(1)(a) of the Constitution⁴⁸ which provides that every person shall have the right to "fair labour practices" - a non-static concept that is invariably influenced by international trends. In conclusion, section 3(c) requires compliance with public international law - which also includes the diffusion of jurisprudence from international law. If these arguments are sound, then it seems that the LRA does indeed invite comparative legal research.

At first the use of foreign jurisprudence seems to be an uncomplicated task. Unfortunately, the abundance and variety of foreign provisions is very problematic. It is inevitable that the law of each nation should be different, particularly because the laws of each nation are a direct result of the specific needs and problems of each society. Considering this, the application of foreign law by any other country could quite easily be disastrous. As Froneman DJP states in *Foodgro v Carol Keil*:⁴⁹

⁴⁸ 108 of 1996

⁴⁹ 1999 ILJ (LAC) 2521

“The usefulness of these comparative provisions should not be overstated. The differences in wording from section 197 are quite obvious, as is the fact that they find their applications in societies different in history and development from our own. It would be unnecessarily parochial, though, not to enquire whether the treatment of these provisions in these jurisdictions do not provide some insight for the proper interpretation and application of section 197 of the Act.”⁵⁰

Although Froneman DJP concedes that these provisions will be helpful to provide insight into the workings of section 197, he expresses concern about the importance of applying a provision in its specific national context. An examination of the development and history of similar foreign provisions would therefore necessarily preclude a transplantation of these findings to the South African situation. Before any transplantation we would need to establish definite points of correspondence to determine if foreign law could be of any relevance. In the context of labour law we would need to establish for example the correspondence between basic terms such as employer, employee and business. Perhaps of more importance and more specifically in relation to the continuity of employment at the sale of a business, we would also need to consider the purpose of the various provisions, the extent of the workings there of and how it effects the individual and/or collective rights of the employer and employees.

2 IDENTIFYING THE RELEVANT JURISDICTIONS

At its heart, all provisions that regulate the transfer of the contracts of employment on the transfer of a business seek to balance the interests of the employer and the employee.⁵¹ This is unfortunately no easy balance to strike and quite often a system opts to protect the interest of the one over the other. In South Africa and the European Union, the focus of such provisions seem to be the protection of the employee by means of an automatic transfer of the contract of employment. A study of the different provisions that ensure such continuity of employment in the European Union would therefore provide valuable insight into how such objectives can be achieved in South Africa.

⁵⁰ 2527F

⁵¹ Jordaan "Transfer, Closure and Insolvency of Undertakings" 1991 12 5 *ILJ* 935

In certain circumstances, for example, if the business is transferred due to insolvency, the rights of the employees are also more limited in South African law. This acknowledges the need for more flexibility on the part of the employer and the owners of the capital and promotes an approach more in line with that employed by the United States of America; although, admittedly, not quite as severe. A brief look at such provisions would therefore also be justified.

Whether provisions attempt to provide stability for the employee or flexibility for the employer, it has to be noted that none of these approaches are considered to be totally ideal. The approach in the US is often harshly criticised for the way in which it fails to acknowledge the importance of the employees to the successful survival of a business.⁵² Meanwhile, the European approach is considered by some to be too rigid. Collins argues that as long as the new employer is not enabled by statute to negotiate new terms of employment after the transfer, they would simply resort to retrenchments prior to the transfer itself.⁵³ As a result, such provisions actually encourage retrenchment. The golden midway would seem to be the provision of such a statutory right to negotiate to restructure *after* the transfer. Such a right exists in Canadian law, although only in regard to collective agreements. A brief study of the Canadian solution might therefore also be useful in conclusion.

3 EUROPEAN UNION

Although the legislator never provided clarity as to what inspired section 197, many writers have pointed towards the similarities between it and the Acquired Rights Directive⁵⁴ of the EEC and especially the UK Transfer of Undertakings (Protection of Employment) Regulations 1981. A brief study of these provisions would clearly illustrate the similarities between these provisions and section 197, but will also serve to highlight the differences, in order for us to ascertain the relative merit of transplanting these findings in South African law.

⁵² Blackie & Horwitz "Transfer of Contracts of Employment as a Result of Mergers and Acquisitions: A Study of Section 197 of the Labour Relations Act 66 of 1995" 1999 20 *ILJ* 1394

⁵³ Collins "Transfer of Undertakings and Insolvency" 1989 *ILJ UK* 18 144

⁵⁴ 77/187/EEC

3.1 THE ACQUIRED RIGHTS DIRECTIVE

The Acquired Rights Directive⁵⁵ was unanimously adopted by the Council of the European Community in 1977 and sought to address the challenges posed by the ever increasing occurrence of business restructuring in the European Community⁵⁶ and the need to provide "for the protection of employees in the event of a change of employer, in particular to ensure that their rights are safeguarded."⁵⁷ The Directive is based on Article 100 of the EC Treaty concerning the approximation of laws and as a result member states were required to adopt the provisions of the Directive into national legislation within a specific time.

In essence the Directive provides that on the fulfilment of certain conditions during a transfer of an undertaking, the contracts of employment and any associated right arising from it⁵⁸ are automatically transferred from the transferor to the transferee,⁵⁹ thereby ensuring continuity of employment.

3.1.1 DEFINITIONS AND SCOPE

As a point of departure, it is necessary to note that the Directive does not contain an express definition of the term *employee*. As a result, *employee* within the meaning of the Directive must be interpreted as covering any person who, in the Member State concerned, is protected as an employee under national employment law. It is therefore not the intention of the Directive to establish a uniform level of protection throughout the Community on the basis of common criteria.⁶⁰

The Directive does however provide definitions for the terms *transferor*⁶¹, *transferee*⁶² and *transfer*.⁶³ With regard to the latter, considerable interpretational problems have arisen over the years, particularly with regard to the scope of the transfer itself.⁶⁴

⁵⁵ Here after called "the Directive"

⁵⁶ Hunt "Success at last? The Amendment of the Acquired Rights Directive" 1999 *European Law Review* 215

⁵⁷ Stated in the preamble to the Directive.

⁵⁸ The automatic transfer of employees' rights to old age, invalidity or survivor's benefits under supplementary company or inter-company pension schemes are, however, excluded by Article 3, §3.

⁵⁹ Article 3, §1

⁶⁰ Blanpain & Engels *European Labour Law* (1997) 319

⁶¹ The transferor is any natural or legal person who, by reason of the transfer of an undertaking, ceases to be employer. (Article 2A and B)

⁶² The transferee is any natural or legal person who, by reason of the transfer of the undertaking, becomes the employer of the undertaking. (Article 2A and B)

3.1.2 ACQUIRED RIGHTS

The transfer of an undertaking affects various rights, the most prominent being individual rights flowing from a contract of employment, rights flowing from collective agreements and the rights regarding to social security, as well as the rights with regard to a dismissal by reason of the transfer.

3.1.2.1 INDIVIDUAL RIGHTS

The Directive provides that in the case of the transfer of a business or undertaking, the rights and obligations of the employee arising from his contract of employment are automatically transferred to the new employer. The terms of the contract will accordingly stay intact after the transfer. However, these provisions are only activated when the part of the undertaking for which the employee was working, is transferred.⁶⁵ The reason for this is that the Court of Justice argues that the employment relationship is essentially characterised by the link existing between the employee and the part of the undertaking or the business to which he is assigned to carry out his duties.⁶⁶ In order to decide whether the rights and obligations under an employment relationship are transferred, it is therefore sufficient to establish that the part of the undertaking or business where the employee was assigned was transferred.

The Directive states further that after the date of the transfer and by virtue of the transfer alone, the transferor is discharged from all obligations arising under the contract of employment.⁶⁷ This legal consequence is not subject to the consent of the employees concerned.

⁶³ The Directive applies to the transfer of an undertaking, business or part of a business to another employer as a result of a legal transfer or a merger (Article 1, §1-2). Blanpain & Engels explain that the key element of the definition lies in the fact whether the employees are, as a consequence of the transfer of the undertaking, confronted with a new, legal employer. A sale of shares that would result in a new economic owner is therefore not relevant. See also *H Berg and JTM Busschers v IM Besselen* Joined cases nos 144 and 145 87 IELL Case Law No.122, where the Court of Justice stated that: "The Directive is applicable where, following a legal transfer or merger, there is a change in the legal or natural person who is responsible for carrying on the business and who, by virtue of that fact, incurs the obligations of an employer vis-à-vis the employees of the undertaking, regardless of whether or not ownership of the undertaking is transferred." As a result only when the capacity of employer is transferred will it be seen as a transfer in terms of the Directive.

⁶⁴ Chapter 4 deals with this subject.

⁶⁵ Blanpain & Engels *European Labour Law* (1997) 518

⁶⁶ *A. Watson Rask and K. Christensen v ISS Kantineservice A/S*, No. C-209/91, *op. cit.*

⁶⁷ Article 3, §1

3.1.2.2 COLLECTIVE AGREEMENTS

According to Article 3, §2 of the Directive, the transferee shall, following the transfer, continue to observe the terms and conditions agreed in any collective agreement on the same terms applicable to the transferor under the agreement, until the date of the termination or expiry of the collective agreement or the entry into force or application of another collective agreement. Member States may limit the period of observing such terms and conditions, with the proviso that it shall not be less than one year.

3.1.2.3 SOCIAL SECURITY

The provisions regarding acquired rights do not cover employees' rights to old age, invalidity or survivor's benefits under pension schemes.⁶⁸ It is up to Member states to regulate this position individually to protect the interests of employees.

3.1.2.4 DISMISSAL

Article 4, §1 of the Directive protects the concerned employees in the case of a transfer against dismissal by the transferor or the transferee on the grounds of the transfer, except for economic, technical or organisational reasons entailing changes in the workforce.

3.1.3 INFORMATION AND CONSULTATION

The Directive provides that the transferor and the transferee shall be required to inform the representatives of their respective employees affected by the transfer with the following information:

- the reasons for the transfer;
- the legal, economic and social implications of the transfer for the employees;
- the measures envisaged in relation to the employees.⁶⁹

3.1.4 CONCLUSION

The increasingly expansive interpretation to the Directive granted by the Court of Justice resulted in the Directive finding application beyond the traditional methods of business transfer, such as sale and merger, which were the primary means of business restructuring at the time the Directive was adopted. As a result of the interpretation

⁶⁸ Article 3, §3

⁶⁹ Article 6, §1

afforded by the Court, the situation became such that outsourcing, market testing, competitive tendering, facilities management, and third party administration may all be caught by the Directive. Unfortunately this resulted in removing much of the attraction of contracting out as a cost saving mechanism, and the resulting outcry led to the inevitable revision process becoming an increasingly politicised battle. Eventually the process of securing agreement was rendered less onerous by making certain new provisions optional.⁷⁰ Despite the successes of the new Directive, which will be operative from the end of 2001, it is, however, considered to be unlikely that these revisions will succeed in laying to rest the controversies surrounding the definitions and scope of the Directive.⁷¹

3.2 UNITED KINGDOM

The British Transfer of Undertakings (Protection of Employment) Regulations 1981⁷² resulted from the Directive. Consequently, there are several aspects of the operation of the Regulations where in the courts of the United Kingdom have been influenced in their interpretation of this statutory instrument by the Directive, or where decisions of the ECJ have affected interpretation in the UK.⁷³

In its original form, the Regulations contained several limitations and exceptions that did not appear in the Directive. An example is the restriction that the Regulations do not cover transfers that are not in the nature of a commercial venture. In consequence, it was found to be defective as an implementation of the Directive and the Commission started infraction proceedings against the British Government in October 1992. The result was a set of amendments⁷⁴ in 1993 that brought the Regulations closer in line with the Directive.⁷⁵

⁷⁰ As a result, Member States can opt whether or not they provide inter alia for joint and severable liability of the transferor and transferee; whether they adopt measures to ensure that full disclosure is made by the transferor of the rights and obligations falling under the contract transferred; whether they apply the Directive to benefits which fall outside the statutory social security schemes; and whether the Directive applies in the case of insolvency.

⁷¹ Hunt "Success at last? The amendment of the Acquired Rights Directive" 1999 *ELR* 230

⁷² Here after called "the Regulations".

⁷³ Holland & Burnett *Employment Law* (1998) 265

⁷⁴ These amendments were brought about by the Collective Redundancies and Transfer of Undertakings (Protection of Employment)(Amendment) Regulations 1995 (SI 1995/2587)

⁷⁵ Holland & Burnett *Employment Law* 272 claims that one aspect of the Regulations is still not in line with the Directive: Regulation 5 gives the employee a statutory right to object to the transfer of employment. The effect of such an objection would be to end the contract, however, such termination would not for any purpose be regarded as a dismissal. The result would be that the

In essence, the Regulations preserve continuity of employment on a relevant transfer. The definition of a relevant transfer itself is however considered inadequate.⁷⁶ The whole or part of an undertaking that is transferred is limited by the definition in regulation 2(1) to an undertaking that includes any trade or business. The assumption is therefore that the transfer must take place as a going concern. Although the words “business” and “trade” also appear in the English version of the Directive, it seems that the Directive itself cannot be interpreted so narrowly.⁷⁷ This discrepancy seems to be direct result of significant differences in the terminology of the different languages in which the Directive was published: most of which use a term better translated as “economic entity” than “business”.⁷⁸ This conflict was mostly resolved in the leading case of *Council of the Isles of Scilly v Brintel Helicopters*⁷⁹ where the court provided a set of guidelines for determining the scope of TUPE 1981, by relying extensively on the European Court of Justice decision in *Spijkers v Gebroeders Benedik Abattoir CV*.⁸⁰

4 ANGLO AMERICAN JURISPRUDENCE

Anglo American labour law differs significantly from the European model. For example, there are no provisions that provide for the protection of the individual rights of the employee during a transfer or in the case of a dismissal. As a result, it can only be of limited use. There is however certain provisions that provide for the continuity of collective rights in the case of a transfer of a business. These provisions will be discussed briefly.

4.1 UNITED STATES OF AMERICA

In the United States the protection of collective agreements on the transfer of the business was already brought about in the 1940's. In contrast to the European position, such protection was not guaranteed by any statute, but came into being through the role of the courts.

employee cannot claim constructive dismissal and would also not be entitled to redundancy payment. They argue that such a diminution of the employees rights were clearly not intended by the Directive. See also Harvey *Harvey on Industrial Relations and Employment Law* (1996) F2 [4] – [9] for further criticism on the current state of the Regulations.

⁷⁶ Holland & Burnett *Employment Law* 267

⁷⁷ Holland & Burnett *Employment Law* 268

⁷⁸ For a detailed discussion, see *Schmidt v Spar- und Leihkasse der Früheren Ämter Bordesholm, Kiel und Cronshagen* 1995 ICR 237

⁷⁹ 1995 ICR 249

⁸⁰ 1986 2 CMLR 296

In the case of *Southport Petroleum Co v NRLB*⁸¹ the US Supreme Court found that if after the transfer of the business the employer's identity remains substantially the same despite the fact that it has undergone some technical change, he would still be bound by the obligations that precede the transfer.⁸² Although this ensured that the employer could not escape the workings of a collective agreement by affecting a subtle change in identity, this did not provide any clarity as to whether the employees would be protected from job loss during such procedures. More importantly, this did not regulate the situation where there was indeed a completely new employer.

The Supreme Court only addressed these issues more than 20 years later in the case of *John Wiley & Sons v Livingston*⁸³. The court held that even a bona fide transfer provided a big potential disadvantage to the employees, which was compounded by the fact that they had no part in the negotiations that led up to such a transfer. To minimise this risk, court found that it was necessary to provide that in some circumstances the transfer of the business would not terminate the contracts of employment, but that the new employer would simply replace the old employer. In no way, however, did this affect the rightful prerogative of the employer to rearrange their business as they see fit.

This decision was further limited in 1971 by the case of *William J Burns International Detective Agency v NRLB*⁸⁴ when the court found that it was not in the interest of the employer or the union for contracts of employment to be transferred in this way. The court reiterated that changing the business and the terms of employment upon a transfer was not only the prerogative of the employer, but also essential for the survival of the business. With regard to the unions, the court stated that they might not be willing to make as much concession to a new more financially stronger employer than they would to the old financially troubled employer.

⁸¹ 315 US 106; 90 LRRM 411 (1942)

⁸² Blackie & Horwitz 1999 20 *ILJ* 1392

⁸³ 1964 LRRM 2769

⁸⁴ 32L Ed 2d 61

4.2 CANADA

Early Canadian labour law was based on the English model. General dissatisfaction with the English judicial and legislative approach to employment relations in the 1930s⁸⁵ resulted in the adoption of the more accommodative legislative approach to labour relations prevalent in the US. As a result, Canadian labour policy is more in line with American labour law than it is with British labour law.

At common law, the English principle of privity of contract means that an agreement can only bind its signatories. As a result, Labour legislation⁸⁶ was passed in all Canadian provinces to ensure that collective bargaining rights flow through changes of ownership, as long as there is continuation of the same business. Like in the USA, this concept also became known as successorship, and is an attempt to balance the interests and expectations of all parties: although the employer's liberty to dispose of the business is not encroached upon, the legislation recognises that employees have "vested rights" in the business, which deserve protection from elimination when a business is sold.⁸⁷ The legislation provides for these rights by ensuring the continuity of the collective bargaining rights of the employees upon the sale of the business.

Successorship provisions achieve this in two ways: by protecting the trade union's rights to bargain and by protecting any subsisting collective agreement from the termination upon the sale.⁸⁸ The most novel aspect of these provisions is however the way in which they protect the rights of the new employer to restructure the business. After the transfer of the business the new employer has a statutory right to initiate negotiations with the unions in order to effect any necessary changes to the business. In this way, a flexible process is ensured which can only be beneficial to the business and all the parties involved.

5 CONCLUSION

The Acquired Rights Directive is very detailed and contains definitions for the various concepts involved in the transfer of the contracts of employment on the transfer of the business. Despite these definitions, it still seems that the exact scope of the Directive can be unclear and therefore left open to the interpretation of the courts. This situation

⁸⁵ Adams *Canadian Labor Law* (1985) 1

⁸⁶ For a complete list of all the relevant legislation, see Adams *Labor Law* 398 fn 1.

⁸⁷ Adams *Labor Law* 398

⁸⁸ Adams *Labor Law* 399

seems quite similar to that in South Africa. Due to its detailed nature, the Directive also contains a substantial amount of regulations that do not appear in the section 197. For example, the Directive regulates the transferral of collective rights, as well as the position where a dismissal took place by reason of the transfer itself. Finally, the Directive also provides for a process of information sharing and consultation prior to the transfer taking place.

It is clear from the wording of the Amendment Bill that great reliance has once again be placed on the Directive. This fact alone justifies a study of these provisions.

So far the Labour Courts in South Africa have also relied heavily on the UK Transfer of Undertakings (Protection of Employment) Regulations. As with the Directive, these Regulations also contain definitions of the relevant terms affecting the transfer, and not surprisingly, these definitions are considered to be even more problematic than that of the Directive. When relying on the Regulations it should also be noted that they promote a narrower interpretation as to what should qualify as a transfer of undertaking than the Directive itself.

American Labour Law seems at first glance to be of little relevance to the South African situation, simply because it does not provide directly for the protection of the individual rights of the employee. As an illustration of how business can be promoted during the transfer of an undertaking, it may, however, be of some use. Also the way in which the American courts provided for the protection of the collective rights during the transfer of an undertaking may be worth some note.

As an example of an Anglo American labour law, Canada might prove to be much more worthy of study, even if they also just provide for the protection of collective rights. Not only would such a study provide insight into the relationship between the employee and the business, but also by giving statutory protection to the right to bargain upon and after the transfer of an undertaking, Canadian labour law succeeds in balancing the needs of the employee and business equally in the case of a transfer of business and employment. Of all the attempts by the different nations, this seems to be the most satisfactory and uncomplicated solution.

CHAPTER 4

DEFINING THE TERMS OF SECTION 197

1 INTRODUCTION

Certainty about the interpretation of the terms of any piece of legislation is essential for its effective enactment. Before the scope or even the effectiveness of legislation can be determined, it is therefore necessary to establish the boundaries inside which the legislation should apply. Establishing these boundaries is sometimes the most challenging task when interpreting legislation. Certain aspects of section 197 of the LRA in particular have proved to be very problematic in this regard. The operational terms of the section include: "employer", "employee", "business, part of business or undertaking", "transfer" and "going concern". An analysis of the meaning of these terms will be conducted in this chapter, with the focus on certain problematic instances, such as outsourcing and the sale of the shares.

2 EMPLOYEE

Section 197 provides for the continuity of the contracts of employment of the **employees** affected by the transfer. Section 213 of the LRA defines an employee as:

"(a) any person, excluding an independent contractor, who works for another person or for the State and who receives, or is entitled to receive, any remuneration; and

(b) any other person who in any manner assists in carrying on or conducting the business of an employer".

Although it is clear that the section attempts to differentiate between an employee and an independent contractor – the latter not being included under the protective scope of the LRA – part (b) of the definition is so wide that this distinction can easily be blurred.

As a result, Nugent J found in *Liberty Life Association of Africa Ltd v Niselow*⁸⁹:

"The latter part in particular may seem to extend the concept of employment far beyond what is commonly understood thereby. To adopt a literal interpretation though would clearly result in absurdity. I think that the history of the legislation which has culminated in the present statute, and the subject matter of the statute itself, lends support to a construction which confines its operation to those who *place their capacity to work* at the disposal of others, which is the essence of employment. It is not necessary in this case to decide where the limits of the definition lie. It is sufficient to say that in my view the 'assistance' which is referred to in the definition contemplates that form of assistance which is rendered by an employee, though the person he assists may not necessarily be his employer. In my view it does not extend to assistance of the kind rendered by independent contractors."

As section 197 deals exclusively with the transfer of the contracts of employment, any contracts concluded with independent contractors would therefore not be protected in the same way on the transfer of a business as a going concern. (It should be noted that the contract of employment could be in writing or merely an oral agreement.)

Finally section 2 of the LRA excludes the following employees from the workings of the Act: members of the National Defence Force; the National Intelligence Agency; and the South African Secret Service.

3 EMPLOYER

The transferral of the contracts of employment envisaged by section 197 must take place "from one *employer* (referred to as 'the old employer') to another *employer* (referred to as 'the new employer')..."⁹⁰

The LRA itself does not contain a definition of the term "employer". In determining exactly who the employer is, the courts have therefore in the past applied "a well mixed blend of common sense and a sense of equity".⁹¹ Most often this involves looking at the real relationship between parties rather than merely accepting the parties'

⁸⁹ 1996 ILJ 673 (LAC)

⁹⁰ s197(1)

⁹¹ *MWASA & others v Facts Investors Guide (Pty) Ltd & another* 1986 ILJ 313 (IC) 315C

arrangements at face value.⁹² For example, in the cases of *Shikwambana v Quantum Construction Holdings (Pty) Ltd*⁹³ the respondent contracted out certain services to a close corporation, the sole member of which was a previous employee of the respondent who now provided exactly the same service as before. Piercing the corporate veil on the grounds of fairness, the court stated that:

"The mere fact that the pay envelope of the applicant was slipped into the pocket of his close corporation suit does not mean that the man inside the suit can, in labour law, be ignored."

As to the employees working for the close corporation, the court subsequently also found that Quantum Construction and not the corporation was the actual employer. Such an approach clearly leads to equitable results and ensures the protection of the workers who are individually in a weaker position to bargain. However, it should be noted that the court would only pierce the corporate veil in exceptional circumstances, for example where the fairness of a dismissal could not be otherwise determined.

However, saying that the court applies common sense and that it observes the real relationship, does not go very far in helping us to define what exactly an employer is. It has been suggested that an inversion of the definition of "employee" in the act may be a useful starting point in helping us to distil the most important elements of an employer. An employer can therefore be considered to be "... any person who receives services from an employee for remuneration or is assisted in the conduct of its business by the employee".⁹⁴ Unfortunately this definition does not take into account one important factor when we consider the employment relationship: the **control** that the employer has over the employee. If such control is not to be considered as a prerequisite for identifying the employer, then it is quite reasonable to think that the employer and the entity that exerts the real control over the employee can be two entirely different persons.⁹⁵ It is submitted that such an approach may lead to abuse, especially in the context of the transfer of businesses. The use of service companies, for example, illustrates this point clearly.⁹⁶ In such a case the employees provide

⁹² Du Toit et al *Labour Relations Law: A Comprehensive Guide* (2000) 75-76

⁹³ NH 11/2/2632

⁹⁴ Du Toit et al *Labour Relations Law: A Comprehensive Guide* (2000) 74-75

⁹⁵ Hepple "The Crisis in the EEC Labour Law" 1987 *ILJ UK* 77

⁹⁶ Blackie & Horwitz "Transfer of Contracts of Employment as a Result of Mergers and Acquisitions: A study of Section 197 of the Labour Relations Act 66 of 1995" 1999 20 *ILJ* 1396

services for the trading company, but are themselves employed by a service company. When the trading company is transferred, then the employees would be caught outside the protection of section 197 simply because there is no change in employer in the legal sense, while in actual fact there is a new person exerting control over the employees.⁹⁷ The solution to this problem seems to be the fact that the Labour Court regards substance over form when judging the transactions that led to the abuse.⁹⁸ If the court found that such a transaction was merely simulated to the disadvantage of the employees, then the court might consider this to be a factor indicating that there was indeed a transfer within the scope of section 197. In practice, however, it is usually no simple task to uncover the true intention of the parties and therefore this situation may still remain problematic.

4 TRANSFER

The LRA does not define the term transfer, nor does it contain a list of what types of transactions exactly entail the transferral of a business. It is clear from our general understanding of the word, however, that a transfer entails the carrying over of an object from one entity to another. By implication there should then be at least two entities involved in the transfer: in this case the old employer and the new employer.

Most commonly, such a transfer would be brought about by the conclusion of a contract of sale between these parties. The transfer of a business is however not limited to the **sale** of the business. In *Schutte & others v Powerplus Performance (Pty) Ltd & another*⁹⁹ the judgement of Seady AJ is accurately summed up in the headnotes as follows:

"Although a sale of the business is the normal way in which a business is transferred as a going concern, it is not the only way in which a business is transferred. A business may be transferred as a result of a merger, take-over or part of a broader process of restructuring within a company or a group of companies. It can [also] take place by virtue of an exchange of assets or donation."

⁹⁷ These are the simplified facts of *Banking Insurance & Finance Union v Barclays Bank plc* 1987 ICR 495

⁹⁸ *Schutte & others v Powerplus Performance (Pty) Ltd & another* 1999 ILJ 655 (LC)

⁹⁹ *supra*

Mergers, take-overs, the exchange of assets and donations are all common occurrences in South Africa and the workings there of need not be further discussed for the purpose of this thesis. What is problematic, however, is that all transfers can not necessarily be defined in term of these listed transactions. The most important question in this regard is whether the wording of section 197 allows for a transfer that involves more than these two parties? In foreign law there are many examples of indirect transfers where the transfer is brought about by actions of a third party or by multi-party transactions involving agents and intermediaries. Examples of such transfers are the termination and grant of franchises, licenses, concessions and tenders.

In *Thunder Bay Ambulance Services Inc*¹⁰⁰ the Canadian Ministry of Health decided to consolidate two ambulance services. Parties were then allowed to tender for the operation of the unified service. The court held that the winner of this tender took transfer of the business, even though the tender and the resulting transfer were a result of the involvement of the ministry. In the case of *Taylor Ford Sales Ltd*¹⁰¹ the court made a similar finding. On the facts it held that the withdrawal of a car dealership franchise and the resulting reissue of this franchise to a new party entailed a transfer.

A series of similar cases abound in European and British case law.¹⁰² For example, in the *Daddy's Dance Hall*¹⁰³ case, the ECJ held that a transfer took place where a non-transferable lease of bars and restaurants was surrendered and a new lease granted to a third party. This is considered to be an indirect transfer, but a transfer none the less.

Sometimes, a transfer may even take place without any of the parties intending or sometimes being aware that it came about. The most notable recent case on this subject is the British case of *Charlton v Charlton Termosystems (Romsey) Ltd*.¹⁰⁴ In this

¹⁰⁰ 1978 2 Can LRBR 245

¹⁰¹ 1981 1 Can LRBR 138

¹⁰² See for example the European cases of *Landsorganisationen i Danmark v Ny Mølle Kro* 287/86 1989 IRLR 37 which involved the reversion of a business lease; *P Bork International A/S v Foreningen af Arbejdsledere i Danmark*: 101/87 1989 IRLR 41 which involved the forfeiture of a lease followed by the sale of the freehold to a new owner; *Foreningen af Arbejdsledere i Danmark v Daddy's Dance Hall A/S*: 324/86 1988 IRLR 315 which involved the termination of a non transferable restaurant and bar lease and the grant of a new lease; *Dr Sophie Redmond Stichting v Bartol*: C-29/91 1992 IRLR 366 which involved the transfer of a subsidy from one foundation engaged in assisting drug addicts to another; and the British case of *Kenny v South Manchester College* 1993 IRLR 265 which involved the transfer of prison education service from a local education authority to South Manchester College without a transfer of assets, clients/customers or employees. See also Harvey *Harvey on Industrial Relations and Employment Law* (1996) F/36 [85].

¹⁰³ *supra* (n15)

¹⁰⁴ 1995 IRLR 79

matter, the Directors - who were also the sole shareholders- of a company continued in business several weeks after the company had been struck off the Register of Companies and dissolved for failing to file annual reports. The court held that this continuation of business after the dissolution of the company resulted in a transfer of the undertaking from the company to the Directors.

The motivation behind such a robust interpretation of a "transfer" is simply to "prevent the proliferation of technical mechanisms devised in order to circumvent the legislation."¹⁰⁵ The Canadian court in *Culverhouse Foods Ltd*¹⁰⁶ accurately summed this up when it stated that: "it would be contrary to the purpose of the legislation if only through a double sale the applicability of the legislation was avoided."

This wide interpretation of "transfer" is not accepted unconditionally in South Africa. Wallis argues that such an interpretation is not permissible on the language of section 197 as the section expressly allows for only transfers "by the old employer".¹⁰⁷

Without the involvement of the old employer a transfer according to section 197 would not take place. Although Wallis also argues that section 3 of the LRA does not allow the Labour Court to ignore the language of the statute, it seems that a more robust approach to interpreting a transfer seems to have found favour in the Labour Court in South Africa. In *Tekweni Security Services CC v Mavana*¹⁰⁸ the manager of Protector CC set up a new close corporation - Tekweni Security Services CC - after the sole member of Protector CC left the country. The clients of Protector were asked to transfer their contracts to the new corporation. The court held that there was indeed a transfer of the business, even though there was no evidence of an agreement between the member of Protector (the old employer) and the members of Tekweni Security Services.¹⁰⁹

The Amendment Bill does not give greater clarity into how transfer should be interpreted. It provides, similar to the current provision that a transfer is a transfer of a business by one employer ("the old employer") to another employer ("the new employer") as a going concern. The wording in this regard has not changed.

¹⁰⁵ Blackie & Horwitz 1999 20 *ILJ* 1402

¹⁰⁶ 1976 OLRB 691

¹⁰⁷ Wallis "Section 197 is the Medium. What is the message?" 2000 21 *ILJ* 4

¹⁰⁸ 1999 ILJ 2721 (LC)

¹⁰⁹ The court held that the presence of an agreement affecting the transfer is merely a factor when determining if there was a transfer of a business as a going concern. See *infra*.

In conclusion, it seems that the Labour Court will easily find that a transferral took place, whether it was direct or indirect, provided that what was being transferred was a business, part of a business or an undertaking and provided that this business has moved from one employer to the next.

5 “BUSINESS, PART OF BUSINESS OR UNDERTAKING”

The LRA does not contain a definition of what exactly a "business, part of business or undertaking" entails. These concepts are however not new to labour law in South Africa and Barker & Holtzhausen provide useful definitions. An undertaking is defined as:

"An independent economic organisation with the object of making capital invested therein profitable by supplying goods or services on a continuous basis to the market in anticipation of a demand for such goods and services."¹¹⁰

A part of an undertaking is defined as:

"... a technical unit responsible for the production of goods or rendering of services and operating as a separate economic entity."¹¹¹

From these definitions we could deduce that a business is necessarily something that exists for an economic purpose, but should we interpret the section so narrowly? Initially the Regulations excluded the transfer of undertakings that were expressly run for a non-profit motive. In contrast, the Directive did not make a distinction between commercial and non-commercial ventures.¹¹² Eventually the Regulations had to be brought into line with the Directive by section 33 of the Trade Union Reform and Employment Rights Act 1993 that deleted this distinction.

The current wording of section 197 does not present a problem in this regard, but the definition of a business in the Amendment Bill does. A business is seen as "an economic entity, consisting of an organised grouping of resources that has the object of performing an economic activity."¹¹³ Directive 98/50/EC also provides for the transfer of an "organised grouping of resources which has the objective of pursuing an economic

¹¹⁰ Barker & Holtzhausen *South African Labour Glossary* (1996) 51

¹¹¹ Barker & Holtzhausen *Labour Glossary* 114

¹¹² In groundbreaking cases like *Dr Sophie Redmond Stichting v Bartol supra* involving voluntary organisations, the court never questioned the applicability of the Directive.

¹¹³ clause 47(a)197(2)(a)

activity"¹¹⁴, but also states that the Directive "shall apply to public and private undertakings engaged in economic activities whether or not they are operating for gain."¹¹⁵ The Amendment Bill makes no such provision. Accordingly, if the wording of the Amendment Bill is to be taken at face value, then the applicability of section 197 to the public sector and non-profit organisations might well in the future be brought into question.

It is submitted that this was not intentional, but merely an oversight, seeing that the non-applicability of section 197 to non-profit organisations and the public sector would not be equitable. The LRA applies to all employment relationships except for the few excluded in section 2. There is no apparent reason why the employees of non-profit organisations and the public sector should not be afforded protection under section 197.

Since a business is composed of many different aspects, it is not always clear whether the transferral of one of these components would lead to the transfer of a business or part of a business or not. There are three specific scenarios in particular which create problems when considering if they entail the transfer of a **business**: the transfer of assets, the transfer of shares and outsourcing, which most often entails the transfer of a service or function.

5.1 ASSETS

The modern business consists of many tangible and intangible assets. The question is if the transfer of any or all of these assets alone could be seen as the transfer of the business. Although the Labour Court has never answered this, it has been argued by Brassey in the case of *Ndimma & Others v Waverly Blankets Ltd*¹¹⁶ that the sale of the assets of the business (and by implication therefore also any other transfer of these assets) was "not necessarily contemplated in section 197". Consequently, he argues that the transfer of assets should be seen as a grey area and depending on the specific circumstances, might or might not result in the transfer of a business.

In the pre-Regulations case of *Lloyd v Brassey*¹¹⁷ for example, Lord Denning found that the transfer of farmland did result in the transfer of a business,¹¹⁸ stating that:

¹¹⁴ s1 1.(b)

¹¹⁵ s 1 1.(c)

¹¹⁶ 1999 ILJ 1573A (LC)

¹¹⁷ 1969 1 All ER 382 (CA)

“In my opinion the business of farming consist of cultivating the land... The land itself is the essence of the business, and when the land, together with the buildings, is sold, the business is necessarily sold with it.”

This is clearly an exceptional case with exceptional facts, because the general principle that has been affirmed by numerous cases arising in the UK and the EEC is that a distinction exists between the transfer of assets and the transfer of a business. As a result, when the assets of a business are transferred, this does not necessarily constitute the transferral of the business.

In the case of *Melon v Hector Power Ltd*¹¹⁹ Lord Fraser had to decide if the sale of a tailoring factory was merely the transfer of assets or if it was the transfer of a business. Following *Lloyd v Brassey*¹²⁰ Lord Fraser emphasised the distinction between the transfer of a business and transfer of physical assets as was made in this case.¹²¹ As a result Fraser found that what had been transferred was not a business, stating that:

“It seems to me that the essential distinction between the transfer of a business or a part of a business and a transfer of physical assets, is that in the former case, the business is transferred *as a going concern* (my own emphasis) so that the business remains in the same business but in different hands ... whereas in the latter case, the assets are transferred to the new owner to be used in whatever business he chooses.

In conclusion, Lord Fraser affirmed that all the circumstances should be considered to reveal the true position. The approach that we can deduce from this and other EEC and UK case law¹²² is that in each case the court should look into the specific facts to weigh up if the transfer of the assets indeed did result in the transfer of a business as a going concern or not. It should therefore be determined if the assets by themselves constituted "a going concern" and this would depend on the facts of each situation. As will be discussed later in this chapter, the words "going concern" do not seem to be

¹¹⁸ In construing the words “change ... in the ownership of the business” (then appearing in section 13(1) of the Redundancy Payments Act 1965), Lord Denning found that it meant the same as “a trade or business or an undertaking ... transferred from one person to another” as was the case in *Kenmir v Frizzel* *infra*. Consequently, he applied the “going concern” test proposed by Lord Widgery in that case.

¹¹⁹ 1981 1 All ER 313

¹²⁰ *supra*

¹²¹ 317H

¹²² See in particular also *Daddy's Dance Hall* *supra* and *Premier Motors v Total Oil Great Britain LTD & others* 1984 ICR 58

particularly meaningful. It is submitted that in this case "going concern" means nothing more than that the assets are kept together after the transfer and are used for the same purpose that they were before the transfer, whether independently or not.¹²³ For example: while the transfer of farmland would seem to constitute the transfer of a going concern, if the farmland were sold to developers with the intention of building a casino on the land, it would not.

5.2 SHARES

The most common way in which corporations are transferred is through the sale of a block of shares that leads to a change in the control of the business. Such a transfer of shares is however not considered as being a transfer of a business for the purposes of section 197.¹²⁴ The reason for this is the company itself is considered to be the employer and a change in the ownership of the company need not necessarily imply a change of employer.¹²⁵ The sale of shares could therefore only result in the transfer of the control or the possession of a business and not the transfer of the business itself. In *Ndima v Waverly Blankets*¹²⁶ Zondo J accepted this view, stating that:

"I am unable to agree ... that the transfer of possession and control of a business is sufficient to bring the applicants within the ambit of section 197. Quite clearly, the section requires the transfer of business in order for its operation to be triggered. The transfer of business and transfer of possession and control of a business are two separate concepts."

Although such an interpretation is clearly the correct one, it unearths a serious flaw in the wording of this section. Section 197(1)(b)(ii) provides for the transferral of the contracts of employment when the business is transferred as a going concern by means of the entering into of a scheme of arrangement or compromise to avoid the winding up or sequestration for reasons of insolvency. Such schemes of arrangement are made possible by section 311 of the Companies Act. While the details of these schemes fall outside the scope of this thesis, it is sufficient to note that the way in which the transferral of the business most commonly takes place in such a case is through the

¹²³ See 6 for a discussion on the meaning of the "going concern".

¹²⁴ Le Roux "Transferring Contracts of Employment" 1996 *Contemporary Labour Law* 11

¹²⁵ Such an argument would depend on whom the courts would view as the actual employer. See 3 for a discussion of this topic.

¹²⁶ *supra*

transfer of shares. As a result, the majority of schemes that are specifically provided for by section 197(1)(b)(ii) would be excluded from the ambit of the section simply because they do not entail the transfer of a business to begin with. As a result, employers would be able to side step the provisions of section 197 effortlessly by transferring a business merely through the sale of shares. It is doubted that this was the intention of the legislator. Zondo J also noted this to his alarm, proclaiming "there is a crying need for an amendment of section 197 to cover the situation..."¹²⁷

This position is redeemed somewhat by the fact that the court will consider the "substance rather than [the] form"¹²⁸ of the transaction. In practice, however, this might be easier said than done, as Zondo J states in *Ndim*:

"...in most cases it would be very difficult for anyone to prove that a particular transaction of the sale of shares was a simulation or a sham. Most transactions in which people circumvent the law look genuine on the outside and seem to be perfectly legitimate transactions."

There is no easy solution. The Amendment Bill does not propose to solve this situation either. While great attention is given to the transferral of contracts of employment of the insolvent business, little regard is had for a transfer due to a scheme of arrangement. Clause 47(b) re proposed section 197A(2) only provides that the consequences of the new proposed section 197A(1) can be contracted out of by an agreement concluded according to section 311 of the Companies Act. Nowhere are the consequences of a scheme of arrangement on the contracts of employment regulated. If this position remains, then section 311 of the Companies Act might remain the most effective way to side step the protective workings of section 197.

5.3 OUTSOURCING

Outsourcing is a process whereby activities traditionally carried out internally are contracted out to external providers.¹²⁹ The benefits of such a process are well established and include cost savings, increased flexibility of production, increased market discipline and specialisation.¹³⁰ But there is also a downside to out-sourcing as

¹²⁷ 1575G

¹²⁸ *Kenmir v Frizzel* *infra* as accepted in the cases of *Schutte*, *Ndim* and *UCT*.

¹²⁹ Domberger *The Contracting Organization A Strategic Guide to Outsourcing* (1998) 12

¹³⁰ Domberger *Outsourcing* 51

it could result in the loss of skills as well as a loss of corporate memory¹³¹ and weakened innovative capacity. More importantly, there are also transition costs. These costs, which are financial as well as social, are brought about by the dislocation of employees or loss of employment.¹³² For outsourcing to be a viable option, it is necessary that the benefits should outweigh these costs. Any way to lessen these costs should necessarily promote outsourcing as a business solution. It would therefore be relevant to investigate if outsourcing could be seen as a form of a transfer of a business as going concern.

The single most problematic aspect when dealing with outsourcing in the context of section 197, is determining what has been transferred. Can the contracting out of a service be seen as the transfer of a **business**? To answer this question, we need to consider what exactly a business is. We have already established a definition of a business as an "independent economic organisation". In the case of outsourcing, it is usually an activity or a service that is transferred and as we have learned from the ECJ, the transfer of a service cannot necessarily be seen as the transfer of a business or a part of a business.¹³³

Initially the ECJ was of a different opinion. In *Schmidt*¹³⁴ the ECJ found that the outsourcing of a cleaning service could amount to a transfer of a business as contemplated by the Directive, even though it affected only a single employee and this employee had not been transferred along with the service. The court based its arguments on a wide interpretation of the Directive and found that the fact that the activity that was transferred was only performed by one person did not exclude the application of the Directive since its application did not depend on the number of employees assigned to the part of the undertaking which was the subject of the transfer. The court found further that such an interpretation was in keeping with the second recital in the preamble of the Directive which provided that one of the main objectives of the Directive is to protect employees in the event of a change of employer.

¹³¹ Domberger *Outsourcing* 70. Corporate memory refers to the loss of collective knowledge within the organisation that may be diluted as a result of fragmentation.

¹³² Domberger *Outsourcing* 70

¹³³ See for example *Spijkers v Gebroeders Benedik Abattoir CV* 1986 ECR 1119, ECJ; *Schmidt v Spar- und Leihkasse* 1994 IRLR 302, ECJ; *Dr Sophie Redmond Stichting v Bartol* 1992 IRLR 366, ECJ; *Merckx v Ford Motors Co Belgium SA* 1996 IRLR 467, ECJ.

¹³⁴ *supra*

A retreat from this very wide interpretation of the Directive was discernible in the controversial case of *Süzen*.¹³⁵ The applicant worked as a cleaner at a private church run school in Bonn-Bad-Godesberg in Germany. Zehnacker, an independent contractor, employed her and seven other cleaners. When the school terminated the contract with Zehnacker and contracted-out the cleaning to another company, Lefarth, the fact that Zehnacker had no other work for the cleaners led to their dismissal. The applicant contended that the dismissal was ineffective because under the Directive she ought still to have been engaged in cleaning the school – under the employment of Lefarth. After re-affirming that the decisive criterion for determining whether a transfer had taken place was the question whether the entity retained its identity, the court defined a business as "an organised grouping of person and assets facilitating the exercise of an economic activity which pursues a specific objective".¹³⁶ As a result, the court found that a business cannot be reduced to the activity entrusted to it. The court continued, stating that something more is needed, something which must "emerge from other factors, such as the entity's workforce, its management staff, the way in which its work is organised, its operating methods, or the operational resources available to it".¹³⁷ The court went on to say that the weight that should be given to each factor would necessarily vary depending on the activity that is transferred. If for example the service is provided without the reliance on certain assets, then the transfer of those assets along with the service might not be enough to indicate the transfer of an economic entity. But if, for example, a service is very labour intensive, then the transfer of the workers along with the service would necessarily indicate a transfer of a business.¹³⁸ As a result, the "...mere loss of a service contract to a competitor cannot therefore by itself indicate the existence of a transfer within the meaning of the Directive."¹³⁹ The two major factors that the court identified that could turn the transfer of a service/activity into the transfer of an entity/business was the question if important assets or in the case of a labour

¹³⁵ *supra*

¹³⁶ par 13

¹³⁷ par 15

¹³⁸ That such a test could lead to abuse is painfully apparent: to determine whether there was a transfer as contemplated by the Directive, one of the most important factors that could indicate the transfer of a business in the case of the mere transfer of a service, is the question whether the workers were also transferred along with the service. Clearly, such test leaves the door open for the employer to decide whether he would like the Directive to apply or not.

¹³⁹ n.4 at 259

intensive workplace, a majority of the workforce was transferred along with the service. In conclusion, the court stated:

"The Directive does not apply to a situation which a person who had entrusted the cleaning of his premises to a first undertaking terminates his contract with the latter and, for the performance of similar work, enters into a new contract with a second undertaking, if there is no concomitant transfer from one undertaking to the other of significant tangible or intangible assets or taking over by the new employer of a major part of the workforce, in terms of their numbers and skills, assigned by his predecessor to the performance of the contract."¹⁴⁰

Before *Süzen*, there was no distinction between an activity and an entity or business and by establishing this differentiation, the court effectively limited the applicability of the Directive.¹⁴¹ The ruling was also summarised by the British Court of Appeal who claimed "that the decision in *Süzen* does represent a shift in emphasis, or at least a clarification of the law, and that some of the reasoning of earlier decisions, if not the decisions themselves, may have to be reconsidered".¹⁴² Since *Süzen* did to a degree invalidate the approach up to that time, it had the undesirable effect of making it much more difficult to state with certainty when the Directive applies.¹⁴³ At first glance it does not seem clear how this can be, especially since the facts of *Schmidt* and *Süzen* can be clearly distinguished. In *Schmidt*'s case a bank contracted out one of its ancillary functions (the cleaning of the bank) to an outside contractor. In *Süzen*'s case an outsider that provided cleaning services was replaced with another. In a case where only two parties – the contractor and the employer – are involved with the result that the service or business is contracted out and removed from under the auspices of the original employer we are faced with bilateral outsourcing. (It is also called "first generation" outsourcing.) When there are three parties involved - the original employer, the old contractor, and the new contractor – it is referred to as a case of trilateral outsourcing. This is the scenario where the old contractor loses the contract to a new contractor, usually through a process of competitive tendering. (This is also

¹⁴⁰ *supra*, n.4 at 259

¹⁴¹ Sargeant "European Court of Justice limits the scope of the Acquired Rights Directive" 1997 *British Business Law* 568

¹⁴² *Betts and others v Brintel Helicopters Ltd and KLM Era Helicopters Ltd* 1997 IRLR 366

¹⁴³ Sargeant 1997 *British Business Law* 574

referred to as "second generation" outsourcing.) From the facts it is clear that in the *Schmidt* case we had to do with bilateral or so called "first generation" outsourcing, but in the *Süzen* case we were faced with trilateral or so called "second generation" outsourcing. We might therefore argue that the decision in *Süzen*'s case is only limited to occurrences of trilateral outsourcing. In logic, however, it is impossible to make such a distinction. Whether it is first or second generation outsourcing, if what is being transferred is merely a service or function, then *Süzen* says that the transfer of this service alone is not enough to trigger the Directive.¹⁴⁴ The service can therefore only become a business capable of transfer if the appropriate assets are added on, or in the case of a labour intensive workplace having no other assets than the workforce, if an identifiable workforce is added on. The distinctive factor in the *Süzen* case is consequently that it only relates to the transfer of a service and that it does not affect the usual type of business transfer. In the latter instance, the usual factors (e.g. the extent to which premises, plant equipment, goodwill, intellectual property rights, work in progress and employees have moved across to the new employer) still apply.

The test presented in *Süzen* was incorporated shortly thereafter in the UK in the case of *Betts v Brintel Helicopters*.¹⁴⁵ In this case, which concerned the contracting out of helicopter services, the court found that because no assets or workers were transferred, the mere transfer of the function could not be seen as a relevant transfer of a business. This test was further refined in the UK in the case of *ECM (Vehicle Delivery Service) Ltd v Cox*.¹⁴⁶ On facts similar to *Süzen* – the employees being drivers and yardmen in this case – Morrison P found that the question was whether the employees were *dedicated* to the service in such a way that a transfer of the service would result in loss of employment for the employees. If this were the case, then the transfer of the service would be the transfer of an economic entity. As to the evasion of the Regulations by not transferring the workforce along with the service, Morrison P found that a purposive approach should be adopted when interpreting the Regulations with the result that it "would not be proper for a transferee to be able to control the extent of his obligations by refusing to comply with them in the first place".

¹⁴⁴ Shrubsall "Competitive Tendering, Out-Sourcing and the Acquired Rights Directive" 1998 *The Modern Law Review* 89

¹⁴⁵ 1997 IRLR 361

¹⁴⁶ 1998 IRLR 416

While this case clearly attempts to reconcile the approaches in *Schmidt* and *Süzen*, it unfortunately only adds to the confusion surrounding this subject. The reality of the current situation in EEC case law is that these two decisions are not compatible and that even though *Süzen* does represent the most recent approach it is frustratingly obscure.¹⁴⁷

In contrast, the position in South African case law is much less complicated, simply because so little has been said on the subject so far. Perhaps the confusion in the EEC and UK case law should serve as a warning to the Labour Court to establish its policy regarding outsourcing firmly at the outset, so that a change of policy half way and the resulting difficulties can be avoided.

In *Schutte & others v Powerplus Performance (Pty) Ltd & another*¹⁴⁸ the Labour Court was faced with outsourcing in the context of section 197 for the first time. The second respondent, whose main business was the renting out of vehicles, decided to sell its workshops at Isando. The applicants claimed that this resulted in a transfer of a business in terms of section 197 and that the employees at the workshops had therefore been transferred as well. While Seady AJ found that this had indeed resulted in a transfer as intended by section 197, she found that on the facts it was not necessary to decide if the "outsourcing of an activity or service is in itself sufficient to constitute a transfer of a business as a going concern".¹⁴⁹ This was mostly due to the fact that several assets as well as the workplace itself was taken over by the transferee and as a result it was not only the service or function of the workshops that was transferred.

The first time that the Labour Court actually did consider whether outsourcing of a service or function would indeed result in a transfer of a business or part of a business as a going concern, was in *National Education Health and Allied Workers Union v University of Cape Town and others*.¹⁵⁰

As part of its Strategic Planning Framework, the University decided on the outsourcing of gardening, sports ground maintenance, cleaning and related non-core activities so that it could focus its limited resources on its core activity: learning. After a process of consultation with the First Respondent, the Council of the University resolved in favour

¹⁴⁷ Harvey *Harvey on Industrial Relations and Employment Law* (1996) F/27 66.04

¹⁴⁸ 1999 ILJ 655 (LC)

¹⁴⁹ 6711 – 672A

¹⁵⁰ 2000 BLLR 803; ILJ 1618

of the outsourcing and decided on the termination of the employment of the affected employees due to operational requirements.

The Applicant approached the court and argued that the outsourcing of the affected services resulted in a transfer of a part of the University's business. As a result, section 197 applied and thereby the contracts of employment were automatically transferred to the 2nd to 5th Respondents (the contractors).

At the outset, Mlambo J confirmed that the court should adopt a purposive approach when interpreting section 197. Regard should also be had to all factors and the court should examine the substance of the transaction and not the form. After a brief examination of *Schutte* and *Foodgro* Mlambo J also noted that the court had so far held that section 197 was an "employee protection provision". After an interpretation of the relevant section, the learned judge however came to a different conclusion, finding that section 197 does not result in the automatic transfer of the contracts of employment.¹⁵¹

With regard to outsourcing, Mlambo J found it prudent to consider firstly the two leading ECJ cases on the subject, *Schmidt* and *Süzen*. After a brief analysis of these cases as well as the Directive and *Spijkers*,¹⁵² he came to the following conclusion:

"It is clear from these decisions that the acceptable approach is to examine the substance of the transaction and not the form thereof and to weigh all the factors pointing in either direction and make an overall assessment without treating any individual fact as decisive."¹⁵³

Mlambo J however continued and stated that he found a uniform approach when regarding the ECJ's decisions to be elusive, especially since there is such a difference between approaches in the *Schmidt* and *Süzen* cases. Consequently, he did not rely expressly on the approaches of the ECJ, but instead concluded that in his view, outsourcing is markedly different from the sale of a business, the legal transfer thereof or a merger. The origin of this difference lies in two factors: the fact that outsourcing is usually only for a fixed period and the fact that the outsourcing party retains some control over the outsourced services. Mlambo J therefore argues that in the case of outsourcing it is not a **business** that is transferred, but "nothing more than the

¹⁵¹ The basis of this reasoning and the merits thereof are considered in Chapter 5.

¹⁵² *supra*

¹⁵³ par 28

opportunity to perform the so-called outsourced services."¹⁵⁴ In some cases outsourcing could lead to the transfer of a business, examples of this are where there is a transfer of assets and where the outsourcing party relinquishes the power to dictate the standards of the outsourced service. On the facts of this particular case it was found that the University never transferred all the functions relating to any of the services as a whole to begin with anyway, but only parts of each and that although the outsourced services were identifiable economic entities, they shared those identities with services that were not outsourced by the University. Consequently the transaction was not considered to be a transfer as contemplated by section 197(1)(a).

Even though he rejected certain aspects of *Schutte*, Mlambo J clearly followed a very similar approach to that of Seady AJ by having regard to substance of the transaction rather than the form and in the process weighing up all the factors pointing in either direction, without seeing one factor as conclusive. What the factors were that pointed towards outsourcing of a service being a transfer in this case are not certain, but Mlambo J did clearly state that three factors pointed towards the outsourcing of a service in this case not being a transfer of a business. These three factors were the fact that only parts of the different services were outsourced, the fact that the outsourcing was not permanent and the fact that UCT retained some control over the outsourced service.

Section 197 provides for the transfer of a business or a **part** of a business. A part of a business is defined as a "separate economic entity".¹⁵⁵ On the facts of the case, Mlambo J found that none of the services that were transferred was a completely different economic entity and therefore did not qualify as even a part of a business. The effect of this is that if a service or even a business is subdivided well enough, then the transfer of these subdivided elements can never be the transfer of a business as a going concern in the terms of section 197.

The element of control has already been discussed in 3. The essence of this discussion was that the control over the employees does not necessarily vest in the employer. In the case of outsourcing we find that this is exactly what usually happens. A service that was provided by the original employer is now provided by the contractor. The

¹⁵⁴ par 32

¹⁵⁵ See 5 *infra*

contractor therefore becomes the employer of the workers that provide the service, while the original employer dictates the standards of the work that is done. The source of this control over the outsourced service is the contract between the original employer and the contractor. The contractor in turn has to make sure that *his* employees live up to the standards set by the original employer. It is submitted therefore that in the case of outsourcing, the original employer has no direct control over the employees of the contractor, but can only affect their work standard by exerting control over the contractor. Two things have to be noted at this time. One: it is quite possible that the contract may determine that the original employer has direct control over the employees of the contractor. Two: whether the original employer has direct or indirect control over the employees of the contractor is irrelevant for the purposes of providing whether there was a *transfer* as provided for in section 197 – for these purposes there need only be an old and a new employer - as there clearly are in the case of outsourcing – simply because the one exerting the control need not be the employer. The question that remains then is if the retention of control on the part of the original employer could have the effect of making what is being transferred not a *business*? Mlambo J stated that this is indeed so, but exactly why is not clear. What is clear, is that this requirement would have far reaching consequences as almost all cases of outsourcing would have some element of this control incorporated. This is true to the very nature of what outsourcing is: very few companies would actually contract out a service if they could not have some sort of say in the quality of the service that is to be provided. Seeing that the original employer would be loath to give up such control, it would seem that outsourcing would as a result in most cases be excluded from the workings of section 197.

Thirdly, concerning the stability of the transferred business, Mlambo J differentiated outsourcing from a sale or legal transfer by stating that outsourcing is not a "permanent" transfer: it only takes place according to a contract and is of limited time. At the end of such a period, it is up to the outsourcing party to invite further tenders or even to perform the services itself. Mlambo J argues that in the case of outsourcing, what is transferred is merely the "opportunity" to perform the service, and therefore not a business in itself. This argument relates to the stability of the economic entity that is transferred and evidence is to be found of similar thinking in EEC case law.

In *Lederned Hovedorganisation, acting for Rygaard v Dansk Arbejdsgiverforening, acting for Stro Molle Akustik*¹⁵⁶ work was transferred between contractors on a construction site. After accepting the test proposed in *Spijkers*, (whether the "entity in question [retained] its identity") the court found that such a test presupposes "that the transfer relates to a stable economic entity whose activity is not limited to performing one specific works contract".¹⁵⁷ The court therefore found that the transfer of uncompleted building work was not a transfer as contemplated by the Directive. It has been argued that this case should only be interpreted in the light of its specific facts: a one-off building contract. Applying this case to outsourcing in general, would for example result in the finding that most case of outsourcing would not qualify as a transfer within the ambit of the protective legislation, seeing that almost all forms of outsourcing are only for a limited time.

The effect of *NEHAWU*'s case is that outsourcing would as a rule not qualify as a transfer within the scope of section 197, because what is being transferred does not amount to an independent business: the outsourcer stays in control over the outsourced activity and the outsourcee has only a limited "opportunity" to provide the service. Section 197 would however apply on the off chance that the outsourcer gives up this control or where there is a transfer of assets along with the service. But are these the only exceptions? Are there any other scenarios where section 197 should apply to outsourcing? It is submitted that there are.

Although *Mlambo J* never refers directly to ECJ decisions in his conclusion, it is quite apparent from the wording of his judgement that he adopted many of the concepts developed in these cases. Terms such as "identifiable economic entities" and especially the differentiation between the transfer of a business and the transfer of a service were all born of the ECJ's interpretation of the Directive. In the light thereof it should be essential that these concepts be interpreted in the light of these decisions. For example, *Mlambo J* refers to two instances where the outsourcing of a service might result in the transfer of a business: the transfer of assets and the relinquishing of control by the outsourcer. It is quite clear that the transfer of assets-exception alludes to the *Süzen* case, but as has already been noted, this is only one half of the test proposed in *Süzen*. The second half of this test refers to the transferral of the workforce in a labour

¹⁵⁶ Case C-48/94 1996 IRLR 51

¹⁵⁷ *supra* n.2 56

intensive workplace – a test that has been considered paradoxical and quite controversial¹⁵⁸ especially since the employers can as a result choose whether or not they would like the Directive to apply. Perhaps the controversy surrounding these aspects of the *Süzen* case kept Mlambo J from referring to this exception, but considering his interpretation of the workings of section 197, it is not clear why he should do so. The reason why the identifiable workforce-exception in *Süzen* is problematic is because the Directive affects the automatic transfer of the contracts of employment on the transfer of the business. As a result, the test in *Süzen* has the effect that the transfer of the workforce along with the transfer of a service is seen as a transfer within the ambit of the Directive. This results in the automatic transfer of the contracts of employment. Such a result is problematic because only the actual transfer of the contracts in such a circumstance would therefore lead to the automatic transfer of the contracts and consequently the Directive can be side-stepped by not transferring the workforce. On Mlambo J's interpretation of section 197, there is no such thing as the automatic transfer of the contracts of employment: the section only dictates that the terms of the transferred contracts should remain the same, unless agreed to otherwise, and that the consent of the employee is not necessary for such a transfer in the case of the transfer of the business as a going concern. Therefore, the transfer of the workforce-test that is proposed in *Süzen* would not be problematic if applied to Mlambo J's interpretation of section 197. For example, if a labour intensive gardening service – that does not make use of significant assets to perform its service - is outsourced, then such outsourcing would not attract the working of section 197. But if a significant number of the identifiable workforce is transferred along with the service, then such a transfer of a service would according to the test in *Süzen* result in the transfer of a business, hence section 197 should apply. On Mlambo J's interpretation, such application of section 197 would not be problematic, simply because the only purpose that section 197 would have in such a case would be the protection of the terms in the transferred contracts of employment. As a result, the labourers who were not transferred would not be able to claim that their contracts had been transferred as well. Surely such an exception could only be in the interest of all the parties involved. The (new) contractor would be acquiring skilled labour without the possibility of being forced to employ more employees than he can afford or as a result having to make large

¹⁵⁸ Shrubbsall 1998 *The Modern Law Review* 87

redundancy payments, while the transferred employees can rest assured that they would not be employed on less favourable terms.¹⁵⁹ Currently, however, such protection would not be afforded to labourers transferred along with a labour intensive service. It is submitted that if Mlambo J's interpretation of section 197 is accepted, then such an exception would be essential to provide for fair labour practices in the case of outsourcing of labour intensive services.

The Amendment Bill proposes to simplify this matter slightly. The new section 197 is set only to apply if

"an economic entity, consisting of an organised grouping of resources, that has the object of performing an economic activity is transferred; and

"the economic entity retains its identity after the transfer."¹⁶⁰

This is based on the principles set out in *Süzen* and accepted in article 1.1(b) of the Directive 98/50/EC. All the factors that have been mentioned so far (control, transfer of assets etc.) would only serve to help determine whether what has been transferred was indeed an economic entity.

Finally, it is necessary to note that the term "business" and "going concern" are virtually synonymous. For all intents and purposes the business is the going concern. To illustrate this point, we can consider that section 197 might just as easily have referred only to the "transfer of a going concern" or just the "transfer of a business", without the interpretation being much effected by it. As will appear from the next section, there does seem to be some sense in this approach.

6 TRANSFER OF A BUSINESS AS A GOING CONCERN

Section 197 envisages the scenario where the business is transferred as a going concern.¹⁶¹ We have already established what entails a business and a transfer for the purposes of section 197. It is now necessary to piece together what exactly the *transfer of a business as a going concern* means.

¹⁵⁹ Such an assurance is of course subject to section 196(3) of the LRA that states an employee who unreasonably refuses to accept an offer of alternative employment with the current employer or another employer will not be entitled to severance benefits.

¹⁶⁰ clause 47(a) 197(2)(a) and (b)

¹⁶¹ s197(1)(a) and (b)

The Directive and the Regulations provide for the transfer of a business. The term “going concern” itself is not expressly part of the wording of the Directive or the Regulations. Long before the passing of the Regulations, however, there was reference to this “going concern” in English case law. In *Kenmir Ltd v Frizzell*¹⁶² Lord Widgery, when faced with the question of whether a business was transferred or not, proposed the “going concern” test. This approach was approved in *Lloyd v Brassey*.¹⁶³

“In deciding whether a transaction amounted to the transfer of a business, regard must be had to its substance rather than its form, and consideration must be given to the whole of the circumstance, weighing the factors which point in one direction against those which point in another. In the end, the vital consideration is whether the effect of the transaction was to put the transferee in possession of a going concern the activities of which he could carry on without interruption. Many factors may be relevant though few will be conclusive in themselves. Thus, if the new employer carries on business in the same manner as before, this will point to the existence of a transfer, but the converse is not necessarily true because a transfer may be complete even though the transferee does not choose to avail himself of all the rights he acquires thereunder. Similarly, an express assignment of goodwill is strong evidence of a transfer of the business but the absence of such an assignment is not conclusive if the transferor has effectively deprived himself of the power to compete. The absence of the assignment of premises, stock-in-trade or outstanding contracts will likewise not be conclusive if the particular circumstances of the transferee nevertheless enable him to carry on substantially the same business as before.”

This is necessarily a test that has to be applied on a case by case basis, weighing up the different factors in each case to determine if the transfer was a transfer of a going concern. The one certainty of this test is, however, that transferee/new employer must be placed in the control of “substantially the same business as before”.¹⁶⁴ It is this aspect of the test that seems very similar to the later approach by the ECJ when

¹⁶² 1968 1 All ER 414

¹⁶³ 1969 1 All ER 382

¹⁶⁴ See for example also *Lloyd v Brassey supra* where Lord Denning asked the relevant question: “Does the business remain the same business but in different hands.”

considering the Directive. In the case of *Spijkers v Gebroeders Abattoir CV*¹⁶⁵ the ECJ found:

“It is necessary to determine whether what has been sold is an economic entity which is still in existence, and this will be apparent from the fact that its operation is actually being continued or has been taken over by the new employer, with the same economic or similar activity.”

The test that evolved in this case was therefore if the business retained its identity.¹⁶⁶ The facts that the ECJ found could be of importance during such an enquiry are: the type of the business or undertaking; whether or not the tangible assets of the business are also transferred, the value of such transferred assets, whether or not the majority of the employees and/or customers are also transferred, the similarity of the activities carried on before and after the transfer, and also if such activities were suspended and if so, for how long. When considering these factors, it becomes clear that this test is very similar to the earlier "going concern"-test.

A clear interpretation of the "transfer of a business as a going concern" was made for the first time in South Africa in the case of *Schutte & others v Powerplus Performance (Pty) Ltd and another*.¹⁶⁷ Before this case, the court only made obiter remarks concerning the meaning of the phrase "as a going concern". In *Manning v Metro Nissan – a Division of Venture Motor Holdings Ltd*¹⁶⁸, for example, the Labour Court held that the phrase "as a going concern" was traditionally adopted to distinguish the sale of a business from the sale of assets or the sale of shares. (In the latter instances section 197 does not necessarily apply.) In the case of the sale of a business, the central question was whether the business was "active and operating" so that the purchaser may continue with the operation if he so desired. That a transfer might entail more than the mere *sale* of a business was not considered.

In other instances, the court considered several factors without applying a recognisable test. The case of *Miriam Kgethe & Others v LMK Manufacturing (Pty) & another*¹⁶⁹, for example, the Labour Appeal Court (LAC), mentioned a few factors that led it to

¹⁶⁵ 24/85 1986 2 CMLR 296

¹⁶⁶ See for example *Dr Sophie Redmond Stichting v Bartol* c-29/91 1992 IRLR 366 ECJ

¹⁶⁷ 1999 2 BLLR 169 (LC)

¹⁶⁸ 1998 ILJ 1181 (LC)

¹⁶⁹ 1998 ILJ 524 (LAC)

conclude that a business or a part thereof had been transferred as a going concern. This case involved a dispute about the disclosure of information. The Labour Appeal Court found that if there had been a transfer of a business as a going concern, then disclosure of the agreement of sale between the first and second respondents would be ordered in order for the employees to be able to protect their rights. In order to support its finding that such a transfer had indeed taken place, the court relied on several factors, most notably the fact that the second respondent (transferee) proceeded with business on the same premises as where the transferor had conducted his business (even using the same telephone number).

The first time that a definite test for a transfer of a business as a going concern was proposed by the Labour Court was in *Schutte & others v Powerplus Performance (Pty) Ltd and another*.¹⁷⁰ This case concerned the contracting out of a workshop to another party (the second respondent). While the applicants maintained that there had been a transfer of a business as a going concern, the respondents maintained that it had closed down its workshops and that it had contracted out these functions. In order to determine the applicability of section 197, Seady AJ had to conduct a detailed analysis of foreign law in order to discover what the essence of the "going concern" was. Having regard to cases such as *Kenmir v Frizzel*¹⁷¹ and *Spijkers*¹⁷², she came to the following conclusion:

"An approach for determining whether a business has been transferred can be distilled from the discussions of the ECJ and the English courts. It is an approach that examines substance and not form; that weighs the factors that are indicative of a transfer of a business against those that are not; that makes an overall assessment of the facts, not treating any one as conclusive in itself."¹⁷³

Seady AJ concluded that such an approach would be consistent with the remarks made by the LAC in *Kgethe*.¹⁷⁴ On the facts she found that there had indeed been a transfer of the business as a going concern and that section 197 did apply.¹⁷⁵ The factors that were of importance in this case were: the in-principle agreement to sell the workshop,

¹⁷⁰ 1999 2 BLLR 169 (LC)

¹⁷¹ *supra*

¹⁷² *supra*

¹⁷³ 667J – 668A

¹⁷⁴ *supra*

¹⁷⁵ For a more detailed discussion of this case, see 7.2 regarding out-sourcing.

the terms of the working agreement, the transfer of the majority of the workshop employees, the use of the same premises, the continuation of the business activities without any interruption as well as the intended transfer of the assets and equipment.¹⁷⁶

The test that Seady AJ advocates envisages that a transfer of a business need not necessarily always flow from a sale of a business¹⁷⁷; the existence or not of an agreement of sale is not a decisive factor in determining this. Similarly, the absence of any agreement to **transfer** might also not be enough to prohibit the court from finding that there had indeed been a transfer where section 197 should apply. The benefits of such a test is that it is so related to the particular facts of each case, that the court is allowed enough discretion to intervene where it seems that an attempt has been made so circumvent section 197.¹⁷⁸

While the test that was developed by Seady AJ was almost solely based on the approaches in the ECJ and the UK, it is necessary to note that neither the Directive nor the Regulations make any mention of the concept of a "going concern". Does the inclusion of this term in section 197 have any specific meaning?

In *National Education Health and Allied Workers Union and University of Cape Town & others*¹⁷⁹ Mlambo J when considering the phrase "going concern" commented that it meant nothing more than "continue in actual operation". The basis for this finding seems to be the case of *General Motors SA (Pty) Ltd v Besta Auto Component Manufacturing (Pty) Ltd & Another*¹⁸⁰ where Kannemeyer J quoted with approval the following passage from a turn of the century Australian judgement:

"The words 'as a going concern' are merely intended to mean that the shop is being kept open instead of being closed up, and that the customers are being kept together, so that if the purchaser wishes to keep on the business he can do so; that ... the vendors only propose to sell the stock and fixtures, and they leave it to the person who buys to decide whether he will carry on the business or not, and that meanwhile, lest the purchaser should care to carry on the

¹⁷⁶ 672C

¹⁷⁷ On the facts, for example, there was uncertainty if the workshop would ever be sold. Furthermore, the existence of an agreement of sale could not be proved decisively. Still, Seady AJ found that there had been a transfer of a business as a going concern.

¹⁷⁸ Particular problems arise with the circumvention of s197 when there was a transfer of shares. See 7 1 and also *Ndima & others v Waverly Blankets Ltd* 1999 ILJ 1563 (LC)

¹⁷⁹ 2000 ILJ 1618 (LC); 2000 BLLR 803 (LC)

¹⁸⁰ 1982 2 SA 653 (SE)

business, they keep it open till he takes his choice. In some cases they shut up the shop prior to the sale; in other cases they keep it 'going' so that the trade may not be broken and dispersed."¹⁸¹

This echoes the earlier finding in *Manning*,¹⁸² where the court also relied heavily on *General Motors*. In *Schutte* Seady AJ, however, argued convincingly that *General Motors* is only of limited applicability since it arose in the context of the sale of the business alone and not in the broader range of circumstances contemplated by section 197.¹⁸³ It seems that Mlambo J has, on the contrary, accepted this approach to be binding on all types of transfers, not just the sale of a business.

Despite these superficial differences it is clear that in his general approach Mlambo J accepted the test for the transfer of a business as a going concern that was proposed by Seady AJ. Their different interpretations of the term "as a going concern" did not seem to influence their general approach.

It seems that the term "as a going concern"-itself only finds applicability in extreme cases where the business is closed down prior to the transfer - whether this is only limited to cases where the transfer would take place by way of a sale is moot. Would such a closing down of the business result in the immediate non applicability of section 197 or should this only be a factor that must be weighed up against the other factors that might indicate that a transfer of a business will take place? If this is an overriding factor, for what period of time should a business be closed before it would be considered not to be a "going concern" anymore? So far, the Labour Court has not provided any detail.

It is respectfully submitted that to elevate the fact whether the business is closed down or not to the one single negating factor that could exclude the workings of section 197 would be contrary to the general approach accepted by the Labour Court in *Schutte* and *NEHAWU*. It is further submitted that the term "as a going concern" relates less to the interpretation of section 197 than it does to the effect of this section. It would seem to me that section 197 has the effect of letting the business being transferred as a going concern, as it allows for the automatic transfer of the contracts of employment, which

¹⁸¹ *Ferne v Wilson* 1900 26 VLR 437

¹⁸² *supra*

¹⁸³ 665G

ensures that the business can stay active and operating through the transferral. The fact whether a business is closed down should rather relate to whether what is being transferred is actually a "business" or not.

Despite the questionable value of the term, the Amendment Bill also contains reference to the "going concern".¹⁸⁴

7 CONCLUSION

There are several elements that need to find application before section 197 can be considered to apply to a certain situation. While some of these terms are common to labour law ("employer", "employee", "business") some are not ("transfer" and "going concern").

The term *employee* is defined by the LRA – with certain exclusions contained in section 2. The definition in section 213 serves to differentiate between an employee and an independent contractor – the latter not protected under the LRA. The workings of section 197 are limited to only the contracts of employment of the employees concerned.

The term *employer* in turn is not defined. The court therefore has to look at the real situation –leading in exceptional cases to a piercing of the corporate veil. While the court would therefore rather consider the substance than the form of the relationship of the parties to determine the identity of the real employer, it would not necessarily find that the one exerting control over the employees is the actual employer. The LRA further does not apply to a non South African employer.

In determining what results in a transfer or not, the court follows a very robust approach. Instead of focusing on the different kinds of transfer, the court will find that section 197 finds application if a business moved in any way from an "old" employer to a "new" employer. Direct and indirect transfers – even without any of the parties intending for there to be a transfer – therefore qualify in terms of section 197.

A business or undertaking is a well known concept in labour law. In the case of section 197 it is submitted that the concept of business should be extended to include non profit making organisations as well. Defining the essential element of a business has proven

¹⁸⁴ clause 47(a)197(1)(b)

to be problematic, especially when faced with the transfer of only assets, shares or the transfer of a service as is the case with outsourcing.

A transfer of assets will not entail a transfer within the scope of section 197, unless these assets can be seen as a "going concern". A transfer of shares is always excluded from the workings of section 197, simply because there is no change in employer. It should be noted also that the current wording of the section excludes most schemes of arrangement from the protection afforded by section 197. In the case of outsourcing, the most important question is if a service can be seen as a business. The current position is that something more is needed: either a transfer of assets along with the service or a loss of control by the outsourcer. It is submitted that a transfer of employees along with the service should have the same effect.

The current approach as to whether a business is transferred as a going concern takes cognisance of all the factors that might indicate a transfer and weighs them up against the factors that indicate the opposite. Such an approach is firmly based in the specific facts of each case.

Finally, with regard to the concept transfer of a business as a going concern, it is submitted that the words "going concern" adds very little to the meaning of this section, excepts that it serves to distinguish between a transfer of a business and the transfer of assets.

CHAPTER 5

THE EFFECTS OF SECTION 197

1 INTRODUCTION

Section 197 guarantees continuity of employment on the transfer of a business and also provides for the maintenance of the terms and conditions of the contract of employment subject to any changes brought about by agreement. This represents a remarkable change from the common law position that required a complicated process of novation and negotiation to ensure any continuity of employment. Section 197 itself does not expressly provide for such negotiations or even disclosure of the transfer even though it is arguable that such duties should exist. Perhaps the most important result of section 197 is that the employee is provided with greater job security in a changing business environment. In this context, the connection between dismissals and section 197 will also be discussed in this chapter.

The Amendment Bill proposes to regulate the effects of section 197 in much greater detail. The significance of these suggestions on each of the current effects will also be discussed.

2 CONTINUITY OF THE CONTRACT OF EMPLOYMENT

The most revolutionary and also most controversial effect of section 197 is that it provides for the continuity of the contract of employment by providing for its automatic transfer on the transfer of a business. Section 197 accomplishes this by effecting a change in the parties to the contract, without their consent. This concept varies greatly from the common law position and it will be some time before its full effects are clarified in our law. Determining what exactly this continuity of employment entails, as well as deciding which employees are affected by the section and whether they have a right to object to the transfer or not are also very important questions relating to this issue, which will be discussed in this chapter.

2.1 AUTOMATIC TRANSFER

It is clear from what has gone before that the Directive and the Regulations provide for the *automatic* transfer of the contract of employment on the transfer of the business. Although it is widely accepted that section 197 was modelled on these provisions, there

is currently still no consensus as to whether section 197 provides for the automatic transfer of the contracts of employment or not.

Shortly after the enactment of section 197, the leading opinion was that it did not affect the automatic transfer of the contracts of employment. It was argued that because this position would represent such a serious deviation from the common law, the legislator would have provided for it more clearly.¹⁸⁵ More importantly, it was argued that the automatic transfer of contracts of employment could not provide for job security for employees on the transfer of a business simply because prospective purchasers would not be interested in taking on all the existing employees along with the business. Businesses – especially those in financial difficulties – would therefore be less easily transferred and as a result failure and the loss of jobs would be more prevalent.¹⁸⁶

Other writers have argued that based on the stated purpose of the section as well as the location thereof under Chapter 8 of the LRA –dealing with unfair dismissals - which the section clearly does provide for the automatic transfer of the contract of employment.¹⁸⁷ Until recently this was also the position generally accepted by the Labour Court, although initially it was only implied. For example, in *Miriam Kgethe & others V LMK Manufacturing (Pty) Ltd & another*¹⁸⁸ the Labour Appeal Court stated:

"If in fact a transfer as a going concern had been effected, the appellants would be entitled to the benefits accorded to them in terms of section 197, and they would be entitled to reject any other benefits which either of the respondents sought to accord them in lieu thereof."¹⁸⁹

The appellants in this case were the employees working at the transferred business. Since there had been no agreement between the new employer and the employees to transfer the contracts of employment, their only basis for claiming protection under section 197 was the fact that they were working at a transferred business. By finding that the transfer of such a going concern would affect these employees in terms of the

¹⁸⁵ Le Roux "Transferring contracts of employment. Implications surrounding the sale of a business under the new LRA" 1996 *Contemporary Labour Law* 13

¹⁸⁶ Le Roux 1996 *Contemporary Labour Law* 16

¹⁸⁷ Smit "Word Werksekuriteit Gewaarborg in die lig van Artikel 197 van die Wet op Arbeidsverhoudinge 66 van 1995?" 1997 *TSAR* 549

¹⁸⁸ 1998 ILJ 524 (LAC)

¹⁸⁹ par 37

section, the Labour Appeal Court clearly implied that section 197 does provide for the automatic transfer of the contracts of employment.

This matter was once again addressed by the LAC in *Foodgro v Carol Keil*¹⁹⁰ when it confirmed that:

"Section 197(1)(a) and (b) provides for the *automatic* transfer of an employee's contract of employment upon transfer of the business, trade or undertaking in the circumstances set out in the section."¹⁹¹ (own emphasis)

In both of these cases the finding as to whether section 197 provides for the automatic transfer of the contracts of employment or not was, however, not essential to the dispute. *LMK* dealt with the duty to disclose information to the employees upon a transfer, while *Foodgro* concerned the continuity of employment provided by section 197(4). The first case where the automatic nature or not of the transfer would have affected the finding of the court, was in the groundbreaking case of *Schutte & others v Powerplus Performance (Pty) Ltd & another*.¹⁹²

In this case Seady AJ quoted the Explanatory Memorandum that accompanied the draft Labour Relations Bill. This document referred explicitly to the "automatic transfer of contracts of employment", but mysteriously also provided that such a transfer would only take place, "provided that the employees consent to the transfer". It is submitted that the reference to an automatic transfer in this context is clearly senseless, as an "automatic" transfer that is subject to someone's consent cannot be automatic! Why the wording of the Memorandum was so confusing is unfortunate, because clause 92(2) of the Draft Bill stated unequivocally "the contracts of employment ... shall automatically be transferred to the transferee."¹⁹³ Despite this discrepancy or perhaps because of it, it does not seem that Seady AJ based her finding solely on this document. It is submitted that the Memorandum is only of limited assistance in helping us to understand section 197, as significant changes in the wording of this clause took place when it was

¹⁹⁰ 1998 ILJ 524 (LAC)

¹⁹¹ par 25

¹⁹² 1999 ILJ 655 (LC)

¹⁹³ Clause 92(1) expressly provided that the consent of the employee was not necessary in cases such as envisaged by clause 92(2).

included in the LRA in the form of section 197. In the process, any reference to an automatic transfer in section 197(2)(a) was lost.¹⁹⁴

The primary reason why the honourable judge found that section 197 provides for the automatic transfer of the contracts of employment seems to be the presumption that the primary purpose of the section is the protection of "the rights of employees during certain processes of business restructuring."¹⁹⁵ This line of reasoning assumes that it is only possible to protect the rights of employees during transfer of a business if the contracts of employment are automatically transferred. In *Foodgro* the Labour Appeal Court found it necessary to elaborate on exactly why section 197 is aimed at the protection of employees. These arguments revolve around the fact that section 197 does not in effect procure any advantages for business that it did not have before, but that the automatic transfer does secure advantages for the employees not previously enjoyed by them.¹⁹⁶ More convincingly, the LAC claims that similar provisions in foreign jurisdictions are specifically geared towards the protection of employees. In this regard Froneman DJP refers to the Directive and the Regulations. While these provisions were undisputedly forged to protect the employer, it should be noted – as Froneman DJP did in para 18 – that the wording and social context of these provisions differs somewhat from their South African counterpart. On its own therefore, this fact does not carry too much weight, but it does act as an important contributory factor which it seems was also relied on by Seady AJ in *Schutte*.

Although the basis of these arguments does not always seem sound, one does get the general idea from the concept around which section 197 was formulated, especially in view of the wording of the Draft Bill, that the legislator did intend for the automatic transfer of the contracts of employment. By some mistake or oversight perhaps, this intention was not clearly conveyed by the wording of the section. This is a matter that can be corrected and probably will be in the near future - the Amendment Bill clearly and unambiguously provides for the automatic transfer of the contracts of

¹⁹⁴ Interestingly enough, subsection 2(b) does make reference to an automatic transfer. This situation is discussed in chapter 6.

¹⁹⁵ Par 30

¹⁹⁶ It is respectfully submitted that such a line of argument is not sound. In *Schutte* it is argued that an automatic transfer takes place because section 197 is an employee protection provision. In *Foodgro* this argument is accepted and then the court goes further to motivate that section 197 is an employee protection provision mostly because it provides for the automatic transfer of contracts of employment. This is a textbook example of a syllogism.

employment.¹⁹⁷ Until such time, it seems that the Labour Court is quite content to stretch the limits of judicial interpretation by finding that the section does indeed provide for the automatic transfer of the contracts of employment. This approach has recently come under question.

In *NEHAWU v UCT*¹⁹⁸ Mlambo J strongly criticised the current approach of the Labour Court. To prove his argument that the wording of section 197 does not provide for the automatic transfer of businesses in the scenario contemplated in section 197(1)(a), he proceeded to systematically lay bare the inadequacies of the arguments already mentioned to the contrary. Firstly he argued that section 197 does not provide blanket protection of jobs where businesses are transferred.¹⁹⁹ The basis for this argument is found in the wording of the section. Since the section is essentially concerned with the transfer of the contracts of employment *without the consent of the employee*, Mlambo J reasons that section 197 therefore *only* provides for instances where the consent of the employee is absent. The consent of the transferor and transferee, as required by the common law, would therefore still be a prerequisite for the transfer. If interpreted this way, the section provides that on the transfer of a business as a going concern, the consent of the employee is not necessary for the transfer of the contract of employment to the new employer (as provided by section 197(1)) and the terms of employment remain unchanged, unless agreed to otherwise (as provided by section 197(2)).²⁰⁰ There is therefore no automatic transfer of contracts as neither the transferor nor the transferee is compelled by section 197 to transfer the contracts.²⁰¹ As a result, Mlambo J finds:

"The employee protection alluded to by Seady AJ and Froneman DJP is only relevant where employment contracts are transferred without the employee's consent."²⁰²

The employees are therefore only protected by section 197 as long as their consent to the transferral is lacking. Since there is no automatic transferral of the contracts of employment on such an interpretation, the employers can decide which contracts they

¹⁹⁷ clause 47(a) re proposed section 197(3)(a)

¹⁹⁸ *supra*

¹⁹⁹ par 17

²⁰⁰ par 16

²⁰¹ par 19

²⁰² par 17

would want to transfer and which not. Mlambo J addressed arguments that this would lead to inequitable results in paragraph 22 of the judgement. He compares the improved productivity and viability that results from the streamlining of the business during restructuring by the employers to the unions' pursuit of improved terms and conditions for their members. The only problem would be that the right to strike would not be open to employees to fight restructuring that would lead to job losses. Mlambo J concludes obiter that perhaps this should not be so:

"In my view the right to strike should be open to employees whose employer transfers his business and elects to retrench rather than redeploy or transfer their contracts of employment. I see no reason why the employees concerned should not prevail on their employer to do what in their opinion is in their best interest and where no agreement is achieved to be allowed to strike to force the employer's hand."²⁰³

Mlambo J's interpretation of the wording of section 197 is strictly logical and it is submitted quite sound. It lays section 197 bare for the disjointed, badly formulated piece of legislation that it is. Surely the legislator could not have intended to provide for an automatic transfer in the case of insolvency, but not for a transfer of an undertaking in normal turn of business. Such a position would prove little if no improvement over the draconian common law position, leaving the employees out in the cold, something that is entirely against the spirit and wording of the LRA. On this aspect, section 197 is in need of urgent amendment and hopefully the Amendment Bill will remain unchanged on this aspect.

Fortunately, for the moment, *UCT* serves as little more than a warning of things to come failing such an amendment, because even though Mlambo J disagrees with Seady AJ in *Schutte* that section 197(1)(a) provides for the automatic transfer of employment contracts, he is still bound by the Labour Appeal Court decision in *Foodgro* wherein Froneman DJP accepted the former position. For the time being, therefore section 197 still provides for the automatic transfer of the contracts of employment upon the transfer of the business as a going concern in the South African law.

²⁰³ par 22

2.2 CONTINUITY

In *Carol Keil v Foodgro*²⁰⁴ the question arose whether the employer and employee could by agreement cause the transfer of the business to interrupt the continuity of the employment of the employee who would be transferred along with the business. On the facts, the employee had signed a letter of appointment with the new employer after being transferred. The LAC found that this agreement could not interrupt her continuity of employment as it was expressly forbidden by section 197(4). The court found that while "all the rights and obligations between the old employer and each employee at the time of the transfer"²⁰⁵ could be varied by agreement, the employee's continuity of employment could not. With reference to *Macer v Abafast Ltd*²⁰⁶, Froneman DJP held that the continuity of employment is neither a right nor an obligation between the old employer and employee, but merely a calculation and a fact. Section 197 therefore effectively ensures the continuity of employment on the transfer of the business, even when the terms of the contracts of employment are varied by agreement. The Amendment Bill makes similar provisions in clause 47(a) re proposed section 197(3)(c).

2.3 WHICH EMPLOYEES ARE TRANSFERRED?

As long as it remains that section 197 provides for the automatic transfer of the contracts of employment, it would always have to be determined exactly which employees are transferred. This position can be very problematic – especially since the section does not provide an express guideline according to which the employees for the transfer are chosen. As a result, such measures should be deduced from the wording of the section.

Firstly, it is clear that the transferred parties should be *employees* who have concluded a contract of employment with the initial employer or transferor. According to the LRA the concept "employee" is wider than in most foreign jurisdictions. For example, an employee that is unfairly dismissed is still considered to be an employee.

Consequently, the unfair dismissal of an employee prior to the transfer would not

²⁰⁴ *supra*

²⁰⁵ s197(2)(a)

²⁰⁶ 1990 IRLR 137 (EAT)

In this case the EAT held that the continuity of employment is purely a question of calculation based upon the findings of facts.

preclude the transfer of that employee and there need not be made specific reference to such an occurrence.²⁰⁷

The important moment to determine when employees are transferred seems to be the moment of the transfer of the business²⁰⁸ – all persons that have the status of employee at that moment would be transferred. While this poses no problem to a normal transfer of a business, it is foreseeable that problems might arise where a transfer takes place after the insolvency of the old employer, as insolvency ends all contracts of employment. To overcome this problem, the legislator provided that the contracts of employment that existed "immediately before" the insolvency be transferred.²⁰⁹ The critical moment in such a situation is therefore not the moment of the insolvency itself, but that fraction in time before it.²¹⁰

The Amendment Bill proposes to alter this position drastically. In the case of a normal transfer of a business, clause 47(a) re proposed section 197(3)(a) provides that the contracts of employment in existence immediately before the transfer are transferred to the new employer. The critical moment in this case is now the fraction in time before the transfer. In the case of insolvency, though, the legislator proposes to provide a whole new section 197(A) that would regulate this transfer in detail, having the effect that insolvency would no longer terminate the contracts of employment. This position will be discussed in Chapter 6.

The questions still remains how do we determine exactly which employees are transferred? (This is a question that has not been addressed by the Amendment Bill either.)

In the case of the transfer of the whole business, it would be easy to conclude that all the employees would be transferred along with the business. On the other hand, the

²⁰⁷ Such an unfair dismissal would usually take place as a result of the transfer itself. Employees can claim relief under s188 and s197. When the court finds that the dismissal was unfair, s197 will result in the reinstatement of the employees in the service of a new employer. See *Schutte supra*.

²⁰⁸ See for example the Regulations that require that the transferred employees need to be employed by the transferor "immediately before" the transfer. Such an approach is logically correct, because at the moment of the transfer itself, the contracts will be transferred to the new employer. The old employer should therefore not be considered to be the employer at the time of the transfer, but rather the fraction in time before it.

²⁰⁹ The wording of Regulation 5(3) of the United Kingdom, which is remarkably similar, probably served as inspiration for this particular concept.

²¹⁰ In practice this is a very problematic situation, as the business is usually only transferred quite a while after the actual insolvency. The status of the contracts of employment until such time is as a result a very controversial topic. This will be discussed in Chapter 6.

transfer of only a part of a business could be very problematic. In such a situation, only a portion of the employees would be transferred. Determining which employees should be transferred and which should stay is no easy task. The guideline that is employed by the ECJ is whether the employee could be said to have been assigned or allocated to that part of the business that is transferred.²¹¹ This is a factual question. In *Duncan Web Offset (Maidstone) Ltd v Cooper*²¹² the British EAT provided obiter guidelines as to how this "assignment" was to be established in three different situations. Firstly, where X transferred part of the business to Y, then the ECJ test should be applied, with regard to all the relevant factors. Secondly, where X employed workers to work on Y's business and Y transferred this business to Z, then the Regulations would prima facie not apply. Special regard would however be given to cases where devices such as service companies and other complicated group structures were used to evade the Regulations. Finally, where X was one of a group of companies and employed people that worked for some of the other companies in the group as well, the transferral of the X's business to Y would normally result in the transferral of these employees as well. Such a finding is however reliant on the amount of work that the employees do for the other companies in the group: if a high proportion of the employee's work is done for the other companies, then it would seem that the employee would not be transferred. The basis of this finding is the protective purpose of the Directive for the employee.²¹³ Therefore, if it would seem that if the employee does so much for other businesses that the transfer of the business in which he was originally employed to work would not result in her redundancy, then the employee would not be transferred along with the business. For example, if a part of a business were transferred, then the administrative staff of the business would usually not be transferred along with that part of the business, because they would not be made redundant by such a transfer. If one of these administrative personnel were however exclusively employed in that part of the business, or if the transfer of the part of the business would result in that personnel becoming redundant, then it would seem that that administrative employee would be transferred along with the business.

²¹¹ *Botzen v Rotterdamsche Droogdok Maatschappij BV* 186/83 1986 2 CMLR 50 ECJ

²¹² 1995 IRLR 633 EAT

²¹³ *Harvey Harvey on Industrial Relations and Employment Law* (1996) F/48 [143]

In *Foodgro* the Labour Appeal Court stated clearly that section 197 is an employee protection provision.²¹⁴ Therefore such an interpretation of section 197 would be acceptable in South African labour law. To determine whether an employee is assigned to work in a certain business, the courts would have to assess whether on the facts the non-transferral of the employee would lead to redundancy or a drastic change in duties. In determining this, the court should adopt a flexible approach, having regard to the protective purposes of the section and also being mindful that corporate structures are not being used to thwart this purpose.

2.4 RIGHT TO OBJECT TO TRANSFER

Section 197 does not explicitly provide the employee with a right to object to the transferral of his contract of employment. This position stands in contrast to the common law principle that the employee must have freedom to choose whom he will serve, as advocated in *Nokes v Doncaster Amalgamated Collieries*.²¹⁵ Although it has been established that section 197 does alter the common law position with regard to the transferral of contracts of employment on the transfer of a business as a going concern, it has not yet been established without doubt that the section intends to deny the employee his right to choose for whom he works.

The Directive also does not contain reference to such a right. In *Katsikas v Konstantindis*²¹⁶ however, the ECJ found that the Directive was not to be construed as obligating the employee to continue the employment relationship with the transferee. In that case, the employee worked as a chef in a restaurant. When the restaurant was sold, the employee refused to work for the new owner, resulting in his dismissal by the transferor. A dispute arose as to whether the transferor was actually the employer at the time of the dismissal, since it took place *after* the transfer of the business. The court found that nothing in the Directive prevented an employee from objecting to the transfer. Accordingly, the employee had by his own choice not been transferred. Such a finding is in line with the German BGB that provides for an automatic transfer but which has also been interpreted to allow the employee to object to such a transfer.²¹⁷

²¹⁴ This point was discussed in chapter 4.

²¹⁵ 140 AC 1014. This case was cited with approval in the leading South African case of *Ntuli v Hazelmores t/a Musgrave Homes* 1988 ILJ 709 IC

²¹⁶ 1993 IRLR 179, ECJ

²¹⁷ Smit 1997 TSAR 549

As a result of this case, legislation was passed in the UK to allow explicitly for such a right by informing the transferor and transferee accordingly.²¹⁸

In South Africa, section 197 at most provides for the variation of the terms of the contract of employment by agreement. In *Foodgro*, however, the LAC concluded that in some cases a right to refuse the transfer of the contracts of employment existed. Upon examining the differences between section 197(1)(a) and (b), Froneman DJP found that "section 197(2)(b) allows for the contracting out of the transfer of the contract of employment itself, but section 197(2)(a) does not."²¹⁹ This argument is based on the contention that the subject matter of section 197(2)(b) can be contracted out of. Seeing that the subject matter in this case is "all the rights and obligations between the old employer and each employee at the time of the transfer" as well as the automatic transfer of the contract of employment itself, Froneman argues that in this case the parties can agree that the contracts of employment should not be transferred. At the most, however, this is not a one sided right to object as contemplated in the Regulations, but merely a right to prevent a transfer by *agreement* in certain limited instances. Also, the employee would not necessarily be a party to this agreement. Section 197(3) provides that the agreement intended in section 197(2) should be with the person or body mentioned in section 189(1). These are

- (a) any person whom the employer is required to consult in terms of a collective agreement;
- (b) if there is no collective agreement that requires consultation, a workplace forum, if the employees likely to be affected by the proposed dismissals are employed in a workplace in respect of which there is a workplace forum;
- (c) if there is no workplace forum in the workplace in which the employees likely to be affected by the proposed dismissals are employed, any registered trade union whose members are likely to be affected by the proposed dismissals;
- (d) if there is no such trade union, the employees likely to be affected by the proposed dismissals or their representatives nominated for that purpose.

²¹⁸ s33 of the Collective Redundancies and Transfer of Undertakings (Protection of Employment)(Amendment) Regulations 1995 (SI 1995/2587)

²¹⁹ par 25

The situation is further complicated by section 196(3) that states:

"An employee who unreasonably refuses to accept the employer's offer of alternative employment with that employer or any other employer is not entitled to severance pay in terms of subsection (1)".

Therefore, even if the employee should be given a right to object to her transfer, then such an objection may not be unreasonable or she may forfeit her severance pay.

Section 197 therefore does not expressly provide the employee with a right to object to the transfer of his contract of employment. The common law, in contrast, does provide for such a right, as it was considered essential that the employee should be able to choose whom he serves. It is submitted that a purposive interpretation of the section 197 would lead to the same conclusion. It is not conceivable how an employee protection provision can force an employee into a transfer against his will. How the employee can be furnished with such a right to object is however a matter for the court or the legislator to decide.²²⁰ It does not seem likely that such changes will take place in the near future, as the Amendment Bill also contains no mention of such a right.

3 MAINTENANCE OF TERMS AND CONDITIONS OF EMPLOYMENT

Continuity of employment would not be of much use if the terms and conditions of employment were not preserved by section 197 as well. As was mentioned above, it is possible to agree to different terms and the parties to this agreement would not necessarily include the employees themselves. Lacking such an agreement, however, the terms of the contracts of employment would remain unchanged by the transfer of a business.

3.1 OBJECT OF THE TRANSFERRAL

Section 197(2)(a) provides that all the rights and obligations between the employer and employee at the time of the transfer are transferred. Unlike in other jurisdictions,²²¹ these rights and obligations are not expressly limited to rights and obligations flowing from the contract of employment itself, but could supposedly also flow from another contract, a delict or a statute. It would be necessary to look at the nature of the

²²⁰ For example, should the employee be required to give notice of his objection? To which parties should he give notice? What would be considered sufficient notice?

²²¹ Directive 98/50/EC for example provides in Article 3.1 that the "rights and obligations arising from a contract of employment or from an employment relationship" shall be transferred.

particular rights and obligations in question in each case to determine if they should be transferred or not. Due to the very wide wording of the section, such an inquiry would require a purposive interpretation of section 197 and the LRA.

From the outset it should be noted that the LRA was passed to regulate the law regarding labour relations. Therefore it seems clear that section 197 would only apply to rights and obligations that form part of the employer/employee relationship. Any other rights and obligations that exist between the parties, which does not form part of this relationship (e.g. a private lease) would as a result not be transferred along with the contract of employment. Determining what forms part of the employer/employee relationship is unfortunately not always an easy task.

3.1.1 CONTRACT

It is clear that section 197 should apply to all the right and obligations flowing from the contract of employment, simply because this contract forms the basis of the relationship between the employer and employee. However, quite often the terms of the contract would include something so personal, so relevant to the particular employer or employee that it would not seem fair to transfer these terms. Examples of these are restraint of trade clauses and commission and stock option schemes.²²² The problem is that, although these terms are closely connected to the nature of the employing business (e.g. the profitability of the business, the type of business, the location of the workplace) something which might vary greatly from one employer to the next, there is nothing in section 197 that prohibits the transferral of these terms. To ensure an equitable outcome, it would therefore be necessary to vary these terms by agreement.²²³

Another, even more vexing problem, is the question whether the rights and obligations flowing from other contracts would also be effected by section 197. It is submitted that if a contract was concluded between an employer and employee and this contract added or took nothing away from the employment relationship between them, then such contract would not be effected by section 197. Accordingly, if only a few terms of such another contract affects the employment relationship, should only these terms be

²²² Van Zyl *The Transfer of Undertakings: How does section 197 of the LRA measure up?* LLM Minor Dissertation UCT February 2000 54

²²³ Van Zyl 2000 LLM 55

transferred? Does the LRA sanction the severance of a contract? There is no clear answer to this.

By far the most problematic issue is the question whether the rights and obligations imposed by a collective agreement are to be transferred as well. While all the foreign jurisdictions noted in this thesis do make express provision for this, section 197 does not. It is true to the very nature of collective agreements that they are not concluded between the employer and employee, but most commonly between a registered union and the employer and/or a registered employer's organisation. The employee is never a party to this agreement and is only bound through the workings of section 23(1)(b) of the LRA. This section provides that the members of a party to the agreement are bound by the agreement as far as it is applicable to them. The members of a trade union that is party to a collective agreement are therefore only bound by such obligations and entitled to such rights as are applicable to them. These rights and obligations would usually be between the employer and employee, so in effect only a part of a collective agreement would be affected by section 197. However, due to the workings of section 23(3) such rights and obligations would form part of the contract of employment anyway and would be transferred as part of that contract. In general, section 197, therefore, does not have any real effect on collective agreements. As a result, the new employer would not be bound by the terms of the collective agreement, other than, of course, those terms that are applicable between the employer and employee. The union would be powerless to enforce any rights and obligations flowing from the collective agreement since the new employer is not a party to the agreement. While some may argue that is conceivable that the legislator intended to make the transfer of a business more attractive by formulating it as a way to escape duties imposed by collective agreements, the serious effect that this could have on the rights of the unions and shop stewards seem rather to indicate that this was an overlooked aspect. The Amendment Bill proposes to correct this. It provides in clause 47(a) re proposed section 197(6) that the new employer is bound by

- (a) any organisational right granted in terms of Chapter III binding on the old employer immediately before the transfer in respect of any workplace that is transferred; and
- (b) any collective agreement binding on the old employer in terms of section 23 immediately before the transfer in terms of which a registered trade union is

recognised by the old employer as representing employees in a workplace that is transferred.

Although the protection of organisational rights and rights born out of collective agreements is essential, there are some practical problems which come to the fore when considering such a transfer - as is clearly illustrated by the Amendment Bill. In an attempt to simplify the matter, the Amendment Bill provides that organisational rights are transferred along with the workplace rather than with the employees individually. Therefore clause 47(a) re proposed section 197(6) would not apply when a mere function or a part of the services is transferred, but only when the workplace itself is transferred. Although this simplifies the position considerably one aspect is still problematic: the status of the union after the transfer. To acquire certain organisational rights, the union needs to have a certain status in the workplace: it must be registered²²⁴ and in some cases it needs majority support²²⁵ in this workplace. It is conceivable that after the transfer the union might lose majority support in the workplace. A transfer usually forms part of a larger process of restructuring, and this might well lead to the restructuring of the workplace itself, resulting in a much larger workplace or even a completely different one, where the union might not majority support anymore. Would these organisational rights then still be binding? On a literal interpretation of the Amendment Bill it would seem that such rights would be binding indefinitely. But surely this would result in an intolerable position. It is important that the rights of the transferred individuals with regard to the workplace be protected, but at what cost? By providing organisational rights to a union which does not qualify in terms of the LRA for such rights, would undermine not only the real majority union in that particular workplace, but also the LRA itself. It is submitted that the transfer of such organisational rights should only be operational for a limited time. If after such a reasonable time the pre-transfer majority union no longer represents the majority in the workplace, then the organisational rights should be forfeited accordingly.

With regard to collective agreements it is submitted that section 197 should not be amended to provide for the automatic transfer of collective agreements. Collective agreements come into being after a protracted process of negotiations, which ensure that the agreement is tailored to the specific needs of the parties and is representative of the

²²⁴ e.g. s11, s15

²²⁵ e.g. s14, s16

balance of power between them. A change of employers would represent a drastic change in these circumstances, enough so that the old collective agreement would not effectively be able to provide for it. If section 197 – or its successor – were to provide for the continued protection of the all the rights and obligations imposed by the collective agreement it would be useful to follow the Canadian example and to impose a duty on the new employer to negotiate with the union to conclude new collective agreements that would replace those voided by the transfer. Until such agreements come into being, the old collective agreements might also still be kept in force by the section for a reasonable time, as a further incentive to replace them. Such a process would ensure that the stability of the transferred entity would be maintained, while also protecting the rights of the relevant parties.

3.1.2 DELICT

Are the rights and obligations that arise from a delict affected by section 197?

Although the wording of section 197 seems to indicate that all the rights and obligations between the employer and employee should be transferred, it has already been discussed how a purposive interpretation of the section and the LRA as a whole would lead us to conclude that only rights and obligations that are connected to the employment relationship itself would be affected by the transfer. Therefore, if an employee damaged an employer's car during work hours, then such liability towards the employer would be transferred to the new employer. If, however, the employee after work negligently crashed his own vehicle into that of the employer, then such liability would not be transferred along with the business, simply because the employee is liable towards the employer in a private capacity and not as his employee.

3.1.3 STATUTE

Statutes frequently create rights and obligations that bind the employer and employee. For example, section 185 of the LRA confers on the employee the right not to be unfairly dismissed, while section 196 provides that all employees are entitled to redundancy payment in the case of a fair dismissal for operational requirements. A more important example is section 193(1) of the LRA that gives the courts the authority to order the reinstatement of an employee who was unfairly dismissed. This right of the employee to claim reinstatement is instrumental to the workings of section 197. If an employee is unfairly dismissed before the transfer of a business, then the dismissed

employee can claim reinstatement from the new employer as a remedy. This is possible, because all rights and obligations between the employer and employee are transferred, even the right to claim reinstatement.

Rights and obligations deriving from other statutes can sometimes be problematic. One such example is the pension rights that derive from the Pension Funds Act.²²⁶ In the UK the Regulations prohibit the transfer of pension rights expressly, but in South Africa section 197 does not contain such a limitation. In a recent decision²²⁷ the Tribunal of the Pension Funds Adjudicator found that most of such pension rights were relevant to the relationship between the employee and the pension fund itself and were not rights between the employee and employer. As a result it was found that section 197 did not apply. Fortunately, in this case, a wide interpretation of section 14 of the Pension Funds Act was held to ensure the continuity of such pension rights on the transfer of the business.²²⁸

In all these cases, the most important factor that determines the applicability of section 197, is the question whether the contract, statute or delict creates rights and obligations *between* the employer and employee, in their capacity as employer and employee. If the rights and obligations do not form part of the employment relationship, then they would, as a rule not be affected by section 197.

The Amendment Bill attempts to clarify this position by stating that:

"anything done before the transfer by or in relation to the old employer will be considered to have been done by or in relation to the new employer".²²⁹

It is respectfully submitted that such a proposition might be overly wide as the exact scope of "anything done" might be interpreted to include much more than the rights and obligations that flow from the employment contract.

Furthermore the Amendment Bill now also provides for the joint and several liability of the old and the new employer in respect of a claim concerning any term or condition of

²²⁶ 24 of 1956

²²⁷ *Younghusband & others v Decca Contractors (SA) Pension Fund and its Trustees* 1999 ILJ 1640 (PFA)

²²⁸ s14 is a generic provision governing all transactions involving the amalgamation and the transfer of pension fund businesses.

²²⁹ clause 47(a) re proposed section 197(3)(c)

employment that arose prior to the transfer.²³⁰ This regulation, completely new to South African labour law, was inspired by article 3.1 of the Directive. It ensures that the employee would not be prevented from enforcing any rights that existed before the transfer. In the claim for damages, the employee would therefore have a choice of which of the employees she would prefer to institute a claim against.

3.2 HARMONISATION OF THE WORKPLACE

Quite often the transfer of the employers due to the transfer of a business as a going concern would result in the new employer being faced with having groups of employers doing similar work but on different terms. It is conceivable that such a situation could lead to dissatisfaction among competing unions and therefore a process of harmonisation of the workplace would be essential to ensure that all employees be employed on similar terms. Such a process would necessarily entail that changes need to be made to the employment contracts themselves. Such results can be achieved in three ways: the dismissal and re-employment of the employees on different terms; one-sided changes to the contracts; or a change in the terms of the contracts by agreement.

Dismissal is no easy solution in the South African labour law. The employer would have to prove that the dismissal was substantively and procedurally fair.²³¹ The transferee would claim that the employees be dismissed on operational requirements, but for such a claim to be successful, the employer would have to embark on an extensive consultation process with the involved parties as set out by section 189. This process exists to ensure that employees could not be dismissed on these grounds without a sound reason. If such a sound reason does present itself, this process goes further to ensure that dismissal be the last resort and that all possible ways of escaping such a consequence have been explored.²³²

One-sided changes to the terms and conditions of employment might be an equally problematic solution. The resulting dispute would have to be referred to the CCMA, and until that time such changes may not be implemented,²³³ and if they have already been implemented, the original terms should be revived.²³⁴ Failure to comply with

²³⁰ clause 47(a) re proposed section 197(1)(9)

²³¹ s188(1)(a) and (b)

²³² s189(2)(a)(i)

²³³ s64(4)(a)

²³⁴ s64(4)(b)

these requirements within 48 hours of the delivery of the demands on him would result in an immediate protected strike.²³⁵

Section 197 provides that the terms and conditions of the contract of employment may be varied by agreement. Subsection 3 provides that the parties to such an agreement should be the same as those prescribed by section 189.²³⁶ Section 197 does not currently stipulate whether the other party should be the old or the new employer. It is submitted that such an agreement would have to take place between the *new employer/transferee* and the party as prescribed in section 189. While the transferor might also take part in the negotiations prior to this agreement, it does not seem likely that the transferor need to be part of such an agreement to vary the terms and conditions of employment, because it would not affect the relationship between him and the employees. The moment when such an agreement is concluded may also be problematic, simply because the transferee might not be the employer yet at that specific time. It is submitted that such an agreement is therefore subject to a suspensive condition (the transferee becoming the employer).

The Amendment Bill attempts to clarify the position by providing that the agreement must be concluded between

- (a) either the old employer, or the new employer, or the old and new employers acting jointly, on the one hand; and
- (b) the appropriate person or body referred to in section 189(1), on the other.²³⁷

(a) is problematic. It is not clear how the old employer can be party to such an agreement if he is not the party who has to uphold these new terms. Surely the old employer can not speak for the new employer, he should at most only be able act jointly with the new employer. Providing otherwise might open the door to abuse.

(b) is merely a restatement of section 197(3). It is important to note that in this regard it would not necessarily be the employee herself consenting to the changes in the terms of the contract but rather the relevant party as prescribed by section 189.

In practice such an agreement would only be concluded after a process of negotiations. As a result of such negotiations it would also not be unusual for the transferee to have to

²³⁵ s64(3)

²³⁶ See 2.4 above for the list of parties.

²³⁷ clause 47(a) re proposed section 197(7)

“buy out” the offending terms. To harmonise working conditions, it is also possible that the transferee could get the parties to agree that the employees employed on more favourable terms not be given any further pay increases until the rest of the workforce be employed on similar terms.

The procedure for securing agreement set out in section 197 is clearly relevant to changes in the contract of employment before the time of the transfer which should come into being on the transfer itself. It is less clear if the same process could be followed after the transfer and if so, for how long after the transfer? It is submitted that once the contracts of employment have been transferred to the new employer, then the process of agreement set out in section 197 no longer applies to these contracts and then any changes in the contracts need to be negotiated in the usual way.

The Amendment Bill also proposes to make the process of harmonisation of the workplace much easier by providing that employment on terms on the whole not less favourable to the employee than those on which they were employed by the old employer would also constitute as the transfer of a contract of employment for the purposes of section 197.²³⁸ This would allow for much greater flexibility in the transfer process, although it could lead to a concern that this might give the new employer the right to alter the terms of employment one-sidedly. Despite this, it allows for the realities of the employment situation, as it is not always possible to employ the employees on exactly the same terms after the transfer, because the circumstances with the new employer and business might differ drastically from that with the old. This provision would ensure that any minor changes in the contract of employment that would have to result from such a change in circumstance could take place, without the employee being affected negatively.

When determining if such terms and conditions of employment are the same or a favourable to an employee as those on which the employee was employed by the old employer, the Amendment Bill further proposes that regard must be had to the employer's contribution to any retirement, medical or similar fund, but not any benefits that the employee is entitled to from that fund.²³⁹

²³⁸ clause 47(a) re proposed section 197(4)(b)

²³⁹ clause 47(a) re proposed section 197(5)

The importance of this provision cannot be overstated. The single biggest criticism against the current mode of transfer of contracts of employment as promoted by section 197 is that the process is not flexible enough and that as a result, employers would rather prefer to terminate the contracts of employment. The ironic result being that an employment protection provision in the end results in lay-offs. A more flexible process as envisioned by the Amendment Bill would go a long way towards resolving this problem.

4 DUTY TO INFORM AND CONSULT

Before the passing of the LRA and section 197, the Industrial Court held in *Ntuli v Hazelmere* that the purchaser of the business had a duty to consult with the employees and their unions prior to the transfer. The object of such consultations would usually be "to discuss the measures which are to be taken to protect the interest of the employees and the preservation of the employment relationship notwithstanding the change of ownership of the business".²⁴⁰

Section 197 was undoubtedly passed to ensure such preservation of the employment relationship. Does this mean that the duty to consult is no longer essential for the protection of the employees? Currently the position is not clear. The main practical problem is that commercial negotiations often need to remain confidential. It is almost impossible for either employer to inform anyone until the deal has reached a point at which consultation is unlikely to change the result.²⁴¹ Section 197 has not expressly altered the common law in this respect and therefore it is uncertain whether such a duty to consult still exists. The LRA provides little insight in this regard. It only requires a process of consultation when a dismissal takes place in accordance with section 189. While dismissals on such a ground would commonly take place before a transfer, this provision does not provide for a general duty to consult in case of a transfer, especially when no retrenchments are set to take place.

The duty to inform is regulated in slightly more detail in the LRA, but once again, not by section 197 itself. Section 16 provides for the disclosure of relevant information to a registered majority union for the union participation in bargaining or for the shop stewards to perform their duties. More importantly section 84(1) allows for the duty to

²⁴⁰ *Kebezi v. Cementile Products (Ciskei)* 1987 1LJ 442 (IC)

²⁴¹ *Holland & Burnett Employment Law* (1998) 276

consult with the workplace forum in the case of for example the restructuring of the workplace. Lastly, section 89 makes general provision for the disclosure of all relevant information necessary for the workplace forum to perform its duties.

In the UK, the Regulations²⁴² provide for a duty to inform and consult with appropriate representatives. The nature of the information²⁴³, the manner of providing the information²⁴⁴, the timing of the information²⁴⁵, the nature of the consultation²⁴⁶ as well as the timing of the consultation²⁴⁷ are all extensively regulated. This stands in contrast to the lack of regulation in South African labour law.

In *Kgethe & Others v LMK Manufacturing (Pty) Ltd & Another*²⁴⁸ the Labour Appeal Court ordered the disclosure of information relating to a transfer bearing on the existence or otherwise of the rights protected in section 197(1). The court found that such an approach not only promoted fairness, but was also practical in that it facilitated the determination of what rights existed and may have had the effect of obviating unnecessary litigation. The facts of the case were the following. After experiencing serious financial problems, the first respondent concluded an agreement with the second respondent, according to which the second respondent would buy the bulk of the assets of the first respondent. The respondent maintained that this was not a transfer of a business as a going concern and accordingly section 197 did not apply. The result was that employment with the second respondent was only secured for the permanent employees and even these contracts were not to be considered a transfer of the employment relationship. The appellants launched an application for an urgent interim interdict, demanding, among other things, the disclosure of the agreement of sale, a copy of the notice to alienate, the details of the assets before the sale as well as all the assets allegedly sold, and the liabilities and creditors of the second respondent at the time of the sale. On appeal, the court found that without the alleged agreement and other information sought by the appellants being placed before the court, it would not be permissible for the court to determine if and when an agreement was in fact concluded

²⁴² Regulation 10 as amended by s 47 and ss61 – 63 of the Collective Redundancies and Transfer of Undertakings (Protection of Employment)(Amendment) Regulations 1995 (SI 1995/2587)

²⁴³ reg. 10(2)

²⁴⁴ reg. 10(4)

²⁴⁵ reg. 10(2) and (8)

²⁴⁶ reg. 10(6)(a) and (b)

²⁴⁷ reg. 10(2)

²⁴⁸ 1998 ILJ 524 (LAC)

and what the effect of this agreement was. In order to find how the rights of the employees had been affected, the court ordered that all relevant information must therefore be disclosed. Only after such information had been disclosed would the employees be able to take further steps regarding their other prayers of relief.

The decision in *LMK* is limited to the disclosure of information in order to determine if section 197 would be applicable. Therefore, if there is already consensus about the application of section 197, *LMK* would not be applicable and it would be unclear if information should be disclosed in such an instance.

The Amendment Bill does not address this issue either.

5 DISMISSALS

Section 197 forms part of chapter 8 of the LRA regulating unfair dismissals, yet nowhere in the section (or the rest of the chapter) is a dismissal purely on the grounds of the transfer established to be unfair or even automatically unfair.

In South Africa the usual grounds for fair dismissal are regulated by section 188 and they incorporate dismissal for misconduct, incapacity and operational requirements. Dismissal for operational requirements is considered a no fault ground for dismissal and is usually utilised in the case of business restructuring.²⁴⁹ A dismissal prior to a transfer would most likely currently take place by this means.

The basis for a fair dismissal due to the imminent transfer of the business is however sometimes unclear. It is conceivable that the transferor would attempt to make his business as attractive as possible to secure a good price on the transfer and such a process would necessarily involve cutting back on employees or even shutting down certain parts of the business. Such dismissal would however only be considered fair if the employer can prove that it was required by the "economic, technical, structural or similar needs of the employer"²⁵⁰ and not merely for enhancing the profits of the business. Dismissal for operational requirements therefore need at least to be obliged by external market factors, and not merely by an attempt to improve the employer's profits,²⁵¹ but determining which is the case is not always an easy task. In the end, this

²⁴⁹ Thompson "Bargaining, Business Restructuring and the Operational Requirements Dismissal" 1999 20 *ILJ* 762

²⁵⁰ As defined in s213(1)

²⁵¹ Thompson 1999 20 *ILJ* 766

is a matter to be decided by the courts. The underlying issue in the case of a dismissal for operational requirements, especially prior to a transfer, is essentially economic.²⁵² This poses a problem for the courts, because the task of the Labour Court in this instance is to determine the fairness of the dismissal and not to meddle in "a critical area of economic decision making."²⁵³ Thompson proposes a solution to this problem, in that the courts should take a more limited approach to operational requirements and that their main task should therefore only be to determine whether there was "*a fair reason* for dismissal *based on* the employer's operational requirements."²⁵⁴ If this should be the case, then dismissals prior to a transfer might more easily be justified, a scenario which is not in line with the employee protection envisaged by section 197.

An unfair dismissal prior to a transfer of a business, on the other side does not effect the workings of section 197. According to section 193(1)(a) the Labour Court can order the reinstatement of the employee if it finds that the dismissal has been unfair. At the same time section 197(2)(a) ensures that all the rights and obligations between the employee and the old employer are transferred to the new employer. The right to re-employment would accordingly be transferred and therefore the employee would be able to claim reinstatement from the transferee/new employer. The courts have also found that the facts that the transferral took place after the dismissal but before the finding of the unfairness of the dismissal would have exactly the same results.²⁵⁵ In the case of a transfer as contemplated in subsection 1(b) problems might however arise, as subsection 2(b) does not provide for the transferral of all the rights and obligations between the old employer and employee to the new employer. As a result such employees would not be able to claim reinstatement from the new employer. This serves as a clear illustration of the different factors involved in these two scenarios. In the case of a transfer due to the insolvency, the survival of the business seems to be the first priority. The possibility of having to restate dismissed employees would have a negative effect on the transferee (new employer) when deciding whether he should take over an already insolvent business in the first place. The legislator therefore decided

²⁵² Thompson 1999 20 ILJ 769

²⁵³ Thompson 1999 20 ILJ 769

²⁵⁴ Thompson 1999 20 ILJ 770

²⁵⁵ NUMSA & Another v Success Panelbeaters & Service Centre CC t/a Score Panelbeaters & Service Centre 1999 ILJ 1851 (LC)

that the old employer should bear the brunt of the unfair dismissals alone by paying damages.

To correct some of the above-mentioned uncertainties, the Amendment Bill proposes a superficial revamp of section 197 with regard to the dismissal of employees prior to a transfer. According to clause 47(a) re proposed section 197(8) an employer may no longer dismiss an employee on account of a transfer covered by section 197. The proposed new section 187(1)(g) states that such a dismissal will be automatically unfair.²⁵⁶ This far-reaching new element to section 197 is however limited by two dooming limitations. Paragraph (a) does not preclude -

- (i) the old employer from dismissing an employee in accordance with the provisions of this Chapter for a reason based on the old employer or the new employer's operational requirements; or
- (ii) the new employer from dismissing an employee in accordance with the provisions of this Chapter for a reason based on its operational requirements.

A careful reading of these exceptions and what was discussed before, indicates that indeed very little has changed. Currently, dismissals take place due to a transfer by way of a dismissal for operational requirements. Section 197 did not prohibit such dismissals in anyway. The Amendment Bill states that dismissals due to a transfer are automatically unfair and prohibited, unless these are dismissals based on operational requirements of either the new or the old employer. What is more, the old employer would in such a case even be able to dismiss the employee based on the operational requirements of the new employer - something that was unheard of until now. This new position holds very little advantage for the employee, except for cases where the dismissal is not based on operational requirements.

²⁵⁶ The inspiration for such changes was probably the Regulations and Directive, as both regulate that a transfer driven dismissal is automatically unfair.

6 CONCLUSION

The two most important effects of section 197 are ensured continuity of employment and the maintenance of the terms and conditions of this employment.

In the leading cases on the subject²⁵⁷ it was accepted that section 197 provides for this continuity of employment by procuring the automatic transfer of the contracts of employment. Although this interpretation is in line with the spirit of the LRA and akin to similar provisions in foreign jurisdictions, it seems that such an interpretation of the wording of especially section 197(2)(a) is not entirely sound. Convincing arguments have been made to the contrary, and it seems that only an amendment to the section would ensure that the status quo be maintained. The courts have also held that this continuity of employment ensured by section 197 is not a right but a fact and therefore not subject to alteration by agreement, except in the case of a transfer as provided by subsection 2(b).

Nowhere in section 197 is it stated in detail which employees should be transferred. While it seems obvious that all the employees would be transferred if the whole of the business were transferred, the transferral of a part of a business might cause some problems. It is submitted that because the section 197 is an employee protection provision, its purpose should be to prevent employees from losing their jobs due to redundancy by reason of a transfer. For this reason, if employees are employed in the part of the business that is transferred and the transferral would result in their redundancy, they should be transferred along with the business.

Section 197 does not give the employees a right to object to the transfer of their contracts of employment. This position is not in line with concept of employee protection and the legislator might do well to add such a right to section 197 in the future. It is possible however for the parties to vary the terms of the contract of employment by agreement. In the case of a transfer as envisaged by subsection 1(a) it is also possible to opt out of the transfer of the contracts of employment by such an agreement.

Secondly, section 197 provides for the maintenance of *all* right and obligations between the employer and employee. It is submitted that a purposive interpretation of the

²⁵⁷ *Schutte supra* and *Foodgro supra*

section would limit these rights and obligations to only those rights and duties that form part of the employment relationship, no matter whether they originate from contract, statute or delict. Another problematic aspect in this regard is the failure of section 197 to provide for the maintenance of the terms of a collective agreement. It is submitted that the legislator could do well to provide for a duty on the new employer to initiate the process to ensure the replacement of the defunct collective agreements. All these rights and obligations that are transferred are also subject to change by agreement of the parties as stipulated in section 189.

There are two further problematic aspects surrounding the effects of section 197. Firstly, the section does not provide for the duty to inform and consult. Consultation might therefore only take place prior to the retrenchment of the employees prior to the transfer. It seems that the common law duty to inform and consult prior to the transfer has also lost favour with the Labour Court. A limited right to inform remains, but only for the purpose of determining whether section 197 should apply or not. Secondly, section 197 does not provide for the scenario where employees are dismissed prior to a transfer – it seems quite possible that employees might be dismissed in such a case on operational requirements and this could undermine the protective purposes of the section. Also, the clumsy wording of subsection 2(b) resulted in the intolerable position that employees that are dismissed prior to a transfer as envisaged in subsection 1(a) can not claim reinstatement with the new employer.

CHAPTER 6

INSOLVENCY

1 INTRODUCTION

Subsections 1(b) and 2(b) of section 197 provide for the case where a business is transferred due to insolvency and sequestration, or where the business is transferred to prevent such sequestration. In practice such an occurrence can be very protracted and it is immediately clear that section 197 does not provide nearly enough detail to regulate such a transfer. Of all the shortcomings of section 197, this is the most glaring – the one area where the haste with which the section was put together shows the clearest. Not only is the wording of subsections 1(b) and 2(b) confusing and unclear, furthermore, a normal interpretation of these subsections leads to a position that is in conflict with the current law of insolvency. It is obvious that these subsections were not well thought through and it is probably only a matter of time before they will be amended as well. Until such amendments are passed, it would still be necessary to study the current workings of these subsections, if only to understand where the legislator went wrong and how it can be amended properly. In the light of this, the drastic changes proposed by the Amendment Bill will then be analysed.

2 COMMON LAW

In common law the insolvency of the employer results in breach of contract. The employee may well be further employed in the business on the choice of the liquidator or trustee -depending on the situation.²⁵⁸ If the liquidator or trustee elects not to provide employment for the employees, then they will have a concurrent claim for damages against the insolvent estate.²⁵⁹

3 PROBLEMS SURROUNDING THE WORDING

In an attempt to provide continuity of employment in the case of such insolvency, section 197(1)(b) and (2)(b) were passed.

²⁵⁸ Jordaan *"Transfer, Closure and Insolvency of Undertakings"* 1991 12 5 ILJ 935

²⁵⁹ *Clarke v Denny* 1884 EDC 300

Although the exact extent of the workings of this section with regards to insolvency is unclear, it is presumed that subsection 1(b) provides for the following two situations:

1. Where a business or part of a business is transferred as a going concern because the old employer has become insolvent and was liquidated or sequestrated.²⁶⁰
2. Where a business or part of a business is transferred by a scheme of arrangement that was concluded in order to save the insolvent employer from such liquidation of sequestration.²⁶¹

It is clear from the above that subsection 1(b) does not cover the cases where liquidation occurs where the natural person did not commit an act of insolvency or where sequestration occurs because a corporate body is wound up either voluntarily or by order of the court.²⁶² Section 197(1)(b) is only limited to cases where the old employer is actually insolvent.

Further, with regard to the wording of section 197(1)(b), there is a reference to the sequestration of the old employer. As only corporate bodies can be sequestrated, it is clear that the corporate body itself is considered to be the employer. When a corporate body is transferred, the identity of the corporate body itself does not change - there are merely new shareholders. It is submitted that a corporate body can not be considered to be an employer for the purposes of section 197, as a transfer envisaged by the section would therefore not be possible, as there would be no "new employer".

Another point that concerns the wording of this subsection is the fact the insolvent business has to be transferred as a going concern. The exact meaning of "going concern" was discussed in length in the previous chapter. From that discussion it became clear that the "going concern" meant that the business should at least be open and in operation.²⁶³ Insolvent businesses - as required by subsection 1(b) - are frequently neither open nor in operation. It is unclear whether this fact will exclude the workings of section 197, or even if it obliges the curator or trustee to carry on the workings of the business.

²⁶⁰ s197(1)(b)(i)

²⁶¹ s197(1)(b)(ii)

²⁶² Wallis "Section 197 is the Medium. What is the Message?" 2000 21 *ILJ* 6

²⁶³ See *NEHAWU v UCT supra*

Section 197(2)(b) in turn provides that in the case of a transfer of a business as envisaged in subsection 1(b), the contracts of employment of all the employees that existed before the liquidation/sequestration of the old employer are automatically transferred to the new employer. Rights and obligations existing between the old employer and employees at the time of the transfer are excluded from such a transfer.

First off all, this subsection states without a doubt that such a transfer should be an automatic transfer. A finding by the LAC that section 197 does not provide for the automatic transfer of a contract of employment would therefore only be limited to the workings of subsection 2(a).

Furthermore, the negative effects of excluding the rights and obligations existing between the old employer and employees at the time of the transfer have also been discussed.²⁶⁴ Still, the legislator may well have had a very good reason to impose such a restriction, as a business free from obligations against employers would be much more attractive to prospective buyers – something which would be essential for the rescue of the insolvent businesses. This is perhaps a case where the interest of the business should outweigh the interest of the employees, especially since the failure of the business would lead to the permanent job loss of the employees.

4 CONFLICT WITH INSOLVENCY LAW

The most controversial aspect of subsection 2(b) is the question whether it provides for the termination of the contracts of employment on liquidation/sequestration and their later revival, or whether it should be interpreted that the contracts of employment survive the liquidation/sequestration process. While the former position seems vague and uncertain, the latter interpretation is in direct conflict with current insolvency law.

Section 38 of the Insolvency Act²⁶⁵ provides that the contracts of employment are automatically terminated on the liquidation of the employer.²⁶⁶ The employee would accordingly still be entitled to a concurrent claim for damages that result from the termination of the contract. Section 100 of the Insolvency Act further provides that the

²⁶⁴ See chapter 5. In short it would mean that employees would not be able to claim reinstatement in the transferred business if they have been unfair dismissal prior to a transfer.

²⁶⁵ 24 of 1936

²⁶⁶ s38 read together with s339 of the Companies Act 61 of 1973 (and s66(1) of the Close Corporations Act 69 of 1984, read with s339 of the Companies Act.) provide that the results would be same in the case of sequestration of a company.

employees are entitled to a preferent claim to any salary in arrears for up to two months and an amount up to R5000.

After such insolvency, the business is continued by the curator or trustee on the authority of the creditors, or lacking this, the Master of the Court. If the business is kept running at this stage, then the employees are directly employed by the curator/trustee. A new contractual relationship is therefore created between the employees and the curator/trustee.

According to the Insolvency Act, the contracts of employment are clearly terminated. Any further employment would continue under the new contracts of employment concluded with the curator. Section 197(2)(b) of the LRA however provides that the contracts of employment are automatically transferred in the case of the transfer of the business in the case of insolvency. The contracts are therefore not considered to be terminated. Whether the contracts survive unconditionally or whether they merely revive at a later stadium retrospectively is irrelevant for the moment, as subsection 4 provides that continuity of employment would not be interrupted. The contracts of employment are as a result not terminated.

This situation is further complicated by section 210 of the LRA that provides that:

If any conflict, relating to the matters dealt with in this Act, arises between this Act and the provisions of any other law save the Constitution or any Act expressly amending this Act, the provisions of this Act will prevail.

Accordingly, section 197 overrides section 38 and the contracts of employment are not terminated where the insolvent business is transferred as a going concern.

This results in the position of the employer, employee and curator or trustee from the moment of the insolvency to the time of the transfer being brought into question. The source of this problem is the inability of the parties to say with certainty when the business becomes insolvent and the contracts are terminated according to section 38, whether the business will ever be transferred. Such a decision could only be reached at the second meeting of creditors, some time later. If a transfer takes place at such a later time, then section 197 applies and the contracts of employment come to life again. But until such a decision is reached, are the contracts of employment terminated or not?

This single question is the root of all the confusion surrounding this subsection: because the contracts of employment regulate and effect all the parties in the workplace,

uncertainty about the status of the contracts of employment would necessarily effect every party to this contract.

Several questions arise. Where the contracts never terminated in the first place? Or does section 197 work retrospectively, bringing the terminated contracts back to life? And how does this affect the employers? Do they lose any claims that they had according to section 38? What happens if they have already successfully instituted such claims? And what happens if they have secured other employment? Are they in breach of contract? These and many other questions abound.²⁶⁷

Quite frankly, the more subsections 1(b) and 2(b) are analysed, the more problems can be isolated, to such a disturbing degree that it seems quite impossible to apply these subsections without ignoring the exact wording of the section - an approach advocated in extreme circumstances. In *Venter v Rex*²⁶⁸ for example the court stated that:

"when to give the plain words of the statute their ordinary meaning would lead to absurdity so glaring that it could never have been contemplated by the legislature, or where it would lead to a result contrary to the intention of the legislature, as shown by the context or by such other considerations as the Court is justified to take into account, the Court may depart from the ordinary effect of the words to the extent necessary to remove the absurdity and to give effect to the true intention of the legislature."²⁶⁹

Fortunately the Amendment Bill proposes to correct this position, and the exact method and merit of such proposals will now be discussed.

5 PROPOSED AMENDMENTS

In the Statement by the Minister of Labour on the occasion of the release of labour law amendments issued by the Department of Labour on 26 July 2000 it is proclaimed that:

"In the context of high unemployment, large numbers of retrenchments and high levels of insolvency, I believe that it is important to provide certainty to employers and employees as to their rights and obligations in such circumstances."

²⁶⁷ Schlemmer and Oelofse "Konflik tussen die Wet op Arbeidsverhoudinge en die Insolvensiewet" 1996 *TSAR* 559-563

²⁶⁸ 1907 TS 910

²⁶⁹ 914-915

The proposed solutions to the problem involving insolvency are twofold: firstly a whole new section 197A which regulates the transfer of contracts of employment on the transfer of a business and secondly drastic changes proposed to the Insolvency Act.

5.1 INSOLVENCY AMENDMENT BILL

The Insolvency Amendment Bill proposes to amend the Insolvency Act so as to regulate the sequestration of employers further; and to provide for matters incidental thereto.

Two problems with regard to the current Insolvency Act are identified in the Explanatory Memorandum accompanying the Amendment Bill:

1. The termination of the contracts of employment on the sequestration of the insolvent employer as a result of section 38.
2. Despite these extreme consequences, neither employees nor the trade unions having any right to be notified of legal proceedings brought to sequester the employer.

The Amendment Bill addresses these shortcomings by providing for a procedural right to be notified of the institution of legal proceedings to sequester an employer and also by amending the consequences of section 38 on the contracts of employment.

5.1.1 RIGHT OF NOTIFICATION

The Amendment Bill tries to ensure that workers are timeously informed about possible liquidations, by providing that a copy of the notice in the Gazette be presented to any registered trade union that represents any of the debtors employees,²⁷⁰ as well as the notification of its own employees.²⁷¹ Similar processes are also proposed for the serving of a section 9 petition²⁷² and a *rule nisi*.²⁷³

5.1.2 NEW SECTION 38

According to the Amendment Bill, the sequestration of the employer will no longer result in the termination of the contracts of employment between the insolvent employer and the employees, but will only result in the suspension of the contracts from the date

²⁷⁰ clause 4(2)(b)(i)
²⁷¹ clause 4(2)(b)(ii)
²⁷² clause 9(4A)
²⁷³ clause 11(2A)

of the granting of the sequestration order.²⁷⁴ During such suspension, no work would be required from the employee and she would not be entitled to any remuneration.²⁷⁵ During such a time, the employee would also not be entitled to any benefits in terms of the Basic Conditions of Employment Act,^{276 277} and would be deemed to be unemployed for the purposes of the Unemployment Insurance Act²⁷⁸ and therefore be entitled to unemployment benefits.²⁷⁹ The employee and trustee²⁸⁰ can come to an agreement to continue in service (by concluding a new contract),²⁸¹ or to terminate the suspended contract.²⁸² The employee can also choose to terminate the contract on her own.²⁸³ Any such termination of the contracts of employment under the new section 38 would still be deemed to be the termination of the contract by operation of law and therefore the protective measure of the LRA would not apply. Fortunately, a new provision ensures that the employee would be able to claim severance benefits against the estate of the insolvent employer.²⁸⁴ It is proposed that for these purposes the employees be treated as employees who have been dismissed because of the employers operational requirements.

The trustee also has the right to terminate the contracts of employment,²⁸⁵ but this right is limited by an obligation to consult with the relevant parties similar to the parties stipulated in section 189(1) of the LRA. The purpose of this consultation process would be to reach consensus on whether the business or a part of the business should be sold or transferred as contemplated by section 197A of the LRA or according to a scheme or compromise as provided by section 311 of the Companies Act²⁸⁶ or any other manner.²⁸⁷ Such consultations can also be initiated by party mentioned in subsection 6

²⁷⁴ clause 38(1)

²⁷⁵ clause 38(2)(a)

²⁷⁶ 76 of 1997

²⁷⁷ clause 38(2)(b)

²⁷⁸ 30 of 1966

²⁷⁹ clause 38(3)

²⁸⁰ To simply matters, all references to trustee and sequestration, will be substitutable for curator and liquidation, unless otherwise stipulated.

²⁸¹ clause 38(4)(a)

²⁸² clause 38(4)(b)

²⁸³ clause 38(4)(c)

²⁸⁴ clause 38(11)

²⁸⁵ clause 38(5)

²⁸⁶ 69 of 1973

²⁸⁷ An important matter which must be noted - and will be returned to later on - is the fact that the proposed section 38 clearly differentiates between a transfer as envisaged by section 197A and a scheme or compromise referred to in section 311. It is submitted that this is the correct approach as a scheme or compromise according to section 311 can never qualify as a transfer according to

by submitting a written proposal of the measures sought to save or rescue the business to the trustee.²⁸⁸ If this proposal reaches the trustee within 21 days after his appointment, then the trustee must consult with these parties²⁸⁹, if he has not done so already.²⁹⁰

The only problematic aspect surrounding the proposed section 38 is the fact that the contracts are only suspended for 21 days after the appointment of the trustee. After such time, the contracts are terminated by operation of law.²⁹¹ The suspension of the contracts can only continue if an agreement is reached between the trustee and employee. It should be noted that the parties to such an agreement are not the same as the parties who are stipulated in section 38(6) who should reach consensus about the transfer of the business. There are therefore no obligations on any of these parties to reach such an agreement, and furthermore, if one party refuses to negotiate over the matter, then it would inevitably lead to termination of the contracts. In practice, such a decision would usually only be made after the consultation process provided for in the section has taken place and a decision has been reached on whether the business should be transferred or not. It is not clear why the legislator would go at such lengths to provide for a process of consultation where the trustee chooses to terminate the contracts before 21 days, if they automatically terminate after 21 days anyway.

5.2 SECTION 197A

The proposed section 197A provides for the transfer of a business due to insolvency and it functions in tandem with the changes brought about by the new section 38 of the Insolvency Amendment Bill. So for example, section 197A expressly provides for continuity of the contracts of employment, subject to the suspension of contracts referred to in section 38.

Certain questions arise over this relationship between these two sections. It is not clear whether if the contracts of employment were terminated according to section 38 if section 197A could still apply to the situation. Section 38 does not force the parties to negotiate on whether the contracts should survive the initial 21 day suspension. It is

section 197A. In the past these two ways of keeping a business alive were confused for the purposes of the transfer, but as been noted, this led to a intolerable position.

²⁸⁸ clause 38(8)(a)

²⁸⁹ clause 38(8)(b)

²⁹⁰ clause 38(8)(c)

²⁹¹ clause 38(10)

therefore quite possible that the contracts can be terminated initially after the 21 days, but that the business is still later transferred. Would section 197A then apply? It seems so. Section 197A does not stipulate that the contracts of employment have to be in existence before it would be applicable. This however revives all the problems with the current section 197. Clearly, the proposed section 197A still needs some work, but at least it recognises the problems that currently exist.

On the whole the provisions of section 197A are mostly similar to those of section 197. The new section also provides that the rights and obligations between the old employer and each employee remain intact after the transfer²⁹² and anything done by the old employer in respect of each employee will be still be considered to have been done by the old employer.²⁹³ The motivation behind such provisions has already been discussed and mostly relate to the ease of transfer of the undertaking. Similarly to the current section 197, the proposed 197A also provides for the continuity of employment, except in the cases of the suspension of the contracts in terms of section 38 of the Insolvency Act. Other than that, section 197A is just a rehash of the proposed section 197 - with two main exceptions: the rights and obligations between the old employer and employees are not transferred,²⁹⁴ and there is no provision for the joint and severable liability of the old and new employer for claims arising prior to the transfer.²⁹⁵ The former exclusion has been discussed on two different occasions, while the latter one is intrinsically connected to it - if the new employer is not the recipient of the rights and obligations prior to the transfer, then it would not be possible for him to be liable for anything that happened before the transfer.

5.2.1 SECTION 311

An important difference between section 197A and the current section 197(1)(b) and (2)(b) is that the transfer of a business as a result of a scheme of arrangement is no longer expressly considered to be the transfer of a going concern for the purposes of the section. Such schemes of arrangement take place according to section 311 of the Companies Act and usually involve the cession of the debts of the company for a

²⁹² clause 47(b)197A(1)(b)

²⁹³ clause 47(b)197A(1)(c)

²⁹⁴ To prevent a discrepancy in the interpretation of the proposed s197A, subsection 5 directly excludes s197(3).

²⁹⁵ clause 47(b) re proposed section 197A(5) also excludes clause 47(a) re proposed section 197(9)

reduced price - something which would not in all cases qualify as the transfer of a going concern.

Section 311 of the Companies Act does have another important influence on the LRA however. According to the proposed section 197A(2) it is possible to vary the effects of subsection 1 through an agreement as contemplated by section 311. An agreement concluded through section 311 of the Companies Act is not a simple procedure and it will be necessary to discuss this procedure in some detail to ascertain the effect that it would have on the proposed section 197A

Section 311 enables the company to negotiate with the parties that have claims against it. The purpose of such negotiations is to conclude a contract that would alter the relationship between the company and the claimants. This is usually the case where financial difficulties on the part of the company necessitate a reduction in the claims of either the shareholders or the creditors. As a special precaution, such an agreement would be enforceable only after the court has sanctioned it.

In practice, section 311 is used to acquire tax advantages through a standard scheme of arrangement. A bankrupt company usually has a substantial assessed loss and this could be a valuable commodity to a prospective purchaser. The claims of the creditors would usually exceed the asset value of the company and they could easily be faced with the prospect of recovering less than 10 percent of their claim. Clearly it would be in the interest of the prospective buyer to reach a compromise with the creditors in order to acquire the assessed loss for only a fraction of its value. Section 20(1)(a) of the Tax Act however closes this door by providing the assessed loss would be reduced by the amount of any such compromise. In order to side step this provision and to ensure that the assessed loss is not reduced by the amount of the compromise with the creditors, the prospective buyer would benefit from an arrangement whereby the creditors could cede their rights to the buyer. Such an arrangement would be advantageous to the creditors as well: to interest them, the buyer would usually offer an amount exceeding the dividend on liquidation and such a process would also usually be much speedier than liquidation. The problem is that the buyer would need the consent of 100 percent of the creditors. Section 311 creates the mechanism to solve this problem: it provides that a majority of three-quarters of the votes at such a meeting would bind all the parties. There is a problem: the measures set out in section 311 are only effective in securing an agreement between the company and the parties. In reality the transaction will only

secure benefit for the purchaser of the business if such a transaction (usually a cession) was between the purchaser and the parties. As a result, several complicated schemes of arrangement have been formulated in order to make it seem like the company is indeed a party to the agreement, while a secondary arrangement between the purchaser and the parties takes place.

The content of such schemes of arrangement is a complicated matter and for the most part outside the scope of this thesis. What is relevant is that the basic content of this arrangement must be an agreement between the *company* and the parties.²⁹⁶ Although the purchaser might be the one that initiates the whole procedure and is usually the one that gains most from the arrangement, he is not considered to be a party to the agreement. Therefore, although the consequences of section 197A(1) can be altered by such an agreement the purchaser would not be able to affect this agreement - any decisions would be taken independent from him.²⁹⁷ This stands in contrast to the proposed section 197(7) that provides that the old employer, or new employer, or the old and new employer acting jointly can conclude the agreement. The most obvious dissimilarity between the two provisions however is not whether the old or new employer concludes the agreement on the one-side, but who the other parties are. According to section 197(7) the other parties are determined according to section 189(1) of the LRA. Section 197A refers us to section 311 of the Companies Act but nowhere in this section is there a reference to employees and their representatives, only to members of a company or its creditors. As a result it would seem that the employee and her representatives has absolutely no say in whether section 197A is adhered to or varied by agreement according to section 311. Herein lies the big difference between section 197 and section 197A. Section 197 is more concerned with securing a transfer of the failing business than protecting the employees - and this is not necessarily a bad thing - as insolvent businesses usually make for poor employers.

6 CONCLUSION

Of all the problems associated with the current format of section 197 relating to insolvency, the most controversial aspect seems to be the unclear wording of the this particular aspect of the section. It seems that the section does not apply to all cases of

²⁹⁶ *Ex Parte Kaplan: In re Robinson Consolidated Industries Ltd* 1987 (3) SA 413 (W)

²⁹⁷ In practice this would not be of any real detriment to the purchaser, as the company would surely not agree to any terms that jeopardise the transfer of the insolvent business.

liquidation or sequestration of the employer, but only to such limited cases where the employer is actually insolvent. Furthermore, the use of terms like "going concern" and "new employer" do not simplify the matter much either. Insolvent businesses can quite seldom be considered a going concern and the rescue of an insolvent business (a form of transfer according to section 197) would also most likely not involve the presence of a "new employer" in the legal sense.

It is clear that the effects of a transfer due to insolvency differ slightly from those of a normal transfer - the most notable difference being that the rights and obligations between the old employer and the employees are not transferred. A problematic aspect about the effects of section 197(1)(b) and (2)(b) is that it stands in direct conflict with section 38 of the Insolvency Act. This section provides that the contracts of employment are terminated by law on the liquidation/sequestration of the employer. Section 197(2)(b) however clearly implies that the contracts of employment are not terminated - and according to section 200, this overrides section 38. The result is endless confusion with regard to the position of the employer, employees and trustee/curator from the time of the liquidation/sequestration to the time of the transfer of the business when the contracts are either transferred or brought back to life.

The Amendment Act seeks to resolve this conflict. A new section 38 will provide that the contracts of employment are suspended for 21 days after the sequestration/liquidation. Providing no agreement is reached on employment after these 21 days, the contracts are still terminated by law. Unfortunately, there is no mechanism to ensure that the employer and the employees or their representatives are approached within this time - rather the focus seems to be on saving the business and providing for negotiations that would ensure the transfer of the business.

The new proposed section 197A seems to have the same focus - while the wording of the section is significantly expanded upon, the effects are mostly the same as those of the proposed section 197, barring a few exceptions related to the fact that the rights and obligations between the old employer and employee stay intact. However, section 197A provides for a completely different mechanism whereby the content of the section can be varied by agreement. In the case of section 197A such an agreement has to take place according to section 311 of the Companies Act. This section provides for a complicated mechanism whereby the company can conclude agreements with the shareholders or creditors of that company. In the interest of saving the business, the

employees and their representatives are not even consulted during such a procedure. The legislature might justify this by claiming that the interest of the business does in the end always override the interest of the employee - if the business comes to an end all employees would lose their jobs anyway. Such reasoning is sound and not new to the LRA. Employees in solvent businesses are faced with dismissals due to operational requirements for exactly the same reason. The only difference is that in the case of a dismissal by operation of law, as would eventually happen in the case of insolvency the employees are not protected under the LRA. It is questionable whether this is a position any trade union would be very happy with.

CHAPTER 7

CONCLUSION

1 THE VALUE OF FOREIGN JURISPRUDENCE

In an attempt to reduce the uncertainty surrounding section 197, the courts and certain writers have turned to foreign jurisprudence: the European Directive and the British Regulations being the most quoted. To a certain degree this approach was justified as the section was partly based on the Directive and the Regulations and valuable insight could be gained from such a study. The fact remains, however, that the wording and the circumstances surrounding these statutes are not entirely the same. And a useful analogy can only be stretched so far. As a result, the most important question that arises in this context is not whether the Directive and the Regulations and the court cases that result from the interpretation of these statutes, are of use, but how much weight should be afforded to these findings by our courts.

It might prove useful to study these provisions in order to fill the lacunas in our law and it might provide the necessary inspiration when new legislation is to be drafted, but ultimately, the law of each country should conform to the specific needs and circumstances in that country. Foreign jurisprudence is therefore only of limited use and should never have more than mere persuasive value. Too much attention to these provisions could be quite dangerous as it is very easy to misconstrue European and British case law. It is very tempting to snatch conclusions from such findings, without realising that most European countries have remedies and labour conditions that differ substantially from our own. Furthermore, there is such a huge assortment of foreign case material on the subject, quite a lot of it so contradictory that it would certainly not be wise to pay much heed to these cases unless we have a desire to emulate such confusion in our own law. Finally, one has to ask whether it is very wise to base any aspect of the labour law of a developing third world country on the provisions of a developed first world society. Surely to ensure long term success and growth of our economy, the flexibility and ease with which business can be transferred should be the first priority, superseding even at times the interest of the employees. In its current format, however section 197 is nowhere close to ensuring such flexibility.

2 INTERPRETATION

The interpretation of section 197 was problematic from the beginning and affects most aspects of this section. The reason for this uncertainty lies mostly in the careless wording of the section. In the light of the major changes brought about the LRA as a whole to the field of South African labour law, it seems that very little attention was paid to the drafting of section 197 itself. The results are quite obvious.

The main problems surrounding the interpretation of section 197 result from the use of the following terminology:

2.1 "TRANSFER ... BY THE OLD EMPLOYER"

Although it is quite clear what a transfer entails, the wording is confusing as section 197 refers to a transfer "by the old employer". In this light, it seems that section 197 therefore only covers a *direct* transfer that the old employer was a party to. The labour court has however on occasion²⁹⁸ applied an interpretation to "transfer" which also includes an *indirect* transfer.

The Amendment Bill also defines a transfer as being by one employer to another. Whether this will in future be taken to indicate that the section only applies to a direct transfer is an open question. It is submitted that such a narrow interpretation would not be in the interest of the employees as it would make it much simpler for the unscrupulous employer to circumvent section 197.

2.2 "TRANSFER OF A BUSINESS, PART OF A BUSINESS OR UNDERTAKING"

From the definition of a business, we draw the conclusion that a business is more than just assets and workers. Sometimes the mere transfer of assets may also be seen as a transfer of a business. The transfer of shares, on the other hand, never results in the transfer of the business as contemplated by section 197, because the sale of shares only cause a change in the possession and control of the company and not a change in employer.

With regard to the outsourcing of services, the question has arisen whether this results in the transfer of a business or if this is merely an opportunity to provide a service for a

²⁹⁸ *Tekweni Security Services CC v Mavana* 1999 ILJ 2721 (LC)

limited time only. For the time being, it seems that outsourcing would not be considered to be the transfer of a business. If the original employer still exercises too much control over the outsourced function it will not be considered to be fully transferred. If, however, assets are transferred along with the outsourced function, then this might be considered to be the transfer of a business or a part of a business.

3 EFFECTS

Section 197 has two primary consequences: it facilitates the transfer of the contracts of employment and it ensures that the terms and conditions of these transferred contracts stay intact. Certain problems also arise in this regard surrounding the duty to inform and consult and dismissals prior to the transfer.

3.1 TRANSFER

With regard to the transfer of the contracts of employment, three important issues exist: Does section 197 provide for the automatic transfer of the contracts of employment? Which employees are transferred when a part of a business is transferred? And do the employees have a right to object to their transferral?

3.1.1 AUTOMATIC TRANSFER

Section 197(2)(a) does not expressly provide for the automatic transfer of the contracts of employment. While the LAC has found that such a transfer should indeed be automatic, no solid arguments have been presented to justify such a marked deviation from the wording of the section except for the claim that section 197 is an employee protection section. A study of the previous Labour Bill and the foreign legislation, on which section 197 was based, does however indicate that the legislator did have just such an intention. For some reason this intention was never articulated clearly. Luckily this position will be clarified soon as the Labour Relations Amendment Bill proposes to provide unambiguously for the automatic transfer of the contracts of employment on the transfer of the business.

3.1.2 EMPLOYEES TRANSFERRED

Neither the legislator nor the courts have yet provided a standard whereby it can be determined which employees should be transferred along with a part of a business or undertaking. It has been established on various occasions that section 197 provides for the protection of the employees. It is therefore submitted that all employees that are

either exclusively employed in the part of the business that is transferred or those that may become redundant as a direct result of the transfer should be transferred.

3.1.3 EMPLOYEE'S OBJECTION

Even though the section attempts to protect the employees, it does not provide for a right to object to the transfer of the contracts. This is in stark contrast to the common law principles that provide that an employee has a very real interest in the employer he works for and should therefore always be able object to the transfer of his contract, if such an objection is deemed reasonable. Does section 197 completely negate this right? There is no consensus on this aspect.

3.2 MAINTENANCE OF THE TERMS

Except in the cases where section 197 provides for a transfer due to insolvency, all the rights and obligations between the employer and employee are transferred. Section 197 is very unspecific about the extent of the affected rights and obligations. To ensure an equitable result the exact scope of the rights and obligations transferred should rather be determined by agreement.

Collective agreements, on the other hand, are not covered at all. This is a major oversight that will be corrected in the near future. The way in which it should be corrected is however also problematic. It is submitted that to provide for the automatic transfer of collective agreements might not be totally satisfactory as collective agreements are the result of the circumstances and the relationship between the bargaining parties, something that would not necessarily be the same from one employer to the next.

Finally, the maintenance of the terms of employment lends a certain rigidity to section 197. In practice the employer would prefer to terminate the contracts of employment to improve the transferability of the business as new employers are not eager to acquire a business if they cannot employ the workers on their own terms. The Amendment Bill proposes to change this position radically by providing that changes to employment contracts on the transfer that are no less favourable than the original terms still constitute a transfer. This new flexible approach to the transfer of contracts of employment would do much to prevent dismissals prior to a transfer.

3.3 DUTY TO INFORM AND CONSULT

At common law there was a limited duty to inform and consult prior to the transfer. Neither section 197 nor the Amendment Bill makes reference to such a duty and it is unclear whether the old common law position is still operational. It is submitted that in practice such a duty would not be in the interest of the business as the publication of such information prior to the transfer could negatively effect this transaction. On the other hand, the LAC has held that section 197 is an employee protection provision. It is quite possible to argue that such a provision would not take away any of the common law rights of the employees without stating so unambiguously. It is possible to argue that the duty to consult and inform therefore still exists in our law.

3.4 DISMISSAL

Currently a dismissal solely based on the transfer of a business is not automatically unfair. Such dismissals are usually based on operational requirements. Unfair dismissals would result in the reinstatement of the employee in the service of the new employer. In the case of an unfair dismissal due to a transfer based on insolvency, the employee would only be able to claim damages or reinstatement from the old employer.

The Amendment Bill proposes that any dismissal based on the transfer of a business should qualify as an automatically unfair dismissal, except where the dismissal can be justified on the grounds of operational requirements. This proposal only affects the instance where dismissals prior to a transfer are justified on some other grounds.

4 INSOLVENCY

This controversial aspect of section 197 contains so many ambiguities and creates so many interpretational problems that it seems that the only way in which it can be rectified is through the intervention of the legislator. The main origin of these problems is the incompatibility of section 197 with section 38 of the Insolvency Act. The uncertainty as to whether the contracts of employment are terminated on insolvency, or whether they survive or are merely revived on a later stadium greatly confuses the position of the employees and curator/trustee until the time of the transfer. In an attempt to clarify this position the Labour and the Insolvency Amendment Bills advise drastic changes to the current legislation. The aggregate effect of these proposals will be that the contracts of employment do not terminate until at least 21 days after the insolvency. Negotiations to ensure that an agreement about a transfer

within that time is encouraged. Furthermore a new section 197A proposes to regulate the transfer of the contracts in more detail.

5 AMENDMENT BILL

The Labour Relations Amendment Bill is an attempt at streamlining certain aspects of the LRA that have proven problematic since its inception. It therefore addresses many of the problems that exist within the current format of section 197. There is, however, still room for improvement. The following matters in particular raise questions.

1. The Bill defines a business as an "economic entity". How literally should this be interpreted? Does this definition exclude the public sector and non-profit organisations? The Directive defines a business in a similar way, yet many of the groundbreaking European cases on the transfer of employment contracts involved non-profit organisations. Should a similar approach be adopted in South Africa?
2. The Bill does not provide the employee with a right to refuse to be transferred. If the protection of the employee is the main aim of section 197, should such a right not be incorporated? (As is the case in England and Germany.)
3. The wording of section 197(3)(c) is overly wide.
4. Should organisational rights be *automatically* transferred from the old employer to the new employer? It is submitted that without an obligation on the side of either party to renegotiate the organisational rights after the transfer such an automatic transfer may be detrimental to one or both of the parties.
5. It is questionable whether the old employer should be able to conclude an agreement with the parties specified in section 189 on his own if this agreement will eventually bind the new employer.
6. There is still no provision that the employees be notified prior to a normal transfer according to section 197.

Finally, with regard to the Insolvency Amendment Bill. Section 38 of the Insolvency Amendment Bill provides that the contracts of employment are suspended for 21 days

before they are terminated. Until such time, no provision exists that ensures that an agreement is reached as to whether the contracts should continue in life after such time.

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