EMPLOYEE PROTECTION DURING BUSINESS RESCUE PROCEEDINGS IN SOUTH AFRICA: A COMPARATIVE PERSPECTIVE

by

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MRTKEL002

Submitted in fulfillment of the requirements for the degree of Master of Laws (Commercial Law)

At the University of Cape Town

December 2013

Supervisor: Richard Bradstreet

Word Count: 24 001

Research dissertation/research paper presented for the approval of Senate in fulfillment of part of the requirements for the LLM in approved courses and a minor dissertation/research paper. The other part of the requirement for this qualification was the completion of a programme of courses.

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I INTRODUCTION

The Companies Act 71 of 2008 (hereafter ‘the Companies Act 2008’) came into force in 2011, bringing with it a corporate rescue regime called ‘business rescue’. If a business is placed under business rescue there are a multitude of legal consequences that follow. A thorough reading of the business rescue provisions reveals that employees are granted a large number of important rights and protections when their employer is placed under business rescue.

This dissertation consolidates the company law and labour law aspects of this area of law in order to gain comprehensive understanding of the protection given to employees during business rescue. It is important for lawyers, employees, employers and business rescue practitioners to understand what rights employees have during business rescue in order for those rights to be enforced and utilised effectively.

While the protection of employees is undeniably an important objective, it has been argued that the amount of protection afforded to employees in chapter 6 is worrying in that their over-protection could potentially be detrimental to the overall success of the business rescue proceedings.¹ This may ultimately have a negative effect on employees as it is in the best interests of the employees for the business rescue proceedings to be successful.

The focus of this dissertation is therefore on whether employees in South Africa are afforded too much protection during business rescue proceedings and, if so, which provisions are problematic. In order to answer this question I have outlined the rights of employees during business rescue in South Africa and have compared this to the protection afforded to employees in both Australia and the United Kingdom. These

two countries share Commonwealth heritage with South Africa and have business rescue regimes with objectives almost identical to the South African regime. I have then assessed the South African provisions in light of the comparison.

(a) Introduction to the Companies Act 2008

The law governing companies is vitally important for a number of reasons, one of which is that it directly impacts the economy and the way in which business is conducted in a country.² Companies are economically important in terms of both creating wealth and in terms of the restoration of society.³ Badly drafted or out of date legislation can have devastating effects on an economy, while carefully drafted and comprehensive legislation can promote economic growth. It is therefore vitally important that South Africa’s company law is up to date, concise and well drafted.

Prior to the Companies Act 2008, South Africa’s company law was governed by the Companies Act 61 of 1973 (hereafter ‘the Companies Act 1973’). This Act was in force for 37 years and was amended almost every year since it was enacted.⁴ For this reason, the Companies Act 1973 has been described as ‘a cut and paste piece of legislation’.⁵ The foundations of the Companies Act 1973 were based on Victorian English law, and the fact that English company law was reviewed in the early 2000s was an indication that the same needed to be done in South Africa.⁶ The legislation was out-dated, complicated and overly technical.⁷

In the new millennium the South African government recognised that South Africa’s company law needed to be changed dramatically.⁸ It was clear that the environment in which South Africa’s corporate legislation had to operate had changed materially since 1973.⁹ Most importantly, the apartheid regime had ended and South Africa

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⁴ Carl Stein & Geoff Everingham The New Companies Act Unlocked (2011) at 3.
⁵ Ibid.
⁶ Department of Trade and Industry Guidelines op cit note 3 at 5.
⁷ Cassim et al op cit note 2 at 3.
⁸ Stein & Everingham op cit note 4 at 3.
⁹ Cassim et al op cit note 2 at 3.
became a democracy subject to a new constitution. These changes affected the economic, social and political environment in South Africa. The regulation of companies was also affected by new legislation that came into force after 1973, for example, the Consumer Protection Act 68 of 2008, the Labour Relations Act 66 of 1995 (hereafter ‘the LRA’) and the National Credit Act 34 of 2005. Additionally, there were global changes that occurred which impacted how corporations needed to be governed. For example, over time business became increasingly globalised and there was a revolution regarding the use of electronic communication in business. New corporate concepts such as high corporate governance standards and new disclosure and accountability standards had also come into play since the Companies Act 1973 was enacted. Due to these global changes many jurisdictions started to review and change their company law.

The Department of Trade and Industry started the process of reform in 2003. In May 2004 the Department published a policy paper called ‘South African Company Law for the 21st Century: Guidelines for Corporate Law Reform’ in which the Department recognised the local and global developments and cited them as important reasons for the review of South Africa’s company law. The policy paper also stated that South Africa’s company law would be reviewed in its entirety, meaning that the review would include not only the Companies Act 1973, but also the common law and the Close Corporations Act 69 of 1984. Once the policy paper was published, the Department initiated public consultation sessions in order to receive comments on the contents of the paper. The sessions spanned over four months and were conducted in all nine provinces. In addition, there were workshops involving the Portfolio Committee on Trade and Industry of the National

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11 Cassim et al op cit note 2 at 4.
12 Stein & Everingham op cit note 4 at 2.
13 Ibid at 1.
14 Cassim et al op cit note 2 at 3.
15 Department of Trade and Industry Guidelines op cit note 3 at 9.
16 Stein & Everingham op cit note 4 at 3.
17 Department of Trade and Industry Guidelines op cit note 3.
18 Ibid at 5.
19 Ibid at 11.
Parliament of South Africa and the Select Committee on Economic and Foreign Affairs.\textsuperscript{21}

The drafting process commenced in late 2005 and in 2007 the first of a number of draft Companies Bills was published.\textsuperscript{22} In 2008, Parliament accepted the final draft and on 8 April 2009 it was signed by the President of South Africa. On 9 April 2009 it was published in the \textit{Government Gazette} 3212 (Notice No. 421) as the Companies Act 71 of 2008. However, the Act did not come into force automatically once signed as the Act specifically stated that it would come into force on a fixed date set by the President.\textsuperscript{23} The Companies Amendment Act 3 of 2011 was enacted to address some of the concern and errors in the Act and on 1 May 2011 the amended Companies Act 71 of 2008 came into force.\textsuperscript{24}

II OVERVIEW OF BUSINESS RESCUE

This chapter will provide a basic overview of the business rescue provisions found in the Companies Act 2008. The aim of this overview is to give context to the rest of this paper and to provide a concise summary of what business rescue is. It is necessary to have at least a basic understanding of how business rescue works in order to understand and critically evaluate how employees are protected when their employer is placed under business rescue. The rights of employees and affected persons (the definition of which includes employees) are summarised in more detail in the next chapter. This overview is important as these rights need to be read and understood in the context of the business rescue procedure as a whole.

Before discussing the business rescue provisions in chapter 6 of the Companies Act 2008, it is important to understand that ‘business rescue’ was not the first corporate rescue regime in South Africa.\textsuperscript{25} Before the Companies Act 2008 came into force, the ‘rescuing’ of a company in financial distress was governed by a procedure called judicial management. This procedure was introduced to South Africa in the

\textsuperscript{21} Ibid.
\textsuperscript{22} Stein & Everingham op cit note 4 at 4.
\textsuperscript{23} Mongalo op cit note 20 at 25.
\textsuperscript{24} Stein & Everingham op cit note 4 at 5.
\textsuperscript{25} Joubert, van Eck & Burdette op cit note 1 at 74.
Companies Act 46 of 1926 and was retained, with some amendments, in the Companies Act 1973.\textsuperscript{26} It is generally accepted that judicial management was unsuccessful and ineffective in practice due to a number of weaknesses.\textsuperscript{27} One of those weaknesses was that judicial management relied heavily on court proceedings and therefore highly trained personnel, making it an expensive remedy for companies that were already in financial distress.\textsuperscript{28} Another factor which led to judicial management being unsuccessful was that the South African courts’ attitude towards judicial management was that it was a remedy to be used only in exceptional circumstances.\textsuperscript{29} The business rescue provisions introduced in the Companies Act 2008 replaced the judicial management procedure in the Companies Act 1973 and addressed a number of the weaknesses.\textsuperscript{30} For the purposes of this dissertation it is important to note that another identified weakness of judicial management is that the interests of the creditors were emphasised over and above the interests of other parties.\textsuperscript{31} As will be discussed in this chapter, the new business rescue provisions address this problem by shifting the focus of the procedure to a broader category of persons affected by business rescue.\textsuperscript{32}

Section 7(k) of the Companies Act 2008 states that one purpose of the Act is ‘to provide for the efficient rescue and recovery of financially distressed companies, in a manner that balances the rights and interests of all relevant stakeholders’. In order to achieve that purpose, the Act introduced ‘business rescue’ which is dealt with in Chapter 6 of the Companies Act 2008. These provisions were shaped by corporate

\textsuperscript{26} Ibid.
\textsuperscript{30} Joubert, van Eck & Burdette op cit note 1 at 75.
rescue regimes in countries like the United Kingdom and the United States of America.\textsuperscript{33}

Chapter 6 contains its own definition section in which it defines business rescue as ‘proceedings to facilitate the rehabilitation of a company that is financially distressed’ by placing the company and the management of its business, property and affairs under temporary supervision, by placing a moratorium on the rights of those with claims against the company and by providing for the development and implementation of a business rescue plan by a business rescue practitioner.\textsuperscript{34} The definition goes on to say that the business rescue plan should restructure the company in such a way that the probability of the company continuing to exist on a solvent basis is increased or, if that is not possible, to give the company’s creditors or shareholders a better return than if the company went into liquidation immediately.\textsuperscript{35} The central idea is that the company may be worth more if it continues to run as a going concern than if it is placed under liquidation.\textsuperscript{36}

In order for a company to be placed under business rescue it must be in financial distress which is defined by the Act as a company which is reasonably likely to be unable to pay its debts as they fall due within six months, or likely to become insolvent within six months.\textsuperscript{37}

What follows is a discussion of the main aspects of the business rescue provisions. Namely, commencement of business rescue, the business rescue practitioner, the business rescue plan, the legal effects of business rescue, the rights of affected persons and the termination of business rescue proceedings.

\textit{(a) Commencement of Business Rescue}

Business rescue proceedings can commence in two different ways. Firstly, the company’s board of directors can pass a resolution in terms of s 129 to voluntarily

\textsuperscript{33} Joubert, van Eck & Burdette op cit note 1 at 74.
\textsuperscript{34} Companies Act 2008 s 128(1)(b).
\textsuperscript{35} Companies Act 2008 s 128(1)(b).
\textsuperscript{36} Cassim et al op cit note 2 at 862. Also see Rajak & Henning op cit note 28 at 277.
\textsuperscript{37} Companies Act 2008 s 128(1)(f).
begin proceedings\textsuperscript{38} or, secondly, an affected person can apply to court for an order that the company be placed under business rescue in terms of s 131.\textsuperscript{39}

(i) Commencement by Board Resolution

Arguably one of the most important sections in the Act, s 129 allows the board of directors to enter into business rescue voluntarily without a court order and without shareholder approval.\textsuperscript{40} In order for the board of directors to place the company under business rescue in terms of s 129, it must have reasonable grounds for believing that the company is in financial distress and reasonable grounds for believing that ‘rescuing the company’\textsuperscript{41} is a reasonable prospect.\textsuperscript{42} In these circumstances business rescue proceedings begin once the resolution has been filed or once the company has applied to court in terms of s 129(5)(b) for consent to file the resolution.\textsuperscript{43} If the company is already under liquidation, such liquidation proceedings are a bar to adopting a s 129 resolution.\textsuperscript{44} Additionally, once the resolution has been adopted, the company may not adopt a resolution to place the company under liquidation until the business rescue proceedings have ended.\textsuperscript{45}

Once the resolution has been filed, the company has five business days to publish a notice of the adopted resolution to every affected person,\textsuperscript{46} along with a sworn statement of the relevant facts, and to appoint a business rescue practitioner.\textsuperscript{47} Within two business days after the practitioner is appointed the company has to file a notice of the appointment, and within five business days the company has to publish a copy of the notice to each affected person.\textsuperscript{48}

\textsuperscript{38} Companies Act 2008 s 129(1).
\textsuperscript{39} Companies Act 2008 s 131(1).
\textsuperscript{40} Stein & Everingham op cit note 4 at 412.
\textsuperscript{41} As defined in the Companies Act 2008 s 128(1)(b).
\textsuperscript{42} Companies Act 2008 s 129(1)(a) and (b).
\textsuperscript{43} Companies Act 2008 s 132(1)(a).
\textsuperscript{44} Companies Act 2008 s 129(2).
\textsuperscript{45} Companies Act 2008 s 129(6).
\textsuperscript{46} As defined in chapter II(a)(ii) of this dissertation.
\textsuperscript{47} Companies Act 2008 s 129(3)(a) and (b).
\textsuperscript{48} Companies Act 2008 s 129(4)(a) and (b).
An affected person can apply to court for an order that the resolution of the board be set aside on the grounds that the company is not financially distressed, rescuing the company is not a reasonable prospect or the procedural requirements set out in s 129 have not been complied with.49 Attempting to have the resolution or appointment of the practitioner set aside may be an expensive and complicated decision as an application to court will have to be made and the affected person has the onus of proving one of the grounds mentioned above. If the board does not pass a s 129 resolution despite that fact that there are reasonable grounds for believing that the company is in financial distress, the board must explain why they did not adopt such a resolution to all affected persons.50

(ii) Commencement by Court Order

The second way that a company can be placed under business rescue is by court order in terms of s 131. The application would have to be made by an affected person,51 which the Act defines as:

‘A shareholder or creditor of the company, any registered trade union representing employees of the company and, if any of the employees of the company are not represented by a registered trade union, each of those employees or their respective representatives’.52

As these groups of people can be materially affected during business rescue proceedings they are referred to as ‘affected persons’ as a collective group and are given a wide range of rights during business rescue proceedings.53

An affected person can bring a s 131 application provided there is no s 129 resolution in place.54 The party bringing the application would have to give notice of the application to all other affected persons and would have to serve the company and Commission a copy of the application.55 Once the application is made, business

49 Companies Act 2008 s 130(1)(a).
50 Companies Act 2008 s 129(7).
51 Companies Act 2008 s 131(1).
52 Companies Act 2008 s 128(1).
53 Stein & Everingham op cit note 4 at 411.
54 Companies Act 2008 s 131(1).
55 Companies Act 2008 s 131(2).
rescue proceedings begin.\textsuperscript{56} If the court is satisfied that rescuing the company is a reasonable prospect and that the company is either in financial distress, has ‘failed to pay over any amount in terms of an obligation under or in terms of a public regulation, or contract, with respect to employment-related matters’\textsuperscript{57} or if it is otherwise just and equitable, the court may grant the order.\textsuperscript{58} If the court grants such an order it may appoint an interim practitioner who has been nominated by the party bringing the application, as long as the nominated interim practitioner satisfies the requirements set out in s 138. This appointment would have to be ratified at the first meeting of creditors by the holders of a majority of the independent creditors’ voting interests.\textsuperscript{59}

If an order in terms of s 131 is made the company cannot place itself under liquidation until the proceedings have ended and the company must, within five business days of the order, notify affected persons of the order.\textsuperscript{60}

\textit{(b) The Business Rescue Practitioner}

Section 128(1) of the Act states that ‘business rescue practitioner’ means:

\begin{quote}
'[A] person appointed, or two or more persons appointed jointly, in terms of this Chapter to oversee a company during business rescue proceedings and “practitioner” has a corresponding meaning.'
\end{quote}

Once a practitioner has been appointed he or she holds a number of powers and duties during the business rescue proceedings. The practitioner gains control of the management of the company, substituting the board of directors and previous management of the company.\textsuperscript{61} However, the practitioner can delegate his or her powers and functions to a member of the board or previous management.\textsuperscript{62} The practitioner has the power to remove a person from the management of the

\begin{footnotes}{\footnotesize
\item[56] Companies Act 2008 s 132(1)(b).
\item[57] Companies Act 2008 s 131(4)(a)(ii).
\item[58] Companies Act 2008 s 131(4)(a).
\item[59] Companies Act 2008 s 131(5).
\item[60] Companies Act 2008 s 131(8).
\item[61] Companies Act 2008 s 140(1)(a).
\item[62] Companies Act 2008 s 141(1)(b).
}\end{footnotes}
company\textsuperscript{63} or, subject to s 140(2), appoint a person to management.\textsuperscript{64} The practitioner must also develop and implement (if adopted) a business rescue plan.\textsuperscript{65}

The practitioner is also required to investigate the affairs of the company in order to determine whether there is a reasonable prospect that the company can be rescued.\textsuperscript{66} If there is no reasonable prospect that the company can be rescued the practitioner must make an application to court for an order discontinuing business rescue proceedings and ordering that the company be placed under liquidation.\textsuperscript{67}

\textit{(c) The Business Rescue Plan}

It is the business rescue practitioner’s responsibility to develop and implement a business rescue plan.\textsuperscript{68} In order to develop the business rescue plan the practitioner must consult with the creditors of the company, its management and other affected persons.\textsuperscript{69} The company must publish this plan, after which the practitioner must hold a meeting of creditors and other holders of a voting interest to consider and possibly adopt the plan.\textsuperscript{70} A notice of the meeting must be given to all affected persons at least five business days before the meeting, including information on the date, time and place of the meeting, the agenda of the meeting and the voting and participation rights of affected persons.\textsuperscript{71} At the meeting the practitioner must introduce the proposed plan, state whether he or she still believes that there is a reasonable prospect of rescuing the company, give the employees’ representatives a chance to address the meeting and accommodate discussion and voting on motions to amend the plan or to adjourn the meeting to revise the plan.\textsuperscript{72} The practitioner must then hold a vote for the preliminary approval of the proposed plan.\textsuperscript{73}

\textsuperscript{63} Companies Act 2008 s 140(1)(c)(i).
\textsuperscript{64} Companies Act 2008 s 140(2) says that the practitioner may not appoint a person to management if that person has a relationship with the company that would make a reasonable third person think that due to the relationship the integrity, impartiality or objectivity of the person is questionable, or be related to a person with such a relationship.
\textsuperscript{65} Companies Act 2008 s 140(1)(d)(i) and (ii).
\textsuperscript{66} Companies Act 2008 s 141(1).
\textsuperscript{67} Companies Act 2008 s 141(2)(a)(ii).
\textsuperscript{68} Companies Act 2008 s 140(1)(d).
\textsuperscript{69} Companies Act 2008 s 150(1).
\textsuperscript{70} Companies Act 2008 s 150(1).
\textsuperscript{71} Companies Act 2008 s 151(2).
\textsuperscript{72} Companies Act 2008 s 152(1)(a)-(d).
\textsuperscript{73} Companies Act 2008 s 152(1)(e).
The proposal will be adopted on a preliminary basis if the holders of more than seventy five per cent of the creditors’ voting interests vote in favour of the plan, which must include at least fifty per cent of the independent creditors’ voting interests. If not, the plan is rejected.

Whether the plan is deemed to also be adopted on a final basis depends on whether the plan alters the rights of the holders of a class of the company’s securities. If the plan is finally adopted it binds the company, the company’s creditors and the holders of the company’s securities, whether or not they were at the meeting convened in terms of s 151, voted in favour of the adoption of the plan or whether, with regards to creditors, they had proven their claim against the company. According to Cassim et al this is known as ‘cramdown’, which is described as ‘the process by which creditors are forced to accept a reorganisation or business rescue plan, even against their wishes’. This provision makes it possible for the company to implement the business rescue plan despite the fact that one or more creditors object to its implementation.

If the business rescue plan is rejected the practitioner may, in terms of s 153, prepare and publish a revised plan after a vote of approval from the holders of voting interests or apply to court to set aside the result of the vote on the grounds that it was inappropriate. If the practitioner does not take either of these steps, an affected person at the meeting can require the practitioner to prepare and publish a revised plan by getting a vote of approval from the holders of voting interests or can apply to court to set aside the result of the vote on the grounds that it was inappropriate. Affected persons could also offer to buy the voting interests of persons who oppose

74 Companies Act 2008 s 152(2).
75 Companies Act 2008 s 152(3)(a).
76 In terms of s 152(3)(b) and (c), if the plan does not alter these rights, the preliminary adoption of the plan is deemed to constitute the final adoption of the plan. If the rights of any class of holders of the company’s securities are altered by the plan, the holders of the classes of securities whose rights would be altered must vote for the approval of the plan at a meeting held by the practitioner. If the majority of the voting rights exercised are in favour of adoption, the plan is finally adopted. However, if the majority do not vote in favour of adoption, the plan is rejected.
77 Companies Act 2008 s 152(4).
78 Cassim et al op cit note 2 at 907.
79 Ibid.
80 Companies Act 2008 s 153(1)(a).
81 Companies Act 2008 s 153(1)(b)(i).
the plan.\textsuperscript{82} If such an offer is made the practitioner is required to adjourn the meeting for no more than five business days.\textsuperscript{83}

\textit{(d) Legal Effects of Business Rescue}

One of the most important effects that business rescue proceedings have on a company is the general moratorium on legal proceedings against the company. Legal proceedings may not be commenced or continued against the company or its property while business rescue proceedings are in place.\textsuperscript{84} This means that a creditor may not enforce their debt against the company or enforce judgment against the company during business rescue. Essentially, the moratorium gives the company breathing space. There are, however, a number of exceptions to this rule.\textsuperscript{85}

When a company commences business rescue it is important that they receive post-commencement finance so that the company can continue to operate as a going concern. Investors will want their claim to be secure as there is a lot of risk involved in investing in a financially distressed company. In order to encourage banks and creditors to finance the company, the company may use any unencumbered asset as security for such finance.\textsuperscript{86}

The Act provides an order of preference in which such financing will be repaid.\textsuperscript{87} Importantly, the order of preference set out in s 135 will continue to operate in the event that the business rescue proceedings are succeeded by a liquidation order.\textsuperscript{88} Firstly, the remuneration and expenses of the practitioner and the cost of the business rescue proceedings will be paid, followed by money owing to employees for unpaid remuneration which became due and payable after the commencement of business rescue.\textsuperscript{89} Secured post-commencement finance ranks third and unsecured post-

\begin{footnotes}
\item[82] Companies Act 2008 s 153 (1)(b)(ii).
\item[83] Companies Act 2008 s 153(4).
\item[84] Companies Act 2008 s 133(1).
\item[85] For example, in terms of s 133(1) legal proceedings may be commenced against the company if the practitioner provides written consent, if leave of the court is obtained or if they are criminal proceedings against the company, its directors or its officers.
\item[86] Companies Act 2008 s 135(2)(a).
\item[87] Companies Act 2008 s 135(2)(b).
\item[88] Companies Act 2008 s 135(4).
\item[89] Companies Act 2008 s 135(3).
\end{footnotes}
commencement finance fourth. Secured pre-commencement finance ranks fifth. Then money owing to employees for unpaid remuneration which became due and payable before the commencement of business rescue will be paid. Lastly, unsecured pre-commencement finance ranks seventh. This order of preference was set out in the case of Merchant West Working Capital Solutions (Proprietary) Limited v Advanced Technologies & Engineering Company (Proprietary) Limited & Gainsford. Joubert, van Eck and Burdette argue that there are ‘surprising priorities created by this section’ as due to this order of preference it is likely that during business rescue the post-commencement finance that the company receives will be used to pay the salaries of the employees and the fees of the business rescue practitioner before the lender of the post-commencement finance is repaid.

In terms of the effect of business rescue on general contracts, the Companies Act 2008 initially granted the practitioner the power to cancel or suspend the whole or part of a pre-existing contract, unless the contract was a contract of employment. This provision was amended by s 87 of the Companies Amendment Act 3 of 2011. Section 136(2)(b) now says that if the practitioner wants to cancel the whole or part of a pre-existing contract, he or she has to apply to court before he or she can do so. The other party to the suspended or cancelled contact may not claim specific performance, but they do have a claim against the company for damages.

(e) Rights of Affected Persons

Part C of Chapter 6 deals with ‘Rights of Affected Persons During Business Rescue Proceedings’. Under this Part, the rights of employees, creditors and holders of the company’s securities are set out.

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90 Stein & Everingham op cit note 4 at 421.
91 Ibid.
93 Joubert, van Eck & Burdette op cit note 1.
94 Ibid at 79.
95 The effect of business rescue on employment contracts will be discussed in chapter III of this dissertation.
96 Companies Act 2008 s 136(2).
97 Cassim et al op cit note 2 at 886.
98 Companies Act 2008 s 136(3).
As the rights of employees and other affected persons are discussed in detail later in this dissertation, they will not be discussed at length in this chapter. At this point it is sufficient to say that s 144 grants employees a number of rights during business rescue which they can exercise through their trade union or, if they are not represented by a trade union, either directly, or by proxy through an employee organisation or representative.\textsuperscript{99}

The creditors and holders of the company’s securities of a company are also granted a number of rights, such as the right to notice of court proceedings, decisions, meetings and other events regarding the business rescue proceedings, to participate in court proceedings and to participate in the business rescue proceedings to the extent that the Companies Act allows. In addition, creditors are entitled to make proposals for a business rescue plan\textsuperscript{100} and holders of the company’s securities are entitled vote for or against a proposed business rescue plan if the plan would alter their rights.\textsuperscript{101}

S 145(3) entitles creditors to form a creditors’ committee, through which the practitioner must consult the creditors when developing the business rescue plan.\textsuperscript{102} The creditors’ committee may not give the practitioner directions, but can consult the practitioner about matters concerning the business rescue proceedings\textsuperscript{103} and receive reports concerning the proceedings.\textsuperscript{104}

\textit{(f) Termination of Business Rescue Proceedings}

There are four ways in which business rescue proceedings can end. Firstly, if the court sets aside a s 129 resolution or s 131 court order commencing business rescue proceedings or converts those proceedings into liquidation proceedings.\textsuperscript{105} Secondly, proceedings end if the practitioner files a notice terminating the proceedings with the

\textsuperscript{99} Companies Act 2008 s 144(1).
\textsuperscript{100} Companies Act 2008 s 145(1).
\textsuperscript{101} Companies Act 2008 s 146(a)-(d).
\textsuperscript{102} Companies Act 2008 s 145(3).
\textsuperscript{103} Companies Act 2008 s 149(1)(a).
\textsuperscript{104} Companies Act 2008 s 149(1)(b).
\textsuperscript{105} Companies Act 2008 s 132(2)(a).
Commissioner.\textsuperscript{106} Thirdly, business rescue proceedings end if a business rescue plan has been proposed and rejected and no affected person has tried to extend the business rescue proceedings in terms of s 153.\textsuperscript{107} Lastly, business rescue proceedings end if the plan is adopted and the practitioner later files a notice of substantial implementation.\textsuperscript{108}

III EMPLOYEE PROTECTION IN CHAPTER 6 OF THE COMPANIES ACT 2008

While the last chapter introduced the Companies Act 2008 and discussed the business rescue provisions in a broad overview, this chapter will go into more detail on what protection employees are afforded during business rescue proceedings. Chapter 6 protects employees in two ways during business rescue proceedings. Firstly, there are provisions that give employees rights in their individual capacity as employees, and secondly there are rights that are afforded to employees in their capacity as an ‘affected person’.

(a) Rights as an Employee

It is clear from the business rescue provisions in the Companies Act 2008 that the rights of employees during business rescue proceedings are of significant importance. The majority of these rights are set out in s 144, however, there are other sections containing employee rights. It is important to note that s 144(5) states that the rights that are mentioned in s 144 are not exhaustive of the rights of employees as they are ‘in addition to any other rights arising or accruing in terms of any law, contract, collective agreement, shareholding, security or court order’.\textsuperscript{109} This means that, for example, the employees are also entitled to the rights that they have under their contracts of employment and under South African labour law. These additional rights provide employees with substantial protection over and above the protection afforded to them by the Companies Act 2008. This is particularly relevant when the

\textsuperscript{106} Companies Act 2008 s 132(2)(b).
\textsuperscript{107} Companies Act 2008 s 132(2)(c)(i).
\textsuperscript{108} Companies Act 2008 s 123(2)(c)(ii).
\textsuperscript{109} Companies Act 2008 s 144(5).
business rescue plan contemplates retrenching employees or where a part of the business is sold as a going concern as, in these circumstances, South Africa’s labour law provides extensive protection to employees.

In terms of how an employee may exercise their rights, the Act states that they may be exercised through a trade union if the employee is represented by one or, if not, directly or through an employee representative or organisation.\(^{110}\) If the rights are exercised through a trade union they must be exercised in accordance with South Africa’s labour law.\(^{111}\)

Section 144(3) sets out a list of rights that the employees or their trade unions are entitled to during business rescue proceedings. This section is set out below.

‘(3) During a company’s business rescue process, every registered trade union representing any employees of the company, and any employee who is not so represented, is entitled to—
(a) notice of each court proceeding, decision, meeting or other relevant event concerning the business rescue proceedings and such notice must be given to employees at their workplace and served at the head office of the relevant trade union;
(b) participate in any court proceedings arising during the business rescue proceedings;
(c) form a committee of employees’ representatives;
(d) be consulted by the practitioner during the development of the business rescue plan, and afforded sufficient opportunity to review any such plan and prepare a submission contemplated in section 152(1)(c);
(e) be present and make a submission to the meeting of the holders of voting interests before a vote is taken on any proposed business rescue plan, as contemplated in section 152(1)(c);
(f) vote with creditors on a motion to approve a proposed business plan, to the extent that the employee is a creditor, as contemplated in subsection (1); and
(g) if the proposed business rescue plan is rejected, to—
(i) propose the development of an alternative plan, in the manner contemplated in section 153; or
(ii) present an offer to acquire the interests of one or more affected persons, in the manner contemplated in section 153.’

This section demonstrates the wide range of rights that employees have in terms of notice and participation. There has clearly been a recognition that employees should

\(^{110}\) Companies Act 2008 s 144(1).
\(^{111}\) Companies Act 2008 s 144(1)(a)(ii).
be informed of what is happening, should be given an opportunity to have their opinions heard and should be entitled to participate in certain circumstances.

Employees are also given extensive protection if the company owes them any money. If the company owes an employee any money (remuneration, reimbursement for expenses or any other employment related money) that became due and payable before business rescue proceedings began and the employee was not paid that amount immediately before proceedings began, s 144(2) states that the employee is a preferred unsecured creditor of the company to the extent of the amount owing. In these circumstances the employee will be paid after post-commencement finance and before unsecured creditors.\(^\text{112}\)

However, employees are given even more protection when it comes to post-commencement finance. If an amount owing to an employee by the company (remuneration, reimbursement for expenses or any other employment-related debt) becomes due and payable during business rescue proceedings, that money is deemed to be post-commencement finance\(^\text{113}\) and enjoys super-priority status when it comes to repayment. They therefore rank extremely high on the order of preference for repayment, above any non-employment related post-commencement finance and any pre-commencement finance, regardless of whether or not those claims are secured.\(^\text{114}\)

Medical and pension schemes that are for the benefit of past or present employees are also protected by the Act. The medical or pension scheme will be an unsecured creditor of the company for any amount which was due and payable to the trustees of a scheme before business rescue proceedings commenced and was not paid immediately before the proceedings commenced.\(^\text{115}\) On the other hand, if the scheme is a defined benefit pension scheme, the scheme will be an unsecured creditor to the extent of the value of any unfunded liability under that scheme at the time business rescue proceedings commenced.\(^\text{116}\)

\(^{112}\) Cassim et al op cit note 2 at 900.
\(^{113}\) Companies Act 2008 s 135(1).
\(^{114}\) Companies Act 2008 s 135(3).
\(^{115}\) Companies Act 2008 s 144(4)(a).
\(^{116}\) Companies Act 2008 s 144(4)(b).
As stated in s 144(3)(c), employees have the right to establish a committee of employees’ representatives. It is the practitioner’s responsibility to hold a first meeting of employees’ representatives within ten days after he or she has been appointed. At this meeting the practitioner must notify the meeting whether or not he or she believes that rescuing the company is a reasonable prospect. The employees’ representatives then decide whether to appoint an employees’ committee. If they decide to appoint a committee the representatives will appoint the members of such committee. Notice of this meeting must be given to the trade unions representing the employees by the practitioner. If there are employees that are not represented by a trade union this notice must be given to the employees or their representatives.

Like creditors, the committee may confer with the practitioner about business rescue proceedings related matters but may not give the practitioner instructions as to what he or she must or should do. The committee may also receive and deliberate about business rescue proceedings reports on behalf of the employees and is obliged to act independently of the practitioner so that the interests of the employees are represented fairly in an unbiased manner. The benefit of having such a committee is that it gives the employees a unified voice and facilitates communication between the employees and the practitioner.

The effect that business rescue will have on employees is something that the practitioner is required to include in the plan. Under the heading ‘Assumptions and Conditions’ the business rescue plan must set out the anticipated effect that the plan will have on the number of employees employed by the company and the effect that the plan will have on the employees’ terms and conditions of employment.

Section 136(1) deals with the effect that business rescue proceedings will have on employees’ contracts of employment. This section applies regardless of whether or not there has been an agreement to the contrary. Firstly, employees that were employed by the company before business rescue proceedings commenced continue

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117 Companies Act 2008 s 148(1).
118 Companies Act 2008 s 148(2).
119 Companies Act 2008 s 149(1)(a).
120 Companies Act 2008 s 149(1)(b).
121 Companies Act 2008 s 149(1)(c).
122 Companies Act 2008 s 150(2)(c)(ii).
to be employed on the same terms and conditions unless these changes ‘occur in the ordinary course of attrition’ or the company and employees come to an agreement whereby the employees’ terms and conditions are changed. However, such agreement must be in accordance with South Africa’s labour law.\textsuperscript{123}

If the business rescue plan anticipates the retrenchment of employees, such retrenchments have to comply with the LRA, specifically s 189 and s 189A, and any other labour legislation that is applicable.\textsuperscript{124} According to Stein and Everingham, the inclusion of this section was not necessary as according to s 5(4)(b) of the Companies Act 2008, in the event of an unavoidable inconsistency between the LRA and the Companies Act 2008, the LRA prevails.\textsuperscript{125}

While the business rescue practitioner has the power to suspend or cancel (with the consent of the court) the whole or part of an agreement, such power does not extend to an employment agreement.\textsuperscript{126} According to Cassim et al, not even the court has the power to cancel employment contracts unless such cancellation complies with s 136(1), which was discussed above.\textsuperscript{127}

As can be seen from the above discussion, employees (in their individual capacity as such) are given extensive protection during business rescue proceedings. Many of these rights focus on promoting communication between the employer, the business rescue practitioner and the employees so that the employees are kept up to date on what is happening in the company and have the opportunity to voice their opinions about the proceedings. More powerful protection is afforded to employees when it comes to unpaid remuneration, their employment contracts and when retrenchments are contemplated.

\textit{(b) Rights as an Affected Person}

\textsuperscript{123} Companies Act 2008 s 136(1)(a).
\textsuperscript{124} Companies Act 2008 s 136(1)(b).
\textsuperscript{125} Stein & Everingham op cit note 4 at 422.
\textsuperscript{126} Cassim et al op cit note 2 at 886.
\textsuperscript{127} Ibid.
The definition of ‘affected person’ is wide and includes a number of stakeholders, including shareholders, creditors and employees, who are given a number of important rights during business rescue proceedings. What follows is a summary of the most important rights of affected persons, the purpose of which is to demonstrate the extent to which affected persons are entitled to be involved in the different steps of the business rescue process.

In terms of the rights of affected persons at the commencement of business rescue proceedings, if the board of directors passes a resolution to begin business rescue proceedings, affected persons are entitled to receive notice of the resolution and notice of the appointment of the business rescue practitioner. If the board of directors believe that the company is in financial distress but do not adopt a resolution to begin business rescue proceedings, affected persons must be given notification of the failure, along with the reasons for not adopting a s 129 resolution. If a s 129 resolution has been adopted, affected persons have the right to apply to court for an order setting aside the resolution or setting aside the appointment of the practitioner. An affected person can also ask for an order that requires the practitioner to provide security in order to protect the interests of both the company and affected persons. If any of these applications are made, all other affected persons are entitled to be notified of it and are entitled to participate in the hearing of the application.

Some of the most important rights affected persons have are in terms of s 131. As discussed earlier, affected persons have the right to apply to court for an order placing the company under business rescue. The affected person bringing the application may also nominate an interim practitioner. Every affected person is entitled to notification of a s 131 application and they have the right to participate in the hearing of the application. If an order in terms of s 131 is granted, the company

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128 Companies Act 2008 s 129(3)(a) and s 129(4)(b).
129 Companies Act 2008 s 129(7).
130 Companies Act 2008 s 130(1)(a) and (b).
131 Companies Act 2008 s 130(1)(c).
132 Companies Act 2008 s 130(3)(b) and s 130(4).
133 Companies Act 2008 s 131(1).
134 Companies Act 2008 s 131(5).
135 Companies Act 2008 s 131(2)(b) and s 131(3).
must give notice to each affected person. An important aspect of s 131 is that the court can grant the application if, along with the judge being satisfied that rescuing the company is a reasonable prospect, ‘the company has failed to pay over any amount in terms of an obligation under or in terms of a public regulation, or contract, with respect to employment-related matters’.136 According to Stein and Everingham,137 this section provides employees and their trade unions with a very strong right which could be useful in negotiations.138 If the company fails to pay an employee any amount, thereby breaching the employee’s contract of employment, the employee or trade union could bring a s 131 application despite that fact that the company is not in financial distress and regardless of the materiality of the amount that was not paid.139 This gives rise to a legitimate fear that the procedure could be abused by employees or trade unions.

Once the business rescue practitioner has investigated the affairs of the company in terms of s 141, the practitioner must inform all affected persons if he or she concludes that there are no reasonable prospects of rescuing the company or that there are no grounds for believing that the company is in financial distress.140

Before the practitioner prepares the business rescue plan he or she must consult affected persons in terms of s 150(1). The plan must contain enough information for affected persons to decide whether or not to accept the plan.141 Before the practitioner calls a meeting in which the proposed plan will be considered, he or she must notify all affected persons of the meeting and set out the rights that affected persons have to participate in and vote at the meeting.142 If the plan is rejected and the practitioner does not ask for a vote that he or she prepare a new plan or apply to court to set aside the results of the vote, then affected persons have three options. An affected person at the meeting may either ask the holders of voting interests to vote that the practitioner should prepare a new plan or apply to court for an order setting

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136 Companies Act 2008 s 131(4)(a).
137 Stein & Everingham op cit note 4.
138 Stein & Everingham op cit note 4 at 417.
139 Ibid.
140 Companies Act 2008 s 141(2)(a)(i) and (2)(b).
141 Companies Act 2008 s 150(2).
142 Companies Act 2008 s 151(2).
aside the vote due to the fact that it was inappropriate.\textsuperscript{143} The other option is that one or more affected persons can offer to buy the voting interests of persons who rejected the plan. The value of the offer must be the equivalent of the return that the person would receive if the company was liquidated.\textsuperscript{144}

The type of protection given to affected persons is similar to the protection given to employees individually in that many of the sections entitle affected persons to information, to notification of certain matters, to be involved and participate in certain procedures and to be consulted. While each of these rights may seem insignificant when looked at in isolation, a consolidated summary of the rights reveal that affected persons are given relatively extensive and important rights during business rescue. However, it must be remembered that the definition of ‘affected person’ is wide and includes a number of different people. Employees are therefore not the only group of people that are given these extensive rights.

IV EMPLOYEE PROTECTION OUTSIDE CHAPTER 6 OF THE COMPANIES ACT 2008

While chapter 6 of the Companies Act 2008 sets out the rights and protections afforded to employees and affected persons, these are not the only rights and protections that employees have during business rescue. More specifically, employees are also protected by the South African Constitution and the LRA.

\textit{(a) The Constitution of the Republic of South Africa 108 of 1996}

Section 23 of the South African Constitution lists a number of labour relations rights. One of the most important rights is that ‘everyone has the right to fair labour practices’.\textsuperscript{145} The section gives workers the right to ‘form and join a trade union’, to participate in the union’s activities and the right to strike.\textsuperscript{146} Employers, on the other hand, are given the right ‘to form and join an employers’ organisation’ and to

\begin{footnotesize}
\begin{itemize}
\item Companies Act 2008 s 153(1)(b)(i).
\item Companies Act 2008 s 153(1)(b)(ii).
\item South African Constitution s 23(1).
\item South African Constitution s 23(2).
\end{itemize}
\end{footnotesize}
participate in the organisation’s activities.\footnote{South African Constitution s 23(3).} Trade unions, employers’ organisations and employers are also given the right to participate in collective bargaining.\footnote{South African Constitution s 23(5).} These rights are given effect to by the LRA and the Basic Conditions of Employment Act 55 of 1998 (hereafter ‘the BCEA’).

Section 23 gives employees an advantage during business rescue as they are given direct constitutional protection while other groups, such as creditors and shareholders, only have indirect constitutional protection (through the equality clause in s 9 and the property rights enshrined in s 25).\footnote{Joubert, van Eck & Burdette op cit note 1 at 69.}

\textit{(b) The Labour Relations Act 66 of 1995}\footnote{Joubert, van Eck & Burdette op cit note 1 at 73.}

One of the purposes of the Companies Act 2008 is to ensure that South Africa’s company law observes the rights contained in the Bill of Rights,\footnote{Companies Act 2008 s 7(a).} which includes the right of employees to fair labour practices.\footnote{Joubert, van Eck & Burdette op cit note 1 at 73.} In recognition of this purpose, s 5(4)(b)(i)(bb) of the Companies Act 2008 states that if the provisions of the LRA and the Companies Act 2008 conflict and the provisions cannot be applied concurrently, the provisions of the LRA will prevail. This is also reflected in s 210 of the LRA. In addition to this, s 144(5) of the Companies Act 2008, which deals with the rights of employees during business rescue, states that any rights afforded to an employee in terms of that section are in addition to the rights that the employee is entitled to in terms of ‘any law, contract, collective agreement, shareholding, security or court order’. From these sections it is clear that in order to complete a full evaluation of the rights that employees have during business rescue it is important to set out the rights that they have in terms of the LRA.

The two most relevant sections of the LRA with regards to business rescue are s 189, dealing with dismissals based on operational requirements, and s 197, dealing with the transfer of a business or part of a business as a going concern. These two sections are relevant to business rescue because it is possible that a business rescue plan will
contemplate reducing the workforce to save money or selling part of the company to make money and place the focus on the core business.\textsuperscript{152}

As, under business rescue, the business rescue practitioner has the duty of managing the company in place of the board of directors and existing management,\textsuperscript{153} any obligation of the employer that is discussed in this dissertation will be in reference to an obligation of the company, under the management of the business rescue practitioner.

(i) Retrenchments

According to section 136(1)(b) of the Companies Act 2008, if the business rescue plan envisages that any employees will be retrenched, such retrenchments must comply with sections 189 and 189A of the LRA. The LRA places a number of obligations on the employer when he or she contemplates dismissing an employee or employees in order to ensure that the dismissals are fair. If the employer does not comply with these obligations there are consequences that could severely impact the employer’s business. It is therefore crucial, if retrenchments are contemplated in the business rescue plan, that these obligations are fully complied with.

The LRA states that employees have the right not to be unfairly dismissed,\textsuperscript{154} and that if an employee establishes that there was a dismissal, the employer bears the onus of proving that the dismissal was fair.\textsuperscript{155} One of the ways that an employer can do this is by proving that the reason for dismissal was a fair reason based on the operational requirements of the employer.\textsuperscript{156} According to the s 213 definitions section, ‘operational requirements’ means requirements based on the economic, technological, structural or similar needs of an employer’. These terms are elaborated on in the Code of Good Practice on Dismissals Based on Operational

\begin{footnotes}
\item[153] Companies Act 2008 s 140(1)(a).
\item[154] LRA s 185(a).
\item[155] LRA s 192.
\item[156] LRA s 188(1)(a)(ii).
\end{footnotes}
Requirements,\textsuperscript{157} which states that economic reasons are those relating to the financial management of the business, technological reasons are those relating to new technology being introduced which affects the work relationship and structural reasons are those relating to posts becoming redundant after the employer restructures.\textsuperscript{158} In terms of business rescue the employer will most likely argue that the dismissal was based on their economic needs. When dismissals based on operational requirements are discussed the reference is almost always to retrenchments,\textsuperscript{159} therefore I will use the terms interchangeably.

These types of dismissals have been called ‘no fault’ dismissals due to the fact that an employee can be retrenched despite the fact that they have technically not done anything wrong.\textsuperscript{160} For this reason employers are given specific procedural and substantive obligations to ensure that the employees are treated fairly and to ensure that employers consider all alternative options before retrenching any employees.\textsuperscript{161}

Sections 189 and 189A of the LRA deal specifically with dismissals based on operational requirements. The two sections differ in significant respects. Section 189 deals with small-scale retrenchments and section 189A deals with large-scale retrenchments.\textsuperscript{162} More specifically, s 189A applies when an employer who employs more than fifth employees contemplates retrenching a relatively large number of those employees.\textsuperscript{163} If the employer does not fall within s 189A then they must use s 189. The requirements for a procedurally fair retrenchment in terms of each section will be discussed below, followed by a discussion of the requirements for a substantively fair retrenchment.

\textsuperscript{157} Code of Good Practice: Dismissals Based on Operational Requirements GN 1517 Government Gazette No 20254 of 16 July 1999 (hereafter ‘Code of Good Practice’).
\textsuperscript{158} Ibid reg 1.
\textsuperscript{159} Andre van Niekerk Unfair Dismissal 4 ed (2008) at 85.
\textsuperscript{160} Code of Good Practice op cit note 157 reg 2.
\textsuperscript{161} Ibid.
\textsuperscript{162} Van Niekerk op cit note 159 at 84.
\textsuperscript{163} Section 189A applies if, in terms of s 189A(1)(a), an employer who employs more than fifty employees contemplates retrenching at least; 10 employees if up to 200 employees are employed, 20 employees if the employer employs more than 200 but not over 300 employees, 30 employees if the employer employs more than 300 but not over 400 employees, 40 employees if the employer employs more than 400 but not over 500 employees or 50 employees if the employer employs more than 500 employees. Section 189A also applies if, in terms of s 189A(1)(b), the number of employees that the employer contemplates retrenching, together with the number of employees retrenched in the 12 months preceding the date on which the employer issued a s 189(3) notice, is the same as or is greater than the relevant number mentioned above.
Procedural fairness for small-scale retrenchments (s 189)

Section 189 requires an extensive consultation process which forms the basis the procedural fairness of the dismissal. In order to determine who the employer must consult with, the section establishes a hierarchy setting out which parties must be consulted when retrenchment is contemplated. Due to this hierarchy the employer is only required to consult with the party with the primary claim. For example, employers do not need to consult with individual employees if the employees are represented by a trade union.

In terms of s 189(3) of the LRA the employer must give written notice to the other consulting parties inviting them to consult with him or her and is further required to disclose certain information in writing, including the reasons for the contemplated retrenchments, the alternatives that were considered and the reason for their rejection, the suggested selection criteria and the number of employees that are likely to be affected. There are a number of other required disclosures listed in the section, however it is not a closed list.

The parties involved in the consultation process are required to ‘engage in a meaningful joint consensus-seeking process’. According to the Labour Court decision of Van Rooyen v Blue Financial Services (SA) (Pty) Ltd this means that ‘both parties are required, in good faith, to seek consensus. This is not a mechanical process – meaningful joint decision-making requires that the parties act with the honest intention of exploring the prospects of agreement’.

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165 In terms of s 189(1) of the LRA, if there is a collective agreement requiring the employer to consult with any person or persons, the employer must consult with that person or persons. If there is no collective agreement requiring such consultation and the workplace of the affected employees is covered by a workplace forum, then the employer must consult with the workplace forum, as well as any trade union whose members are expected to be affected by the retrenchments. If there is no workplace forum then the employer must consult with the trade union or, if there is no such trade union, with the employees likely to be affected or their representatives.
166 Van Niekerk op cit note 159 at 94.
167 Du Toit et al op cit note 164 at 435.
168 LRA s 189(3).
170 LRA s 189(2).
In order to do this the parties must try to reach consensus on ways to avoid dismissals, ways to minimise the number of dismissals, measures to change the timing of the retrenchments and ways to alleviate the negative effects of the retrenchments.\textsuperscript{173} The consulting parties must also try to agree on severance pay and the selection criteria that will be used to determine which employees will be dismissed.\textsuperscript{174} During the consultation the employer must give the other party an opportunity to make representations about matters relating to the contemplated retrenchments and must respond to such representations, providing reasons if they disagree with any of the representations.\textsuperscript{175}

\textit{Procedural fairness for large-scale retrenchments (s 189A)}

The main differences between s 189 and s 189A is that if s 189A applies, a facilitator can be appointed to help in the consultation process and, in certain circumstances, employees may strike and employers may lock out.

As with the s 189 process, consultation is initiated by the employer issuing a written notice to the other party, inviting them to consult with the employer.\textsuperscript{176} The employer is also required to disclose all relevant information as specified in s 189(3). In the s 189(3) notice the employer can request that the Commission for Conciliation, Mediation and Arbitration (hereafter ‘the CCMA’) appoint a facilitator to assist in the consultation process.\textsuperscript{177} If an employer makes such a request the CCMA must appoint a facilitator. A facilitator must also be appointed if the consulting parties representing the majority of the affected employees request such appointment\textsuperscript{178} or if the parties agree to appoint a facilitator.\textsuperscript{179}

\textsuperscript{172} Van Rooyen supra note 173 para 19.
\textsuperscript{173} LRA s 189(2)(a).
\textsuperscript{174} LRA s 189(2)(b) and (c).
\textsuperscript{175} LRA s 189(5) and 189(6)(a).
\textsuperscript{176} Van Niekerk op cit note 159 at 97.
\textsuperscript{177} LRA s 189A(3)(a).
\textsuperscript{178} LRA s 189A(3)(b).
\textsuperscript{179} LRA s 189A(4).
If the CCMA appoints a facilitator the process is suspended for 60 days, during which the parties must engage in the consultation process and may take no further legal action.\textsuperscript{180} Once the 60 days have elapsed the employer is entitled to give notice that the employees’ contracts will be terminated.\textsuperscript{181} In terms of the affected employees, once the time period has elapsed they, or a trade union, may give notice that they are going to strike, or they may refer the dispute to the Labour Court for it to determine whether the reason for the dismissal was fair.\textsuperscript{182} If no facilitator is appointed the parties may not refer the dispute to the CCMA or a bargaining council until 30 days has passed since the s 189(3) notice was given.\textsuperscript{183} Once the dispute has been referred to the CCMA or bargaining council and either a certificate has been issued stating that the dispute remains unresolved or 30 days has passed since the referral, the employer is entitled to give notice that he will terminate the employment contracts and the affected employees or trade union may give notice that they will strike or refer the dispute to the Labour Court.\textsuperscript{184}

If the employer does not follow a procedure that is fair, the other consulting party must make an application to the Labour Court in terms of s 189A(13) for an order forcing the employer to follow a fair procedure, stopping the employer from retrenching the employees before following a fair procedure, ordering reinstatement until a fair procedure is complied with or ordering compensation if the other orders are inappropriate.\textsuperscript{185} Du Toit et al\textsuperscript{186} presume that this rule was formulated to create a quick and simple way to resolve procedural unfairness disputes.\textsuperscript{187}

\textit{Substantive fairness}

While the consultation process mainly relates to the procedural fairness of the dismissal, employers must also make sure that the dismissals are substantively fair. The fairness of both the reason for the retrenchments and the selection criteria used

\textsuperscript{180} Van Niekerk op cit note 159 at 98.
\textsuperscript{181} LRA s 189A(7)(a).
\textsuperscript{182} LRA s 189A(7)(b).
\textsuperscript{183} LRA s 189(8)(a).
\textsuperscript{184} LRA s 189(8)(b).
\textsuperscript{185} LRA s 189A(13).
\textsuperscript{186} Du Toit et al op cit note 164.
\textsuperscript{187} Ibid at 446.
must be assessed. The Labour Appeal Court in *BMD Knitting Mills (Pty) Ltd v SA Clothing & Textile Workers Union*\(^{188}\) suggested that the test for a substantively fair reason for dismissal should be as follows:

‘The starting point is whether there is a commercial rationale for the decision. But, rather than take such justification at face value, a court is entitled to examine whether the particular decision has been taken in a manner which is also fair to the affected party, namely the employees to be retrenched. To this extent the court is entitled to enquire as to whether a reasonable basis exists on which the decision, including the proposed manner, to dismiss for operational requirements is predicated. Viewed accordingly, the test becomes less deferential and the court is entitled to examine the content of the reasons given by the employer, albeit that the enquiry is not directed to whether the reason offered is the one which would have been chosen by the court. Fairness, not correctness is the mandated test.’\(^{189}\)

In the more recent decision of *CWIU & Others v Algorax (Pty) Ltd*\(^{190}\) the Labour Appeal Court expanded this test by expressing the view that employers have an obligation to only retrench employees if it is a ‘measure of last resort’.\(^{191}\)

In the context of business rescue where the company in question is in financial distress it is likely that this test will be easy to satisfy. The employer would have to show that there was a commercial rationale for the dismissals (i.e. that they had a bona fide economic need for the dismissals), that the dismissals were fair and that the alternatives to retrenchment had been considered but were not viable options.

According to s 189A(19), if there are large scale retrenchments the Labour Court must find that the dismissals were substantively fair if the reasons were based on the economic, technological, structural or similar needs of the employer, the retrenchments were ‘operationally justifiable on rational grounds’, the employer considered alternatives to retrenchment, and the criteria used to select employees were fair and objective.\(^{192}\) Du Toit *et al* argue that s 189A(19) does not add anything to the principles established by the case law and hold the view that clarification on the issue of substantive fairness should be sought from the established

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\(^{188}\) (2001) 22 *ILJ* 2264 (LAC).

\(^{189}\) *BMD Knitting Mills* supra note 188 para 19.

\(^{190}\) (2003) 24 *ILJ* 1917 (LAC).

\(^{191}\) *CWIU* supra note 190 para 70.

\(^{192}\) LRA s 189A(19).
jurisprudence.\textsuperscript{193} It is important to note that, according to the wording of the section, this rule only applies to retrenchments in terms of s 189A (large-scale retrenchments).\textsuperscript{194} However, Van Niekerk \textit{et al} argue that ‘the development of different tests would be undesirable and there seems to be no reason why a uniform approach should not be adopted’.\textsuperscript{195} Du Toit \textit{et al} also suggest that courts will apply the rule as a general standard to all dismissals based on operational requirements,\textsuperscript{196} and add that applying different criteria of fairness to employees could potentially infringe their right to equality as expressed in the South African Constitution.\textsuperscript{197}

If the Labour Court finds that a dismissal was unfair they may reinstate the employee, re-employ the employee or, in certain circumstances, they may make an order that the employee be compensated by the employer.\textsuperscript{198}

If an employee or employees are retrenched, even when the retrenchment is fair, the employer is obligated to pay the retrenched employees severance pay which must amount to ‘at least one week’s remuneration for each completed year of continuous service with that employer’.\textsuperscript{199} However, if the employer offers the employee alternative employment, whether it is with that employer or another, and the employee unreasonably refuses that offer, then the employee is not entitled to severance pay.\textsuperscript{200}

As the above discussion reveals, employees are given extensive protection when retrenchments are contemplated. If the requirements of s 189 and s 189A are not complied with the financial consequences could have a devastating effect on an already weak and vulnerable company.\textsuperscript{201}

(ii) Transfer of a business

\textsuperscript{193} Du Toit \textit{et al} op cit note 164 at 424.
\textsuperscript{194} Ibid at 445.
\textsuperscript{195} Van Niekerk \textit{et al} \textit{Law@work} 2ed (2012) at 304.
\textsuperscript{196} Du Toit \textit{et al} op cit note 164 at 424.
\textsuperscript{197} Ibid at 445.
\textsuperscript{198} LRA s 193(2).
\textsuperscript{199} BCEA s 41(2).
\textsuperscript{200} BCEA s 41(4).
\textsuperscript{201} Loubser op cit note 27 at 67.
It is possible that a business rescue plan will involve selling part of the business or a service that the business offers in order to gain capital or direct the focus of business rescue on the core business. It is also possible that the company will be sold as a going concern once business rescue attempts end, as stated by Stein and Everingham:

‘Business rescue is not restricted to nursing a company back to solvency. It is also a system to temporarily protect a company against the claims of creditors so that its business can be restructured and thereafter be sold for maximum value as a going concern, thus giving creditors and shareholders a better return.’

Sections 197 and 197A of the LRA regulate the consequences of a transfer of a business as a going concern. These sections have a dual purpose in that they aim to protect employees’ security of employment and to facilitate the sale of the business. The provisions have serious consequences in terms of both employee protection and the obligations that are imposed on the buyer of the business. It is therefore necessary to set out when the sections will apply and what the consequences of such a transfer will be.

In terms of which section to use when dealing with business rescue, s 197 applies to the transfer of a solvent business and s 197A applies to the transfer of an insolvent business or ‘if a scheme of arrangement or compromise is being entered into to avoid winding up or sequestration for reasons of insolvency’. According to Loubser, in order for a company to qualify as insolvent for the purposes of s 197A(1) they must at least be under provisional liquidation, i.e. they must be legally insolvent as opposed to commercially insolvent. Therefore, in the context of business rescue it seems as though one would have to apply s 197, as there is no mention of business rescue in s 197A(1).

Application of s 197

202 Stein & Everingham op cit note 4 at 25.
204 LRA s 197A(1).
205 Loubser op cit note 27 at 68.
According to the Constitutional Court in *Aviation Union of SA & Another v SA Airways (Pty) Ltd & Others*, 206 whether s 197 applies to the sale of a business does not depend on the type of transaction effected, but on whether three requirements are met: that the entity being transferred is a business, that there is a relevant transfer, and that the business is transferred as a going concern. 207

In terms of whether the entity can be considered a ‘business’, s 197(1) states that the term refers to the ‘whole or part of any business, trade, undertaking or service’. However, when deciding whether a service constitutes a business for the purposes of s 197, the Constitutional Court in *Aviation Union* 208 stressed it must be the business that supplies the service that is transferred, as opposed to the service itself. 209 Section 197(1) further states that the word ‘transfer’ refers to ‘the transfer of a business by one employer to another employer as a going concern’. The Constitutional Court elaborated on this by saying that the business ‘must have changed hands’. 210 The phrase ‘as a going concern’ is not defined in s 197, however, the Constitutional Court in *NEHAWU v University of Cape Town & Others* 211 shed some light on its meaning. The court stated:

‘In deciding whether a business has been transferred as a going concern, regard must be had to the substance and not the form of the transaction. A number of factors will be relevant to the question whether a transfer of a business as a going concern has occurred, such as the transfer or otherwise of assets both tangible and intangible, whether or not workers are taken over by the new employer, whether customers are transferred and whether or not the same business is being carried on by the new employer. What must be stressed is that this list of factors is not exhaustive and that none of them is decisive individually’. 212

Taking these definitions into consideration, s 197(2) states that when a business is transferred the following consequences follow, unless there has been an agreement in terms of s 197(6):

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206 (2011) 32 ILJ 2861 (CC).
207 Ibid para 44.
208 Ibid.
209 Ibid para 52.
210 Ibid para 46.
211 NEHAWU supra note 203.
212 Ibid para 56.
36

‘(a) the new employer is automatically substituted in the place of the old employer in respect of all contracts of employment in existence immediately before the date of transfer;

(b) all the rights and obligations between the old employer and an employee at the time of the transfer continue in force as if they had been rights and obligations between the new employer and the employee;

(c) anything done before the transfer by or in relation to the old employer, including the dismissal of an employee or the commission of an unfair labour practice or act of unfair discrimination, is considered to have been done by or in relation to the new employer; and

(d) the transfer does not interrupt an employee’s continuity of employment, and an employee’s contract of employment continues with the new employer as if with the old employer.’

In essence, therefore, the new employer steps into the shoes of the old employer, leaving the employment contract and terms and conditions of employment unaffected by the transfer. These consequences apply automatically by operation of law unless there is an agreement that complies with s 197(6). Section 197(6) states that if different consequences are agreed to, such agreement must be a written agreement concluded by the new employer, the old employer and the consulting party established by the hierarchy set out in s 189(1) (as discussed in the previous section).

Obligations of the new employer

Despite the fact that the new employer replaces the old employer in terms of the contract of employment, s 197(3) states that the new employer can change the employees’ terms and conditions of employment on transfer as long as the new terms and conditions as a whole are ‘not less favourable’ to the employees than the old terms and conditions. The exception to this is that the terms and conditions cannot be changed if there is a collective agreement which determines the employees’ conditions of employment.

It is also important to note that, unless there is an agreement that complies with s 197(6), the new employer will be bound by arbitration awards and collective

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213 LRA s 197(2).
214 Van Niekerk et al op cit note 195 at 326.
215 Ibid at 328.
agreements that the old employer is bound by immediately before the transfer takes place.\textsuperscript{216}

The LRA holds the old and new employer jointly and severally liable in certain circumstances, for example, for claims that arose before the transfer which concern terms or conditions of employment.\textsuperscript{217} Unless the old employer can show that he or she complied with s 197, the old and new employer will also be held jointly and severally liable for one year after the transfer in respect of certain claims by employees where the employees are retrenched or where the employer is liquidated or sequestrated.\textsuperscript{218} These ‘certain claims’ are claims for accrued leave pay, severance pay and other accrued payments which have not been paid to the employees.\textsuperscript{219}

\textit{Consequences of not complying with s 197}

In terms of the remedies available to employees where an employer has breached s 197, one has to look at the meaning of a dismissal. In terms of s 186(1)(f) if, after a s 197 or 197A transfer, an employee terminates their employment contract due to the fact that the new employer provided the employee with conditions or circumstances which were less favourable than the conditions or circumstances provided by the old employer, such termination is regarded as a dismissal. Unless the employer can prove that the dismissal was fair, the Court may order the employer to reinstate the employee, re-employ the employee or pay the employee compensation that is just and equitable, but not more than 12 months’ remuneration.\textsuperscript{220}

Section 187(1)(g) states that a dismissal will be regarded as automatically unfair if it is established that the reason for the dismissal is a transfer contemplated in s 197 or 197A, or a reason relating to such transfer. In terms of remedies, if it is established that the dismissal is automatically unfair as opposed to just unfair, the amount of compensation that the Court can award increases to 24 months’ remuneration.\textsuperscript{221}

\textsuperscript{216} LRA s 197(5).
\textsuperscript{217} LRA s 197(9).
\textsuperscript{218} LRA s 197(8).
\textsuperscript{219} LRA s 197(7)(a).
\textsuperscript{220} LRA s 192(2), s 193(1) and s 194(1).
\textsuperscript{221} LRA s 194(3).
Effect of using s 197 instead of s 197A for companies under business rescue

Section 197A, which deals with insolvent employers, is similar to s 197 in that the employees’ contracts of employment are transferred to the new employer when the business is transferred and their continuity of employment is not interrupted by the transfer. However, the consequences of the sections differ in two significant respects. Firstly, the rights and obligations that exist between the employees and the old employer at the time of the transfer remain between those parties. This means that the rights and obligations of the old employer are not transferred to the new employer.222 Secondly, the old employer remains responsible for anything it did before the transfer, for example, dismissals, unfair labour practices and unfair discrimination.223

From the above it is clear that the consequences that apply when using s 197 are far more severe than when using s 197A. Most importantly, this would mean that potential buyers would not be responsible for things that the financially distressed company did before the transfer and the existing rights and responsibilities between the employees and the old employer will not be transferred to them. When referring to the differences between s 197 and s 197A, Loubser argues that the additional consequences that flow from s 197 make the business far less appealing to potential buyers, particularly when the potential buyer knows that the business has faced financial difficulties and could have engaged in a number of unfair labour practices in an effort to revive itself.224 For that reason, Loubser argues that it would be preferable to use s 197A instead of s 197 when dealing with companies that are being ‘rescued’.225 While Loubser was referring to companies under judicial management, the same argument can be applied to companies under business rescue. This change would make the sale of the business or part of it more attractive to potential buyers and, as a result of the transfer, the business could gain capital that could help business rescue proceedings succeed.

222 LRA s 197A(2)(b).
223 LRA s 197A(2)(c).
224 Loubser op cit note 27 at 68.
225 Ibid.
In terms of the negative aspects of using s 197A for companies under business rescue, this would mean that the old employer, i.e. the company under business rescue, would retain certain obligations and responsibilities. This could negatively impact business rescue attempts depending on, for example, whether the company committed any unfair labour practices or unfairly dismissed any employees before the transfer. Applying s 197A to companies under business rescue could therefore be positive or negative depending on the facts of the case at hand. However, as a general rule I agree with Loubser, that companies in financial distress should be subject to s 197A, as the benefits derived from selling part of the business will likely outweigh the negative consequences of using the section.

The above discussion serves to illustrate the generous protection afforded to employees when a business is sold as a going concern and sets out the responsibilities and obligations that potential buyers will gain if they purchase a business that is subject to s 197 or 197A. It is clear that the liabilities and obligations that are imposed on buyers in terms of 197 as opposed to s 197A are far more severe and can make a business less appealing to potential buyers.

V COMPARATIVE PERSPECTIVE

In the preceding chapter the rights and protections afforded to employees during business rescue proceedings in South Africa were set out. However, in order to assess whether the South African corporate rescue regime over-protects employees, it is necessary to compare the South African provisions with the corporate rescue provisions in other jurisdictions. According to Kloppers, comparing South Africa’s regime with that of Australia and England is logical for a number of reasons.²²⁶ Firstly, in both Australia and England there were inquiries into their insolvency regimes in the 1980’s which ultimately led to new corporate rescue mechanisms in both countries.²²⁷ Secondly, South Africa, England and Australia all share Commonwealth heritage.²²⁸ Additionally, the comparison with England is logical due

²²⁶ Kloppers op cit note 29 at 419.
²²⁷ Ibid at 420.
²²⁸ Ibid.
to the influence that English law has had on South Africa’s company law.\textsuperscript{229} On the other hand, the comparison with Australia is important because their previous corporate rescue regime, official management, was largely based on South Africa’s judicial management regime.\textsuperscript{230} Comparison with Australia is also logical due to the commonality between South Africa and Australia’s company law.\textsuperscript{231} Kloppers was using this comparison in order to assess whether South Africa’s judicial management regime needed to be reformed. However, his reasons for comparing South Africa with England and Australia are still applicable, despite the fact that South Africa’s corporate rescue mechanism has since changed. Due to these reasons, this dissertation compares the protection and rights of employees in South Africa to the protection afforded in the jurisdictions of both Australia and the United Kingdom.

Currently both Australia and the United Kingdom have corporate rescue regimes called ‘administration’. Although these procedures share the same name it must be noted that they are different procedures.

In the United Kingdom the administration procedure is contained in the UK Insolvency Act 1986 (c.45) (hereafter ‘the UK Insolvency Act’). Initially the procedure was governed by the provisions of Part II of the Act, however this was changed when the Enterprise Act 2002 (c.40) (hereafter ‘the Enterprise Act’) came into force in 2003.\textsuperscript{232} The Enterprise Act introduced Schedule B1 to the UK Insolvency Act which, for most companies, replaced the administration provisions contained in Part II of the UK Insolvency Act.\textsuperscript{233} While Schedule B1 has replaced Part II for the majority of company administrations, Part II still applies to limited types of companies.\textsuperscript{234} Due to the limited application of Part II, this dissertation will focus on the administration provisions contained in Schedule B1 of the UK Insolvency Act.

\textsuperscript{229} Ibid.
\textsuperscript{230} Ibid.
\textsuperscript{232} Nicholas Bourne \textit{Bourne on Company Law} 5ed (2011) at 308.
\textsuperscript{233} Andrew Keay & Peter Walton \textit{Insolvency Law: Corporate and Personal} 2ed (2008) at 90.
\textsuperscript{234} Ibid at 91. For example, Part II still applies to water companies, air traffic controlling companies and building societies.
Australia’s previous corporate rescue regime, official management, was enacted in 1961 and was for the most part based on the judicial management regime in South Africa.\(^{235}\) However, in 1993 this regime was repealed by the Corporate Law Reform Act\(^{236}\) due to the general consensus that it was an unsuccessful corporate rescue regime\(^{237}\) and was rarely used in practice.\(^{238}\) Official management was replaced with administration, the provisions of which are found in Part 5.3A of the Corporations Act No. 50 of 2001 (Cth) (hereafter ‘the Corporations Act’) which is Australia’s company law statute.\(^{239}\)

An important thing to note about administration in Australia and the United Kingdom and business rescue in South Africa is that the aims of these procedures are very similar. In all three jurisdictions the primary objective is to rescue the company, but if that is not possible the secondary objective is to get a better return for creditors than they would have received from immediate liquidation.\(^{240}\) The United Kingdom, however, has a third aim which is ‘realising property in order to make a distribution to one or more secured or preferential creditors’.\(^{241}\) As the United Kingdom lists the purposes in a hierarchy,\(^{242}\) this third aim can only be pursued if achieving the first two objectives is not reasonably practicable and only if the interests of the creditors are not unreasonably harmed.\(^{243}\)

The protection and rights afforded to employees during administration in the United Kingdom and Australia will be discussed below under four headings. Firstly, the role that employees play in the commencement of corporate rescue proceedings. Secondly, the order in which employment claims are paid when administration ends or when assets are realised and their proceeds distributed. Thirdly, whether employees are entitled to any notice of proceedings and whether they are allowed to participate in those proceedings in any way. Lastly, the rights that the employees have in terms of any applicable labour law will be discussed.

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\(^{235}\) Rajak & Henning op cit note 28 at 263 and Anderson op cit note 231 at 107.
\(^{236}\) 1992 (Cth).
\(^{237}\) Rajak & Henning op cit note 28 at 263.
\(^{238}\) Anderson op cit note 231 at 107.
\(^{239}\) Ibid at 104.
\(^{240}\) Companies Act 2008 s 128(1)(b); Corporations Act s 435A; UK Insolvency Act Sch B1 para 3(1).
\(^{241}\) UK Insolvency Act Sch B1 para 3(1)(c).
\(^{243}\) UK Insolvency Act Sch B1 para 3(4).
(a) Commencing the Proceedings

In terms of the procedure in both Australia and the United Kingdom, administration begins when an administrator is appointed. However, the parties that can appoint an administrator differ between the two jurisdictions.

In the United Kingdom there are three ways in which an administrator can be appointed. Firstly, the court may appoint an administrator by making an administration order. Such an order can only be made if the court is satisfied that the company is unable to pay its debts or will likely become unable to pay them and only if the court is satisfied that the purposes of administration are likely to be achieved by the order. In terms of paragraph 12, there are four parties that can bring such an application to court. These parties are the company, the directors, one or more of the company’s creditors or the justices’ chief executive of a magistrates’ court when exercising his or her power under s 87A of the Magistrates’ Courts Act 1980 (c. 43). In addition to this, an administration application can be made by the company’s liquidator, the supervisor of a voluntary arrangement and the Financial Services Authority.

The second way that an administrator can be appointed in the United Kingdom is when the holder of a qualifying floating charge appoints one under paragraph 14 of Schedule B1. The floating charge in question will be ‘qualifying’ if either on its own or together with other securities it relates to the whole or substantially the

244 Corporations Act s 435C(1)(a) and UK Insolvency Act Sch B1 para 1(b).
245 UK Insolvency Act Sch B1 para 10.
246 UK Insolvency Act Sch B1 para 11.
247 UK Insolvency Act Sch B1 para 12.
248 UK Insolvency Act Sch B1 para 38.
249 UK Insolvency Act s 7(4)(b) and UK Insolvency Act Sch B1 para 12(5).
250 Section 359 of the Financial Services and Markets Act 2000 (c. 8).
251 In the case of Re Yorkshire Woolcombers Association Ltd [1903] 2 Ch 284 at 295, Lord Justice Romer identified the characteristics of a floating charge as such: ‘(1.) If it is a charge on a class of assets of a company present and future; (2.) if that class is one which, in the ordinary course of the business of the company, would be changing from time to time; and (3.) if you find that by the charge it is contemplated that, until some future step is taken by or on behalf of those interested in the charge, the company may carry on its business in the ordinary way as far as concerns the particular class of assets I am dealing with.’
252 UK Insolvency Act Sch B1 para 14(1).
whole of the company’s undertaking’. In addition, the instrument that created the charge must state that paragraph 14 applies, must purport to give the holder of the charge the authority to appoint an administrator or must purport to give the holder of the charge the authority to appoint an administrative receiver. An appointment of an administrator by the holder of a qualifying floating charge may only be made if the floating charge is enforceable. For this type of appointment the appointer is not required to apply to court. However, he or she is required to file a notice of appointment with the court.

The third and last way that an administrator can be appointed in the United Kingdom is when one is appointed by the directors or by the company (in a general meeting by ordinary resolution of the company members or an equivalent) under paragraph 22 of Schedule B1. As with the appointment under paragraph 14, this type of appointment does not require an application to court. The appointer is, however, required to file a copy of the notice of intention to appoint and a notice of appointment with the court.

In Australia there are also three parties that may appoint an administrator. Firstly, the company can appoint an administrator by resolution of the board of directors if, in the opinion of the board, the company is insolvent or will likely become insolvent in the future. This is the most common way an administrator is appointed and is beneficial in that it allows directors to act quickly without having to refer to members or creditors. Secondly, an administrator can be appointed by a liquidator or provisional liquidator if he or she is of the opinion that the company is insolvent or will likely become insolvent in the future. Lastly, a chargee can appoint an

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253 Keay & Walton op cit note 233 at 102 and UK Insolvency Act Sch B1 para 14(3).
254 UK Insolvency Act Sch B1 para 14(2).
255 UK Insolvency Act Sch B1 para 16.
256 UK Insolvency Act Sch B1 para 18(1).
257 In terms of the UK Insolvency Act Sch B1 para 105 the term ‘directors’ includes a reference to a majority of the directors.
258 Keay & Walton op cit note 233 at 104.
259 UK Insolvency Act Sch B1 para 21.
260 UK Insolvency Act Sch B1 para 27(1).
261 UK Insolvency Act Sch B1 para 29(1).
262 Corporations Act s 436A.
263 Anderson op cit note 231 at 112.
265 Corporations Act s 436B.
administrator. Section 436C of the Corporations Act describes a chargee as ‘a person who is entitled to enforce a charge on the whole, or substantially the whole, of a company’s property’. Such a secured creditor may only appoint an administrator if the charge is enforceable. As these are the only parties allowed to appoint an administrator, courts, employees, shareholders and ordinary creditors have no power to commence administration proceedings.

As can be seen from the above discussion, South Africa is the only country out of the three jurisdictions discussed that specifically allows employees to commence business rescue/administration proceedings. This gives South African employees significant power as they can impact what happens to a company that is in financial difficulty.

(b) Priority of Employment Claims

The United Kingdom

In the United Kingdom, the priority in which employment claims will be paid is dealt with in paragraph 99 of Schedule B1, which applies when an administrator’s appointment ends due to resignation, death, removal from office or because the administrator’s appointment no longer has effect. The paragraph states that the expenses and the remuneration of the administrator will be paid out of the property which he or she controlled and had custody over prior to his or her vacation of office and that such claims will be paid in priority to floating charges. In terms of employee claims, paragraph 99(4) and (5) read together state that claims arising from contracts of employment which the administrator adopted before his or her vacation of office shall be paid out of the property which he or she controlled and had custody over prior to his or her vacation of office and that such claims will be paid in priority to the administrator’s expenses and remuneration. Therefore these employee claims rank ahead of floating charges and the administrator’s expenses and remuneration, but behind secured creditors. However, it must be noted that the employee claims...

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266 Corporations Act s 436C.
267 Corporations Act s 436C(1).
268 UK Insolvency Act Sch B1 para 99(1).
269 UK Insolvency Act Sch B1 para 99(3) and para 70.
that are given this ‘super priority’ status in terms of paragraph 99 are limited to the payment of ‘wages or salary’. For these purposes ‘wages or salary’ includes:

(a) a sum payable in respect of a period of holiday (for which purpose the sum shall be treated as relating to the period by reference to which the entitlement to holiday accrued),
(b) a sum payable in respect of a period of absence through illness or other good cause,
(c) a sum payable in lieu of holiday,
(d) in respect of a period, a sum which would be treated as earnings for that period for the purposes of an enactment about social security, and
(e) a contribution to an occupational pension scheme.

As evidenced by the case law on what constitutes ‘wages and salary’, the courts have taken a restrictive interpretation on what employee entitlements fall under paragraph 99. In the case of Re Allders Department Stores the court had to decide whether liabilities arising from redundancy and unfair dismissal are also given priority in terms of paragraph 99. It was concluded that these payments were not ‘wages or salary’ for the purposes of paragraph 99, therefore they are not prioritised. A restrictive approach was also adopted in Re Huddersfield Fine Worsteds Ltd, where the court decided that liabilities for protective awards and, in most cases, payments in lieu of notice do not fall within the scope of paragraph 99. Parry argues that the decisions in these cases indicate that courts prefer the interests of administration over the entitlements of employees.

In terms of employee claims for work done before administration began, employees are regarded as preferred creditors. While these claims do not enjoy ‘super priority’ status, it is important to note that in the United Kingdom unpaid employees can claim from the National Insurance Fund. When an employee makes a

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271 Para 99(6) of Sch B1 of the UK Insolvency Act.
272 Ibid.
274 [2005] EWHC 172 (Ch).
275 Ibid para 21.
276 Re Huddersfield Fine Worsteds Ltd supra note 270.
277 Ibid paras 47 and 52.
278 Parry op cit note 273 at 32.
279 Keay & Walton op cit note 233 at 133.
280 Employment Rights Act s 182-190.
successful claim against the Fund, the Fund steps into the shoes of the employee and has a claim against the company in administration.  

In the United Kingdom, employee claims are also high on the order of priority when a company is liquidated. After secured creditors and the expenses of winding up have been paid, preferential debts are paid. In terms of s 386 read with Schedule 6 of the UK Insolvency Act, certain employee claims such as unpaid remuneration and accrued holiday pay are regarded as preferential debts. As such, these debts are paid in priority to unsecured creditors and, in certain circumstances, holders of floating charges. Employees are given this priority due to their weak bargaining position and the fact that their salary is likely to be their only income.

**Australia**

As discussed above, administration in Australia commences when an administrator is appointed by either the company, a liquidator or a chargee. Once the administrator is appointed he or she must convene a meeting of creditors about 20 days after his or her appointment, at which the creditors will determine the future of the company. If the creditors decide that the company must execute a deed of company arrangement, voluntary administration will end. The company ceases to be under administration and is instead under a deed of company arrangement. In this regard an administration has two phases. The first stage is in terms of a statute and the second is in terms of a contract (the deed of company arrangement).

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282 UK Insolvency Act s 175. Also see Keay & Walton op cit note 233 at 460.
283 For the four months prior to the relevant date, subject to a prescribed limit. See UK Insolvency Act Sch B1 para 9.
284 UK Insolvency Act Sch B1 para 10.
285 Keay & Walton op cit note 233 at 446.
286 Ibid at 469.
287 Corporations Act s 436A-C.
288 Corporations Act s 439A.
289 A deed of company arrangement is ‘the contract that governs the dealings of the company once the voluntary administration comes to an end’. Tony Ciro & Christopher Symes *Corporations Law in Principle* 8ed (2009) at 602.
289A Corporations Act s 435C(1) and s 435C(2).
290 Austin & Ramsay op cit note 264 at 1673.
291 Ciro & Symes op cit note 289 at 539.
The administrator is required to set out the terms of the deed, specifying the order in which creditors are to be paid when assets of the company are realised and their proceeds distributed. The deed can treat different creditors or different categories of creditors differently, but if the order is materially different from that which applies when a company is wound up it is more likely to be challenged by creditors in court. In this regard, important amendments were made to the Corporations Act in 2007 by the Corporations Amendment (Insolvency) Act. These amendments increased the amount of protection employees have in terms of their entitlements by making it mandatory for a company’s deed to include a provision that the order of priority for employee creditors will be at least equal to the order of priority they would be entitled to if the company was being wound up. However, this provision does not need to be included if the eligible employee creditors, at a meeting convened by the administrator, agree that such a provision should not be included or if the Court makes an order stating that they approve of a decision not to include such a provision.

This is beneficial to employee creditors as under the statutory winding up order employee claims are given priority over unsecured claims. In terms of s 556 of the Corporations Act which deals with priority payments, when a company is being wound up a number of administrative expenses, followed by certain employee entitlements, are to be paid before other unsecured creditors. These employee entitlements are paid out in the following order: wages and superannuation, outstanding leave of absence and then retrenchment payments. These claims are paid out after debts secured by a fixed charge (secured creditors) but before claims of floating charge holders if the remainder of the company’s property is not sufficient to pay the employee entitlements mentioned above.

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293 Corporations Act s 444A(3).
294 Corporations Act s 444A(4)(h).
295 Ciro & Symes op cit note 289 at 539.
296 No. 132 of 2007 (Cth).
297 Corporations Act s 444DA.
298 Corporations Act s 444DA(2).
299 Corporations Act s 556.
300 Corporations Act s 556(1)(e), (g) and (h).
301 Corporations Act s 561(a).
The employee entitlements discussed above are employee claims that arose before the company entered into administration. In determining what happens to employee claims that arise once the company is under administration, the Australian Securities and Investments Commission (hereafter ‘ASIC’) guidelines state:

‘If the voluntary administrator continues to trade the business, they must pay out of the assets available to them ongoing wages for services provided and other employee entitlements that arise after the date of their appointment. These payments are treated as an expense of the voluntary administration.’

If the administration is followed by liquidation, these claims would rank at the top of the preferred claims listed in s 556(1). According to Wellard, it is generally accepted that post-appointment wages would fall under s 566(1)(a), as they are ‘expenses properly incurred by a relevant authority . . . in carrying on the company’s business’. The definition of ‘relevant authority’ provided in the Act includes an administrator. While these claims are regarded as a ‘first priority liquidation expense’ and rank ahead of other unsecured creditors, they still rank after secured creditors.

However, if administration is followed by liquidation the Australian government, in terms of the Fair Entitlements Guarantee (or the General Employee Entitlements and Redundancy Scheme if the liquidation occurred before 5 December 2012), will assist employees who have lost their jobs due to the liquidation and have outstanding entitlements. The guarantee provides that an advance can be made by the government to eligible employees for certain kinds of employee entitlements. If such an advance is made, the government can claim the amount they advanced from...

302 Corporations Act Section 444A(4)(i).
305 Ibid at 22.
306 Corporations Act s 556(2).
307 Wellard op cit note 304 at 22.
308 Fair Entitlements Guarantee Act No. 159 of 2012 s 3(a). Also see the Fair Entitlements Guarantee Bill 2012 Explanatory Memorandum.
309 These entitlements are specified in the Fair Entitlements Guarantee Act s 6.
the company through the liquidation process. This gives employees added protection if their employer is placed under liquidation.

Again it is clear that the South African provisions protect employees more than the United Kingdom and Australia when it comes to the priority of their claims. South Africa is the only jurisdiction, out of the three discussed, that ranks employee claims ahead of secured creditors.

(c) Notice and Participation

In the United Kingdom’s Insolvency Act and the Australian Corporations Act there is a noticeable lack of reference to employees, especially when compared to the South African business rescue provisions. The focus of the United Kingdom and Australian provisions, in terms of notice and participation, is primarily on the creditors. This will be demonstrated by briefly looking at who is notified when an administrator has been appointed, the procedure regarding the administrator’s proposal (or deed of company arrangement in Australia) and lastly the provisions requiring certain meetings and committees.

In both the United Kingdom and Australia when an administrator is appointed he or she is required to notify certain parties of the appointment. In the United Kingdom these parties include the company itself, each creditor whose claim and address is known, the registrar of companies and ‘such parties as may be prescribed’. In Australia these parties include the company (if the administrator was appointed by a chargee), persons holding a charge over all, or almost all, of the company’s property and persons holding a number of charges on the company’s property which, when combined, constitute almost all of the company’s property. In addition, the administrator is required to lodge a notice of the appointment with ASIC and publish the notice firstly, in a national newspaper and secondly, in a daily newspaper in the States or Territories in which the company’s office is registered or conducts its

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310 Fair Entitlements Guarantee Act s 31(1).
311 UK Insolvency Act Sch B1 para 46(1)-(5).
312 Corporations Act s 450A(2).
313 Corporations Act s 450A (3).
business.\textsuperscript{314} It is only the South African provisions that specifically state that employees, as affected persons, must be notified when a business rescue practitioner is appointed.\textsuperscript{315}

The next question that needs to be addressed is which parties have rights of notice when it comes to the administrator’s proposal in the United Kingdom and the deed of company arrangement in Australia. In the United Kingdom, in terms of paragraph 49 of Schedule B1, the administrator is required to produce a statement which sets out proposals as to how the purpose of administration can be achieved. A copy of this statement must be sent to the registrar of companies, every creditor whose claim and address is known as well as every member whose address is known.\textsuperscript{316} In Australia the company’s creditors, at a creditor’s meeting convened under s 439A, can decide that a deed of company arrangement must be executed.\textsuperscript{317} Once it is executed, the administrator is required to send a written notice that the deed has been executed to the company’s creditors and to lodge a copy of the deed with ASIC.\textsuperscript{318} In South Africa, creditors and holders of voting interests can adopt the business rescue plan at a meeting, but affected persons, including employees, are given notice of this meeting and employee representatives are given a chance to address the meeting.\textsuperscript{320}

Lastly, the United Kingdom and Australian provisions regarding meetings and committees will be discussed. In the United Kingdom the administrator is required to invite creditors to a creditors’ meeting\textsuperscript{321} where he or she will present a copy of the statement of proposals.\textsuperscript{322} At this meeting the creditors can approve the proposals or approve them subject to modifications to which the administrator approves.\textsuperscript{323} An important right of creditors is that the creditors at this meeting can establish a

\textsuperscript{314} Corporations Act s 450A(1).
\textsuperscript{315} Companies Act 2008 s 129(4)(b) and s 131(8)(b).
\textsuperscript{316} UK Insolvency Act Sch B1 para 49(4).
\textsuperscript{317} Corporations Act s 439C(a).
\textsuperscript{318} Corporations Act s 450B.
\textsuperscript{319} Companies Act 2008 s 151(2).
\textsuperscript{320} Companies Act 2008 s 152(1)(c).
\textsuperscript{321} UK Insolvency Act Sch B1 para 51(1).
\textsuperscript{322} UK Insolvency Act Sch B1 para 51(3).
\textsuperscript{323} UK Insolvency Act Sch B1 para 53(1).
creditors’ committee, which can require that the administrator provide them with information regarding the exercise of his or her functions as an administrator.\textsuperscript{324}

In Australia there are two meetings of creditors. The first meeting is convened so that the creditors can decide whether a committee of creditors should be appointed and to decide who the members of such a committee should be.\textsuperscript{325} This committee is required to consult with the administrator and to receive and consider the administrator’s reports.\textsuperscript{326} At this initial meeting the creditors may also remove the administrator and replace him or her with another administrator.\textsuperscript{327} At the second creditors meeting the creditors have to decide on the company’s future.\textsuperscript{328} They can decide that a deed of company arrangement should be executed, that the company should be returned to the control of the directors or that the company should be placed under liquidation.\textsuperscript{329} There is also provision in s 444DA for a meeting of employees. However, this meeting is limited to ‘eligible employee creditors’ and is convened so that eligible employee creditors can decide whether to accept the non-inclusion of s 444DA(1), which protects the priority of employee creditors in the deed of company arrangement.\textsuperscript{330}

South Africa, on the other hand, provides for both a meeting for creditors\textsuperscript{331} and a meeting of employees’ representatives.\textsuperscript{332} There is also provision for a creditors’ committee\textsuperscript{333} and a committee of employees’ representatives.\textsuperscript{334} The committee of employee representatives can confer with the practitioner\textsuperscript{335} and receive and deliberate on business rescue reports.\textsuperscript{336} It is therefore clear that while the United Kingdom and Australia focus on meetings and committees of creditors, South Africa also takes employees into account.

\textsuperscript{324} UK Insolvency Act Sch B1 para 57.
\textsuperscript{325} Corporations Act s 436E.
\textsuperscript{326} Corporations Act s 436F.
\textsuperscript{327} Corporations Act s 436E(4).
\textsuperscript{328} Corporations Act s 349A-C.
\textsuperscript{329} Corporations Act s 439C.
\textsuperscript{330} Corporations Act s 444DA(2).
\textsuperscript{331} Companies Act 2008 s 147(1).
\textsuperscript{332} Companies Act 2008 s 148(1).
\textsuperscript{333} Companies Act 2008 s 145(3).
\textsuperscript{334} Companies Act 2008 s 144(3)(c).
\textsuperscript{335} Companies Act 2008 s 149(1)(a).
\textsuperscript{336} Companies Act 2008 s 149(1)(b).
This section on ‘Notice and Participation’ demonstrates the lack of reference to employees in the United Kingdom and Australian provisions. The South African provisions, on the other hand, frequently refer to employees in their capacity as both employees and as affected persons. In South Africa employees are entitled to notice of, and to participate in, almost every step of business rescue. The same level of concern for employees is not evident in the other two jurisdictions.

(d) Rights in Terms of Labour Law

When a company is in financial distress, two of the most important question regarding employee rights are firstly, what rights employees have if they are made redundant and, secondly, what rights employees have if the business or part of the business is transferred. This section will consider the relevant legislative provisions relating to termination of employment contracts and the transfer of the business enterprise in each jurisdiction respectively.

The United Kingdom

- Termination of employment contracts

In the United Kingdom, administration does not automatically terminate employees’ contracts of employments. The contracts remain in force and are considered to be adopted if the practitioner does not terminate them within the first fourteen days of entering administration.337

If, during administration, the practitioner decides to make employees redundant, he or she will have to comply with consultation and redundancy payment requirements as set out in the Employment Rights Act 1996 (c. 18) (hereafter ‘the ERA’) and the Trade Union and Labour Relations (Consolidation) Act 1992 (c. 52) (hereafter ‘the TULRA’). An important distinction to make is that different procedures are required depending on the number of employees being dismissed.

337 Powdrill v Watson sub nom Re Paramount Airways Ltd (No 3) [1995] 2 AC 394. Also see the UK Insolvency Act Sch B1 para 99(5)(a).
In terms of s 188 of the TULRA, if an employer proposes making 20 or more employees redundant within 90 days, the employer is required to consult with the representatives of the affected employees. These can be referred to as ‘collective redundancies’. If it is proposed that more than 100 employees will be dismissed, the consultation must begin 45 days before any dismissal takes effect. Otherwise, 30 days must elapse from the beginning of the consultation period to the first dismissal.\(^{338}\) The employer and representatives are required to consult on ways to avoid the redundancies, ways to decrease the number of redundancies and ways to reduce the negative effects of the redundancies.\(^{339}\) If the employer breaches his or her obligations under s 188, an employee can complain to an employment tribunal, who can make a protective award in favour of the employee.\(^{340}\)

Different provisions apply when less than 20 employees are being dismissed for reasons of redundancy. These can be referred to as ‘individual redundancies’ and are governed by the ERA. Most importantly, the ERA provides employees with the right not to be unfairly dismissed in s 94(1). The ERA provides less guidance than the TULRA on whether consultation is required, what needs to be consulted and when consultation needs to begin. However, it has been established that employers are required to consult for a ‘reasonable period’, the duration of which depends on the circumstances of the case, and that the consultation should begin in ‘good time’ before it has been decided that particular employees will be dismissed.\(^{341}\) This is important as if employees are not consulted appropriately before the dismissals, they could claim that the dismissals were unfair.\(^{342}\)

Even where employees are dismissed fairly due to redundancy, s 135 of the ERA entitles the dismissed employees to redundancy payment. However, as noted in chapter V(b) of this dissertation, redundancy payments in the United Kingdom are not afforded ‘super priority’ status under paragraph 99(4) and (5).\(^{343}\)


\(^{339}\) TULRA s 188(2).

\(^{340}\) TULRA s 189.


\(^{342}\) ERA s 94(1).

\(^{343}\) \textit{Re Allders Department Stores} supra note 274 para 21.
• *Transfer of business enterprise*

The next question that needs to be considered is what rights employees are afforded in the United Kingdom when the business or part of the business is transferred during administration. This is regulated by the Transfer of Undertakings (Protection of Employment) Regulations No. 246 of 2006 (hereafter ‘TUPE’). In terms of regulation 4 of TUPE, the transfer of the company or part of the company does not terminate employee contracts of employment. These contracts continue in force after the transfer as if the contracts were entered into by the transferee and the employees.\(^{344}\) Regulation 4 continues to state that the rights, powers, duties and liabilities of the transferor in terms of the contracts are transferred to the transferee.\(^{345}\) Acts or omissions of the transferor in relation to the contracts of employment are deemed to be acts or omissions of the transferee.\(^{346}\) Regulation 7, another important provision, states that where an employee is dismissed, either before or after the transfer, and the sole or principal reason for the dismissal is the transfer or ‘a reason connected with the transfer that is not an economic, technical or organisational reason entailing changes in the workforce’, such dismissal will be treated as an unfair dismissal.\(^{347}\) Additionally, if such a transfer is contemplated the employer has a duty, in terms of regulation 13, to inform and consult with representatives of the affected employees.

A question that was recently answered by the courts was whether administration qualifies as ‘bankruptcy proceedings or any analogous insolvency proceedings’ in terms of regulation 8(7) of TUPE. If it did, regulations 4 and 7 of TUPE would not apply to the transfer. This would have devastating effects for employees as their contracts of employment would not be automatically transferred to the transferee in terms of regulation 4. Regulation 8(7) applies

\[\text{‘where the transferor is the subject of bankruptcy proceedings or any analogous}\\ \text{insolvency proceedings which have been instituted with a view to the}\]

\(^{344}\) TUPE reg 4(1).  
\(^{345}\) TUPE reg 4(2)(a).  
\(^{346}\) TUPE reg 4(2)(b).  
\(^{347}\) TUPE reg 7(1)(b).
However, in *Key2Law (Surrey) LLP v De’Antiquis*\(^{349}\) the Court of Appeal held that companies under administration do not fall under regulation 8(7),\(^{350}\) therefore regulation 4 and 7 of TUPE both apply to companies that are under administration. This was an important decision concerning employee rights during a transfer as now it is clear that when a business under administration transfers a business or part of a business, the existing employee contracts will be transferred to the transferee.

It is also important to determine whether companies under administration can be said to be subject to ‘relevant insolvency proceedings’\(^{351}\) in terms of regulation 8 as this also has important consequences. In terms of regulation 8(6), relevant insolvency proceedings are ‘insolvency proceedings which have opened in relation to the transferor not with a view to the liquidation of the assets of the transferor and which are under the supervision of an insolvency practitioner’. As the primary aim of administration is to rescue the company and not to realise the company’s assets it is clear that it would be regarded as a ‘relevant insolvency proceeding’ in terms of this regulation.\(^{352}\) This has two very important effects. Firstly, in terms of regulation 9 the transferor and the representatives of affected employees are allowed to agree to certain variations of employment contracts.\(^{353}\) Secondly, employee debts and liabilities found under Parts XI and XII of the ERA are not automatically transferred to the transferee, but must instead be paid to the employee by the National Insurance Fund.\(^{354}\) These debts include holiday pay, redundancy payment and arrears of pay.\(^{355}\) However, there are limits as to how much employees can claim from the Fund, therefore the transferee becomes liable for the shortfall where claims are in excess of those limits.\(^{356}\)

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348 TUPE reg 8(7).
350 Ibid para 103.
351 TUPE reg 8(1).
353 TUPE reg 9(1).
354 TUPE reg 8(4) and (5). Also see Nyombi op cit note 352 at 6.
355 ERA parts XI and XIII.
356 Nyombi op cite note 352 at 6.
While the United Kingdom has similar rules to South Africa when it comes to the termination of employment contracts, there is an important difference when it comes to the transfer of a business enterprise. In the United Kingdom the rules regarding transfers are relaxed when a company is under administration which could make the sale more attractive to potential buyers. Unfortunately the same relaxation is not seen in the South African provisions.

**Australia**

In Australia, most workplaces are governed by the Fair Work Act\(^\text{357}\) (hereafter ‘the FWA’) which replaced the Workplace Relations Act\(^\text{358}\) in 2009. The FWA contains both redundancy and transfer of business provisions, which will be discussed in turn below.

- **Termination of employment contracts**

If, in an administration, certain employees are made redundant, the administrator will have to comply with the redundancy provisions in the FWA. Unlike in the United Kingdom and South Africa, the procedure an employer has to follow when making employees redundant in Australia does not differ depending on the number of employees being made redundant.

In terms of the FWA, a dismissal will be regarded as unfair if it is established that the employee was dismissed, that ‘the dismissal was harsh, unjust or unreasonable’, that the Small Business Fair Dismissal Code was not followed and that the dismissal does not qualify as a ‘genuine redundancy’.\(^\text{359}\)

The dismissal is a ‘genuine redundancy’ if, due to a change in the employer’s operational requirements, the job performed by the dismissed employee is no longer required.\(^\text{360}\) Additionally, the employer must comply with any consultation

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\(^{357}\) No. 28 of 2009.

\(^{358}\) 1996 (Act No. 86 of 1988 as amended).

\(^{359}\) FWA s 385.

\(^{360}\) FWA s 389(1)(a).
obligations contained in an applicable modern award or enterprise agreement.\textsuperscript{361} However, if it would have been reasonable for the employee to be redeployed within the enterprise of the employer or within an associated entities’ enterprise, then the dismissal is not considered a ‘genuine redundancy’.\textsuperscript{362}

If the dismissal is not a case of genuine redundancy, the next question is whether the dismissal was ‘harsh, unjust or unreasonable’.\textsuperscript{363} In order to determine whether the dismissal was harsh, unjust or unreasonable the Fair Work Commission can take into account whether the employer complied with consultation obligations contained in a modern award. In \textit{UES (Int’l) Pty Ltd v Harvey}\textsuperscript{364} it was decided that a failure to consult will not necessarily render a dismissal harsh, unjust or unreasonable, but in the particular case the failure was unreasonable and was held to be sufficient to regard the dismissal as harsh, unjust or unreasonable.\textsuperscript{365} On the other hand, in the case of \textit{Maswan v Escada Textilvertrieb T/A ESCADA},\textsuperscript{366} it was decided that as it was clear that the employee would have been dismissed even if consultation had taken place, the failure to consult in accordance with the modern award did not render the dismissal harsh, unjust or unreasonable.\textsuperscript{367}

If the dismissal is found to be unfair and the employee is protected from unfair dismissals in terms of s 382 of the FWA,\textsuperscript{368} the Fair Work Commission can order that the employee be reinstated or be paid compensation in lieu of reinstatement.\textsuperscript{369}

If the redundancy was a ‘genuine redundancy’ and is therefore not an unfair dismissal, the dismissed employee may still be entitled to redundancy pay in terms of the National Employment Standards. These Standards are statutory minimum

\textsuperscript{361} FWA s 389(1)(b).
\textsuperscript{362} FWA s 389(2).
\textsuperscript{363} \textit{Maswan v Escada Textilvertrieb T/A ESCADA} [2011] FWA 4239 at 14.
\textsuperscript{364} [2012] FWAFB 5241.
\textsuperscript{365} Ibid para 49.
\textsuperscript{366} \textit{Maswan} supra note 363.
\textsuperscript{367} Ibid para 39.
\textsuperscript{368} In terms of s 382 of the FWA, a person is protected from unfair dismissals if they have been employed by the employer for one year (if the employer is a small business employer) or six months (if the employer is not a small business employer). Additionally, the employee must be covered by a modern award, be covered by an enterprise agreement or their annual rate of earnings must be less than the high income threshold.
\textsuperscript{369} FWA s 391(1) and s 392(1).
standards for employees and are contained in the FWA. According to s 119 of the FWA, an employee who is dismissed by their employer because of insolvency or bankruptcy, or because the job of the employee is no longer required by the employer ‘except where this is due to the ordinary and customary turnover of labour’ is entitled to redundancy pay. The amount of payment the employee is entitled to depends on the length of the employee’s service with the employer.

However, not all employees are entitled to redundancy pay due to s 121 and s 123 of the FWA. Section 121 states that employees employed by the employer for fewer than 12 months and employees of small business employers are not entitled to redundancy pay in terms of s 119. It also states that a term which specifies circumstances in which s 119 does not apply may be included in a modern award. If such a term is included, it can be incorporated into an enterprise agreement. In addition, s 123 lists certain employees that are not covered by the redundancy pay provisions, including employees dismissed for serious misconduct, casual employees, apprentices and employees covered by an industry-specific redundancy scheme in a modern award.

- **Transfer of business enterprise**

The next question that needs to be answered is what happens if, as part of the administration, the business or part of the business is transferred. Part 2-8 of the FWA deals with ‘transfer of business’. The provisions under this Part set out the effect that a transfer can have on employees. Importantly, the meaning given to the term ‘transfer of business’ in the Australian FWA is very different to the meaning of ‘transfer of a business’ or ‘transfer of undertakings’ in South Africa and the United Kingdom.
Kingdom respectively. The different definition in the FWA is important because it limits which employees are provided protection under the Part.

In terms of s 311(1) of the FWA a ‘transfer of business’ from an old employer to a new employer occurs if four requirements are satisfied. Firstly, the employee’s employment with the old employer must have terminated. Secondly, the employee must be employed by the new employer within three months of the termination. Thirdly, the work performed by the employee for the new employer must be ‘the same, or substantially the same’ as the employee’s work for the old employer. The last requirement is that there must be a certain type of connection between the old and new employer. The connection that must exist can be that there was an asset transfer between the old and new employer, that work was outsourced by the old employer to the new employer, that the new employer has ceased to outsource work to the old employer (i.e. that there was in-sourcing) or that the old and new employers are associated entities in terms of s 50AAA of the Corporations Act.

If it is established that there was a transfer of business, any transferable instrument, such as an approved enterprise agreement, a workplace determination or a named employer award covering the transferring employee (an employee who satisfies the first three requirements of s 311(1)) and the old employer will continue to cover the transferring employee once they are employed by the new employer. In this regard, the obligations of the first employer will apply to the second employer. In addition, subject to some exceptions, periods of service with the first employer will be counted as service with the second employer. If periods of service with the first employer are counted, the transferring employee is not entitled to claim that due to the termination of employment with the first employer, they are entitled to

380 FWA s 311(1)(a).
381 FWA s 311(1)(b).
382 FWA s 311(1)(c).
383 FWA s 311(1)(d).
384 FWA s 311(3)-(6).
385 FWA s 312(1).
386 FWA s 311(2).
387 FWA s 313(1)(a).
389 FWA s 22(5).
redundancy pay and pay for untaken paid annual leave from the old employer.\textsuperscript{390} The exceptions to this rule are found in s 122(1) and s 91(1) which state that if the old and new employers are non-associated entities, the new employer can choose not to recognise the employee’s service with the old employer for the purposes of untaken paid annual leave and redundancy pay. In such a situation the old employer will be under an obligation to pay those entitlements.

A dismissed employee will also not be entitled to redundancy pay if the new employer offers the employee employment on similar terms and conditions to those that the employee had with the old employer, but the employee rejects the offer.\textsuperscript{391} Additional conditions are that the offer must state that the employee’s service with the old employer will be recognised and the circumstances must be such that there would have been a transfer of employment if the employee had accepted the offer.\textsuperscript{392} If an offer of employment is not acceptable alternative employment because, for example, the employee is expected to accept a significant cut in their salary, the employee is entitled to reject the employer’s offer.\textsuperscript{393}

This description of the ‘transfer of business’ provisions has demonstrated that if an employee qualifies as a ‘transferring employee’, they will be afforded a certain amount of protection by the FWA when there is a transfer of business. However, for an employee to be a ‘transferring employee’, one of the requirements under s 311(1) is that they are employed by the new employer within three months of their termination of employment with the old employer.

The discussion on ‘Rights in Terms of Applicable Labour Law’ demonstrates that while the United Kingdom and South Africa provide similar protection to employees who face redundancy or a transfer of business, the Australian position is more restricted. In particular, it places restrictive limits on which employees can claim redundancy pay and, unlike the United Kingdom and South African position, there is no obligation on new employer to employ existing employees in a transfer of business situation.

\textsuperscript{390} FWA s 122(2) and s 91(2).
\textsuperscript{391} FWA s 122(3)(a)(i).
\textsuperscript{392} FWA s 122(3)(a)(ii) and s 122(3)(b).
\textsuperscript{393} Mantra Hospitality (Admin) Pty Ltd [2013] FWC 1063 at 39.
VII ASSESSMENT OF SOUTH AFRICAN PROVISIONS

When a company is in financial distress and is placed under business rescue, there can be tension between the primary objective of business rescue, which is rescuing the company, and the amount of protection given to employees. This tension is caused by the fact that retaining employees and paying them their entitlements adds to the cost of running the business which could impact the success of the rescue attempt.\(^{394}\) In order to deal with this tension, business rescue provisions need to balance the interests of a company’s various stakeholders including employees, creditors, shareholders and debtors. In recognition of this, the Companies Act 2008 states that this is one of its purposes.\(^{395}\)

However, if the business rescue provisions overprotect employees it may be to the employees’ own detriment.\(^{396}\) This is due to the fact that it is in the employees’ best interests that the company is rescued so that they continue to be employed.\(^{397}\) If the provisions are skewed too far in favour of employees, banks and other investors who are vital to the company’s survival will not want to invest their money in the financially distressed company and the rescue attempt could suffer as a result.\(^{398}\)

Joubert, van Eck and Burdette assessed the South African business rescue provisions and noted that they do not place sufficient emphasis on the objective of rescuing the company.\(^{399}\) The authors came to the conclusion that ‘the provisions are too obviously skewed in favour of the employees’.\(^{400}\) In light of this they found that the rights of stakeholders were not balanced appropriately which, according to the authors, could ultimately weaken the efficiency of the business rescue procedure.\(^{401}\) The authors also raised the concern that employees may be tempted to abuse the

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\(^{394}\) Parry op cit note 273 at 29.
\(^{395}\) Companies Act 2008 s 7(k).
\(^{396}\) Joubert, van Eck & Burdette op cit note 1 at 67.
\(^{397}\) Ibid at 65.
\(^{398}\) Ibid at 67.
\(^{399}\) Ibid at 83.
\(^{400}\) Ibid.
\(^{401}\) Ibid at 84.
procedure for personal gain due to the vast amount of rights given to them during business rescue proceedings.\textsuperscript{402}

In light of the conclusion of Joubert, van Eck and Burdette there are three questions that need to be discussed. Firstly, whether there is any justification for giving employees rights in business rescue proceedings that could negatively impact the company’s chances of success. Secondly, whether the South African business rescue provisions provide too much protection for employees and, if so, which employee rights are excessive and which are justified in the circumstances. These questions will be discussed below.

\textit{(a) Justification for Employee Protection}

The first question that needs to be answered is whether employees should be given rights that could negatively impact the company’s chances of success. It could be argued that companies will perform best, both in terms of efficiency and economic growth, if employers are unconstrained and free to do as they please.\textsuperscript{403} However, there are a number of justifications for protecting employees, and therefore constraining the power of employers, when a company is under business rescue.

One of the most important arguments is that employees should be protected in terms of social justice because they are almost always the weaker bargaining party.\textsuperscript{404} The amount of power between employers and employees is undeniably unequal and not recognising this power imbalance could result in employees being exploited.\textsuperscript{405} As employee contracts of employment are not able to balance this power inequity,\textsuperscript{406} South African legislation needs to protect employees in order to prevent employee exploitation.

\textsuperscript{402} Ibid.
\textsuperscript{403} McCormack op cit note 281 at 250.
\textsuperscript{404} Ibid. Also see Keay & Walton op cit note 233 at 468.
\textsuperscript{405} Joubert, van Eck & Burdette op cit note 1 at 66.
\textsuperscript{406} Ibid.
Another important factor to take into account is that employees generally have the most to lose if the company they work for is struggling financially.\textsuperscript{407} If an employer cannot pay an employee, it is likely that this will take away the employee’s only form of income.\textsuperscript{408} Other creditors, on the other hand, are likely to have a number of sources of income.\textsuperscript{409} In addition, employees are not in the same position as shareholders and other creditors in that they cannot factor in the risk of the employer becoming financially distressed like other stakeholders can.\textsuperscript{410} In order to protect themselves from the risk of a company failing, shareholders can diversity their portfolios.\textsuperscript{411} On the same note, creditors can protect themselves by having a number of customers or by factoring the risk into the rate at which they provide credit.\textsuperscript{412} In this regard employees are ‘involuntary creditors’\textsuperscript{413} as most of them have not voluntarily taken on the risk that their employer will fall into financial difficulty.\textsuperscript{414}

Business rescue provisions in South Africa also need to protect employees in order to give effect to their constitutional right to fair labour practices.\textsuperscript{415} The inclusion of this right in the South African Constitution demonstrates the importance of employee rights in South Africa’s constitutional democracy. The Companies Act 2008 explicitly states that one of its purposes is to ensure compliance with the Bill of Rights, which includes the right to fair labour practices.\textsuperscript{416} As other stakeholders such as creditors, shareholders and debtors do not have this direct constitutional protection, the South African business rescue provisions needed to be, at least to some extent, employee-friendly. In fact, van Eck, Boraine and Steyn argue that the initiatives for the introduction of a business rescue procedure in South Africa were

\textsuperscript{408} Ibid.
\textsuperscript{409} Explanatory Statement to Exposure Draft on Corporations Amendment (Insolvency) Bill 2007 (Cth) November 2006 at 13.
\textsuperscript{410} Johnson op cit note 407 at 13.
\textsuperscript{411} Nyombi op cit note 352 at 2.
\textsuperscript{412} Ibid. Also see Johnson op cit note 407 at 224.
\textsuperscript{413} Explanatory Statement to Exposure Draft supra note 409 at 13.
\textsuperscript{414} Johnson op cit note 407 at 224.
\textsuperscript{415} South African Constitution s 23(1).
\textsuperscript{416} Companies Act 2008 s 2(a).
driven by the labour movement, which was in turn driven by the right to fair labour practices.\footnote{Stefan van Eck, Andre Boraine & Lee Steyn ‘Fair Labour Practices in South African Insolvency Law’ (2004) 121 S. African L.J. 902 at 906.}

In addition to the above arguments, requiring employers to consult with and notify employees about what is going on in the company could result in the employees being more accepting of controversial decisions and could assist the employer in making better decisions.\footnote{McCormack op cit note 281 at 250.}

Lastly, it could be argued that the success of a company depends on how productive its employees are.\footnote{Nyombi op cit note 352 at 4.} If the employees are happy and productive this could benefit the company. However, if the employees are disgruntled and unmotivated, it could have devastating effects on the success of the company.

The above discussion demonstrates that employees should be protected during business rescue proceedings even if it could negatively affect the company’s chances of a successful rescue. However, it has also been established that it is ultimately in the best interests of the employees for the company to be rescued successfully.\footnote{Joubert, Van Eck & Burdette op cit note 1 at 65.} For this reason it would be to the benefit of employees if the correct balance between the rights of stakeholders is struck. The business rescue provisions need to protect employees and at the same time provide a business rescue regime that can be successful.

\underbrace{(b)}_{\text{Do the South African Business Rescue Provisions Overprotect Employees?}}

The next question to be answered is whether the South African business rescue provisions provide too much protection for employees and, if so, which employee rights are excessive and which are justified in the circumstances. In order to answer the posed question, this discussion will focus on the four most important categories of employee rights in business rescue proceedings which were set out in the ‘Comparative Perspective’ chapter. These categories are firstly, the ability of
employees to commence proceedings, secondly, the priority of employee claims, thirdly, employee rights to notice and participation and lastly, employee rights in terms of labour law.

(i) Ability to commence proceedings

Out of the three jurisdictions assessed in this dissertation, South Africa is the only one which allows employees to apply to court for an order that commences business rescue proceedings. According to Loubser,\(^{421}\) this inclusion is excessive and is not in line with international trends.\(^{422}\) The concern with this entitlement is that there is potential for trade unions and individual employees to abuse the right. Trade unions could use this right as a bargaining tool by threatening to apply for a commencement order if the company does not meet its demands.\(^{423}\) Even if the application is rejected, notice of the application would be given to creditors and shareholders, which could cause irreparable damage to the company’s reputation.\(^{424}\) In light of this concern, Loubser suggests that the court should be entitled to make an order for the payment of damages against any person that abuses their right to apply for a commencement order or who brings a ‘malicious or vexatious’ application.\(^{425}\) I agree with Loubser as it is clear that without this safeguard in place the procedure is open to abuse by employees and their trade unions.

(ii) Priority of claims

Unlike in the United Kingdom and Australia, employee claims that arise after business rescue proceedings commence in South Africa are paid in priority to secured creditors. It has been argued that this preference enjoyed by employees may cause practical problems as it could potentially discourage banks and investors from lending the company money.\(^{426}\) The potential creditors will have to take into account

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\(^{423}\) Ibid at 54.

\(^{424}\) Ibid.

\(^{425}\) Ibid at 55.

\(^{426}\) Joubert, van Eck & Burdette op cit note 1 at 80.
that their claim (even if secured) will stand behind those of certain employees. The issue is exacerbated when one considers the fact that if the business rescue proceedings turn into liquidation proceedings this order of preference will stand.\(^{427}\) The criticisms of this preference order seem to be justified, particularly when one considers the important role that post-commencement finance plays during business rescue attempts. Lack of post-commencement finance from banks and investors will ultimately make it far more difficult to run the business as a going concern and could very possibly hinder business rescue attempts.

However, as discussed earlier, employees have the most to lose if the business rescue attempt is not successful and their salary is likely to be their only source of income. It is therefore understandable that if the employees are asked to work for a company that is in financial distress, they should be placed high on the order of priority. The employees are also given such high priority because they are indispensable to the company.\(^{428}\) If employees were lower on the order of priority they may choose to ‘cut their losses’, resign and look for another job.\(^{429}\) Giving employee claims a high priority may motivate the employees and encourage them to carry on working for the company.\(^{430}\) If the employees were to resign, running the company as a going concern would become exceptionally difficult. While one can argue that not receiving post-commencement finance could be detrimental to business rescue attempts, one could also argue that having unmotivated employees, or employees that resign, will have an even worse effect on the rescue attempt. In light of these factors the order of priority contained in the Companies Act 2008 can be justified.

(iii) Notice and participation

The South African business rescue provisions give employees notice and participation rights at almost every stage of the proceedings. While the intention behind these rights may be noble, the reality is that it places a heavy burden on the company in terms of both administration and cost.\(^{431}\) Loubser suggests that affected

\(^{427}\) Ibid.
\(^{428}\) Ibid.
\(^{429}\) Nyombi op cit note 352 at 9.
\(^{430}\) Bradstreet op cit note 32 at 359.
\(^{431}\) Ibid.
persons should only receive notification when they ‘are able to influence the outcome’ of a process.\textsuperscript{432} Loubser also takes issue with some of the participation rights of affected persons, specifically their right to participate in the application to commence business rescue proceedings.\textsuperscript{433} She argues that this could result in long and expensive hearings, and says that it unnecessarily complicates the application which should be decided by the court without a flood of different opinions.\textsuperscript{434} While I agree with Loubser when it comes to participation in certain hearings, I disagree with the suggestion that employees should only be given notice when they can influence the outcome. It seems fair that if an employee is expected to work for a company that is in financial distress, they should be given notification of what is going on in the company.

(iv) Rights in terms of labour law

In terms of employees’ rights when they are retrenched, these rights seem to be justified. The main obligation on employers when they wish to retrench employees is that they have to consult with the employees (or other relevant party in terms of s 189(1) of the LRA). This process is important because it could assist the employer make a better decision as different perspectives and ideas are being included in the process, thereby making the decision making process more effective.\textsuperscript{435} In addition, consultation can ‘take the sting out of’ difficult decisions that employers have to make which will help employees accept the decisions.\textsuperscript{436} The requirements may place a burden on the employer, but considering the devastating effect that retrenchments can have on employees this burden is justified. These requirements are also not materially different from those in the United Kingdom and Australia.

When it comes to the transfer of business, however, the South African position is different to that of Australia and the United Kingdom. As discussed in the previous chapter, when a business or part of a business is transferred in Australia, the new

\textsuperscript{432} Ibid.
\textsuperscript{433} Loubser op cit note 421 at 78.
\textsuperscript{434} Ibid.
\textsuperscript{435} McCormack op cit note 281 at 250.
\textsuperscript{436} Ibid at 215.
employees are not automatically transferred to the new employer.\textsuperscript{437} In the United Kingdom, employees are transferred to the new employer, but if the old employer is under administration some of the rules are relaxed.\textsuperscript{438} In South Africa the rules regarding the transfer of a business are relaxed when the company is insolvent or if a scheme of arrangement or compromise is entered into, but not if the company is under business rescue.\textsuperscript{439} Unlike the rules for an insolvent company, if a company is under business rescue the rights and obligations of the old employer are transferred to the new employer and anything done by the old employer is deemed to have been done by the new employer.\textsuperscript{440} This could make the business less appealing to a potential buyer.\textsuperscript{441} Companies that are being ‘rescued’ should therefore be subject to s 197A of the LRA, which deals with insolvent companies or companies that have entered into a scheme of arrangement or compromise, rather than s 197, which deals with solvent companies. This would mean that the company under business rescue retains some of its obligations to the employees, but the sale is likely to bring in some much needed capital.

This discussion demonstrates that the question of whether the South African business rescue provisions overprotect employees cannot be answered with a simple yes or no answer. There are some rights that are excessive, but others which can be justified. Including some of the changes mentioned above into the business rescue provisions would help in striking a balance between the protection of employees and the effectiveness of business rescue proceedings.

VIII CONCLUSION

The aims of this dissertation were firstly, to provide a consolidated guide to the protection employees are afforded during business rescue proceedings in South Africa. Secondly, to compare the amount of protection South African employees are granted in the Companies Act 2008 with the amount of protection granted in the corporate rescue provisions of the United Kingdom and Australia. Lastly it was to

\textsuperscript{437} FWA s 311(1).
\textsuperscript{438} TUPE reg 8(4) and reg (5).
\textsuperscript{439} LRA s 197A(1).
\textsuperscript{440} LRA s 197(2)(b) and (c).
\textsuperscript{441} Loubser op cit note 27 at 68.
assess whether the South African business rescue provisions are too employee friendly and, if so, which provisions are problematic. The concern is that if business rescue provisions do not strike the correct balance between different stakeholders and they overprotect employees, it could have a detrimental effect on rescue attempts.

Setting out the South African business rescue provisions demonstrated that there is a clear concern for employees in the South African business rescue provisions. Not only do they receive rights in their individual capacity as employees, but they also receive rights as an affected person. This gives the employees a vast number of important rights which, when looked at as a whole, could allow employees to have a big impact on business rescue proceedings.

The results of the comparison with the United Kingdom and Australia demonstrated that the South African business rescue provisions provide employees with far more protection than both of the discussed jurisdictions, especially in terms of the priority of their claims and their rights to notice and participation. The South African provisions are also unique in that they allow an employee, as an affected person, to apply to court for an order commencing business rescue. In terms of the rights that the employees are granted by virtue of labour law, the comparison showed that South Africa provides similar protection to the United Kingdom, but far more than Australia.

In light of this comparison the South African provisions were assessed. It was established that employees should be protected, even if it could negatively impact a company’s chances of successful rescue due to their weaker bargaining position, their constitutional right to fair labour practices, the fact that they have the most to lose if the rescue attempt is unsuccessful and the fact that receiving employee input could lead to better decision-making.

It has been made clear that some of the South African business rescue provisions overprotect employees which could be to the detriment of the business rescue attempt and ultimately the employees. While some of the protective provisions are justified, others seem excessive and are not seen in countries with comparable corporate rescue procedures. This raises the question of whether the South African
provisions should be amended to place more focus on ‘rescuing’ the company and less on the protection of employees. However, it must be kept in mind that, unlike in the United Kingdom and Australia, South African employees have a constitutional right to fair labour practices. Questions then arise as to how the provisions can be amended so that sufficient focus is placed on ‘rescuing’ the company without infringing the right to fair labour practices.

In this dissertation a number of potential changes to the Companies Act 2008 were discussed. These changes include measures to prevent affected persons abusing their right to apply for an order commencing business rescue proceedings, limiting which proceedings affected persons can participate in, and amending the LRA so that companies under business rescue are subject to s 197A instead of s 197 when the business or part of the business is transferred as a going concern. These amendments would help strike the correct balance between various stakeholders and, at the same time, provide employees with enough protection to give effect to their right to fair labour practices. Employee protection is undeniably important, but giving employees excessive rights that place business rescue attempts in jeopardy is not the best way to protect them as it is ultimately in their best interests for the ‘rescue’ attempt to be successful.
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