REPUBLIC OF SOUTH AFRICA

IN THE LABOUR COURT OF SOUTH AFRICA, JOHANNESBURG

JUDGMENT

Reportable

Case no: JS 1039 /10

In the matter between -

STYLIANOS PALIERAKIS **Applicant**

And

ATLAS CARTON & LITHO
(IN LIQUIDATION) **First Respondent**

ATLAS PAPER SACKS C.C **Second Respondent**

ATLAS PACKAGING (PTY) LTD **Third Respondent**

Date heard: 25 November 2013

Date of Judgment: 20 June 2014

Summary: Sale of business as a going concern. Transfer of business in terms of Section 197A (1) of the LRA - Application of common law compromise and scheme of arrangement. Application of section 311 of the Companies Act of 1973 to the provisions of 197A (1) (b) of the LRA. Labelling an agreement as being governed by section 197A(1) of the LRA

JUDGMENT

MOLAHLEHI J

Introduction

[1] The applicant initially lodged the alleged unfair dismissal claim against the first and second respondents. He abandoned the claim against the two respondents after the agreement to have the third respondent joined in the proceedings as a party. The claim against the two respondents was abandoned subsequent to joining the third respondent.

[2] The third respondent has raised a point *in limine* contending that the applicant was not its employee and therefore there is no basis for the claim. To the extent that the applicant relies on the provisions of section 197 of the Labour Relations Act of 1995, (the LRA) the third respondent contends that the applicable section is section 197A of the LRA.

[3] The applicant contends that the third respondent is liable for his unfair retrenchment because the transfer of the business to the third respondent took place in terms of section 197 of the LRA.

Background facts

[4] The applicant was dismissed for operational reasons by the first respondent on 14 April 2010. After his dismissal and on 29 September 2010, the first and second respondent concluded a business sale agreement with the third respondent. Although there is some suggestion in the pleadings that the applicant was employed by the second respondent, it is not clear whether that was indeed the case. It is however not disputed that he was employed by the first respondent. For the purpose of this judgment the matter is approached as if the applicant was employed only by the first respondent.

[5] On 5 August 2011, the first and second respondents went into voluntary liquidation which was converted into compulsory liquidation on 7 September 2011.

[6] The case of the third respondent is that although the transfer of the business from the first respondent took place as a going concern, the provisions of section 197 of the LRA does not apply, but what rather applies are the provisions of section 197A of the LRA. The third respondent's contention is largely based on the agreement concluded with the first respondent.

[7] The sale of business agreement provides for amongst other things in the definition section that employees are "any persons employed by the Seller in respect of the Business before the Effective Date." It also records in relation to the issue of the employees that the business was sold as a going concern in terms of section 197A of the LRA and that all the contracts of employment between the first respondent and the employees shall continue without interruption with the third respondent.

The issue for determination

[8] The issue for determination at this point is whether the provisions of section 197A apply when regard is hard to the facts of this matter and in particular as concerning the provisions of the sale of business agreement. If found that the provisions of section 197A (1) (b) and (c) of the LRA is applicable, then that would be the end of the applicant's claim as against the third respondent. If it is found that it does not then the matter would proceed to the main claim.

The submissions by parties

[9] The third respondent contends that the agreements concluded between it and the other parties in the purchase of the businesses was a compromise or a scheme of arrangement contemplated in section 197(A)(1)(b) of the LRA. In other words, the contention is that, section 197 of the LRA does not apply, but

rather what applies on the facts of this matter are the provisions of section 197A (b) read with (c) of the LRA.

[10] The contention that the business was sold through some compromise or a scheme of arrangement is based on the following suspensive conditions:

a) The written release by Mr Gargassouls (one of the members of the first respondent) of the fixed assets from the Notorial Bond and the Accounts Receivable from cession.

b) The litigation currently existing between the first respondent and Mondi Paper Limited. The agreement in this regard specifically provides that those proceedings are excluded from the agreement and that the first respondent and Mr Gargassouls indemnify the third respondent against any claim which may be made by Mondi Papers.

c) The liabilities of the first respondent in relation specifically to the employees to be assumed by the third respondent.

d) The third respondent undertook to assume the responsibility for the loan of Mr Gargassouls.

[11] The other point on which the third respondent relies on is that, at the time of the conclusion of the sale of the business, the employee's employment contract was already terminated. In this respect, the third respondent contends that the applicant was not its employee on a proper construction and interpretation of the agreement that the third respondent concluded with the first respondent. The ground upon which this contention is based on is that, the first respondent did not in terms of clause 2.1.3 34 of the agreement assume any liability or claims that the applicant may have had against the first and second respondent. Clause 2.1.3 34 reads as follows:

> 'Sold Liabilities"-the liabilities of the Seller to be assumed by the Purchaser and comprising –

2.1.3.3 4.1 the trade liabilities of the Seller in respect of the Business as at the Effective Date, incurred in the ordinary, normal and regular course of business, including without limitation, to all employee related liabilities.'

[12] The third respondent further contends that the provisions of section 197A of the LRA apply in this matter for the following reasons:

a) because the sale agreement took place in the context of some form of a compromise or an arrangement between the parties.

b) the agreement specifically records at clause 19 thereof that the business is sold as going concern in terms of section 197A of the LRA.

Legal principles

[13] The case of the third respondent, as stated earlier is that the provisions of section 197A(1)(b) and (c) of the LRA apply in this matter. The issue of whether the provisions of the section 197A apply is a matter to be determined by considering the objective facts placed before the Court. The issue of whether the provision of section 197 of the LRA applies is an issue to be determined in the main application when the claim of the applicant is considered. In other words what is to be determined in the present instance is the interlocutory point regarding the application of section 197A of the LRA.

[14] Section 197 of the LRA reads as follows:

'**Transfer of contract of employment**. –

(1) In this section and in section 197 A

(a) business" includes the whole or a part of any business, trade, undertaking or service; and

(b) "transfer' means the transfer of a business by one employer ("the old employer") to another employer ("the new employer") as a going concern.

(2) If a transfer of a business takes place, unless otherwise agreed in terms of subsection (6) –

(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 the 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.'

[15] The case of the third respondent is that the provisions of section 197A apply in this matter. Section 197(A) of the LRA reads as follows:

"197A.Transfer of contract of employment in circumstances of insolvency

(1) This section applies to a transfer of a business -

(a) if the old employer is insolvent; or

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

(2) Despite the Insolvency Act, 1936 (Act No. 24 of 1936), if a transfer of a business takes place in the circumstances contemplated in

subsection (1), unless otherwise agreed in terms of section 197(6)-

(a) the new employer is automatically substituted in the place of the old employer in all contracts of employment in existence immediately before the old employer's provisional winding-up or sequestration;

(b) all the rights and obligations between the old employer and each *employee* at the time of the transfer remain rights and obligations between the old employer and each employee;

(c) anything done before the transfer by the old employer in respect of each *employee* is considered to have been done by the old employer;

(d) the transfer does not interrupt the *employee's* continuity of employment and the employee's contract of employment continues with the new employer as if with the old employer."

[16] The consequences of the introduction of section 197A (1)(b) and (c) of the LRA is that despite the provisions of the Insolvency Act 24 of 1936, if a transfer of a business takes place in circumstance where the old employer is insolvent or if a scheme of arrangement or compromise is concluded to avoid winding-up or sequestration, anything done before the transfer by the old employer in respect of each employee is considered to have been done by the old employer. This is different to section 197 of the LRA, where 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. Put in another way, the evocation of section 197A(1)(a) and (b) read with subsection (1) (c) of the LRA, is that the new employer does not automatically substitute the old employer in all contracts of employment except for those in existence

immediately before the old employer's provisional winding-up or sequestration. In this respect, the LAC in *Hydro Colour Ink v CEPPWAWU*[1], held that:

> … Section 197A in so far as it states that the new employer is automatically substituted in the place of the old employer in all contracts of employment in existence immediately before the old employer's winding up or sequestration finds application. It must be emphasised that the automatic substitution only relates to all "*contracts of employment"* in existence immediately before the old employer's winding up or sequestration. This means that the new employer takes no responsibility for the actions of the old employer. By way of an example, any wrongful dismissal by the old employer remains a matter for the old employer."

[17] It is apparent from the reading of section 197A of the LRA that its provisions may, in a transfer of business as a going concern, be triggered in two ways, namely where:

a) if the old employer is insolvent; or

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

<u>The old employer being insolvent</u>

[18] In my view, the provisions of section 197A (1)(a) of the LRA applies where there has been insolvency in the legal technical sense. In terms of the old Act, insolvency occurs when in the technical sense an application to have the company declared insolvent is made and the Court endorses such an application. It needs to be pointed out that the burdensome procedure provided for under the old Act has now been done away with by the Companies Act of 2008 which came into operation in 2011. I will revert to the provisions of section 311 of the old Act latter in this judgment.

[19] In the present matter the transfer of the business occurred before the new Act came into operation and therefore the provisions of the old Act apply.[2]

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[1] *Hydro Colour Ink v CEPPWAWU* JA 48/07 & JA 77/09

[2] *It is no longer necessary under the 2008 Company's Act to have the endorsement of the Court in order to have a company declared insolvent.*

[20] It has been held in *Waverly Blankets v CCMA and Others*[3] that the legislature never intended, with the provisions of section 197A of the LRA to undermine the provisions of section 311 of the Company's Act whenever a company is rescued from insolvency.

[21] The provisions of section 197A (1) (a) of the LRA is triggered when there has been compliance with the provisions of section 311 of the old Act. A company is regarded as insolvent upon a successful application in terms of section 311 of the old Act. In the present instance as would appear from the earlier discussion the third respondent did not base its case on the provisions of section 197A (1) (a) but on (b). The question that then arises is whether the provisions of section 311 of the old Act apply to subsection (b) of section 197A (1) of the LRA. In other words do the provisions of section 311 of the old Act apply in circumstances where the transfer of a business as going concern occurs as a result of an arrangement or a compromise?

[22] It is important before considering the question of whether the provisions of section 311 of the old Act apply to situations involving transfer of a business as a result of an arrangement or a compromise to consider the meaning of the concepts of arrangement and compromise. This approach is adopted in order to address the submission which was made on behalf of the third respondent that a scheme of arrangement can be concluded or an arrangement can be made under common law. As I understood the submission, it is based on the proposition that where a compromise or arrangement is made in terms of the common law, then there is no need to comply with the provisions of section 311 of the old Act on the facts of this case. I do not agree with that proposition for the reasons that appear later in this judgment. In brief, my view is that the provisions of section 311 of the old Act apply to both the transfer of a business in terms of both section (a) and (b) of section 197A (1) of the LRA.

[3][2003] 2 BLLR 236 (LAC)

The concept of arrangement

[23] The concept of compromise is defined by Christie inThe Law of Contract in South Africa as follows:

> 'Compromise, or *transactio,* is the settlement by agreement of disputed obligations, whether contractual or otherwise.'

And Hosten *et al* in Introduction to South African Law and Legal Theory (page 765 at 1.5.) defines compromise as follows:

> 'A compromise or *transactio* is an agreement between two or more parties aimed at terminating the dispute between them. The dispute may be between litigants, but litigation, current or pending, is not a requirement. The compromise agreement must of course comply with all the requirements for a valid contract and may lead to the creation of obligations. Very often a compromise concerns an existing obligation. . .' [4]

[24] According to the Oxford Dictionary the word 'Compromise," means to settle disputes by mutual concessions.

[25] The theme that runs through the above definitions is that a compromise is reached when the parties resolves a dispute or reaches a consensus on how to resolve a disputed obligation which may have given rise to litigation between the parties.

[26] In the present instance, the third respondent seems to have based its case, that there was a compromise, on the provisions of the sale agreement relating to the litigation between third respondent and Mondi Papers Limited and the loan given to the first respondent by Mr Gargassouls. The loan and the issue of the Mondi litigation in my view, far from being a compromise constitute nothing but the ordinary terms and conditions of a business transaction. There is no evidence

[4] *See also Carson v Minister of Public Works* 1996 (1) SA 887 E and page 893 F-H

that there was a dispute between the first respondent and Mr Gargassouls, regarding the payment of the loan.

Scheme of arrangement

[27] The scheme of arrangement is usually used to rearrange the rights of creditors and members where the company is faced with financial difficulties that could result in it going under sequestration. It is usually a method for achieving consensus amongst the stakeholders in particular in relation to the sale of shares. Any scheme of arrangement made, will take effect once approved by the Court under the old Act.

[28] Similar to the issue of compromise which the third respondent sought to rely on, the existence of the scheme of arrangement that it seeks to rely on, is not supported by the objective facts. In my view, there is insufficient evidence to sustain the contention that the member's loan and the Mondi litigation constitute an arrangement that would qualify under section 197A(1)(b) of the LRA.

[29] Turning to the provision of section 311 of the 1973 Company's Act, it reads as follows:

> 'Where any compromise or arrangement is proposed between a company and its creditors or any class of them, or between a company and its members ,the court may, on application of the company or any credit member of the company, or in the case company being wound up, of the liquidator, or if the company is subject to judicial management order, the judicial manager, order a meeting of the company or class creditors, or the members (as the case may be), to be summoned in such matter as the court may deem fit or direct.'

[30] Henochsberg on Company Act 71 of 2008, in dealing with the provisions of section 197A of the LRA correctly observed that:

> 'Section 197(A) of the LRA regulates transfer of a business which takes place pursuant to a scheme of arrangement or compromise which is entered into in order to avoid winding-up for reasons of insolvency, and provided that such a

transfer entails that all employment contracts of the employees of the relevant business are to be transferred from the "old employer" Although specific reference is not made to S311 of the Companies Act, it is submitted that as 197(A) is intended to apply not only to a compromise of scheme implemented in terms of Section 311 but also in respect of common law arrangements and compromise'(my underlining).

[31] In *Waverly Blankets Ltd v CCMA and Others*,[5] held that:

'I can see no fundamental conflict between section 311 of the Companies Act and the provisions of the Labour Relations Act. Section 311 has been on the statute book for many years and it serves a useful purpose, especially when companies run into trouble. That is demonstrated by the facts of the present case. It seems unlikely that Parliament, when enacting the Labour Relations Act, intended to undermine section 311 whenever a company, being rescued from insolvency, has employee creditors and a collective agreement, which is often the case. In the standard type of section 311 arrangement with the creditors, the employees will have a vote as creditors, which they can exercise for or against the proposed scheme according to their best interests. I do not think that the legislature intended to take that opportunity away from them or to preclude the opportunity for compromise afforded by section 311. In this case it was open to the dismissed employees, as creditors, to seek to persuade, first the majority in the creditors meeting, and, secondly, the High Court, that disputes such as the dismissal disputes be referred to arbitration. They did not do so.'

Evaluation

[32] The central issue for determination in this matter is whether the sale agreement constitutes a scheme of arrangement or a compromise which triggered the provisions of Section 197A(1)(a) read with subsection (2)(c) of the LRA.

[33] There seems to be no doubt that the purchase of the businesses was on the basis of an on-going concern. The fact that the businesses of the first and second respondents were purchased as going concern is spelt out very clearly in

[5] (2003) 2 BLLR 236 (LAC) at paragraph 35.

the number of clauses in the agreement. It is clear from the clauses of the agreement that the sale of the business was on the basis of a going concern and more importantly for the purpose of this judgment, provision was made for the transfer and the takeover of employees. The contention of the third respondent is that this does not include the applicant because he was not in its employ immediately when the sale took effect.

[34] In addition to what is stated earlier, the third respondent's argument is also based on clause 19.1 of the sale agreement wherein it is stated that the business is sold in terms of section 197(A) of the LRA.

[35] In my view, clause 19.1 of the sale agreement is nothing but a label which has no legal force and effect in the absence of facts to the contrary. It is only through the objective facts that a determination can be made that the provisions of section 197A of the LRA has been triggered.[6]

[36] It should be noted that section 197(A) does not prescribe what form the scheme of the arrangement or compromise should take. The interpretation of the section, as to what form the scheme of arrangement should be, is informed by the objective that the legislature sought to achieve. There are two objectives which the legislation sought to address through the provisions of section 197A. The first objective is to protect the employment of employees faced with transfer of business in circumstances where the old employer is insolvent. The other objective is to avoid burdening employers who seek to rescue insolvent companies with employment contract of employees who were not in the employ of the old employer immediately on the effective date of the transfer of the business.

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[6] *See NEHAWU v University of Cape Town* (2003) 24 ILJ 95 (CC) and *Aviation Union of South Africa (Pty) Ltd* (2011) 32 ILJ 2861 (CC) *at paragraph 47 where Jafta J in dealing with the provisions of section 197 of the LRA had the following to say: "But whether a transfer as contemplated in section 197 has occurred or will occur is a factual question. It must be determined with reference to objective fact of each case."*

[37] In my view, having regard to the objectives of the legislature and the phrase, “avoiding winding-up or sequestration for reason of insolvency,” there seem to be no doubt that this brings the provisions of section 197A(1)(b) of the LRA within the jurisdiction of section 311 of the old Act. This means for a scheme of arrangement or comprise to trigger the provisions of section 197A(1)(b) of the LRA there should be evidence of compliance with the provisions of section 311 of the old Act.

[38] In light of the above discussions, I find that the objective facts do not support the contention of third the respondent that the provisions of section 197A(1)(a) of the LRA has been triggered. I have already indicated earlier that the question of whether section 197 of the LRA applies is a question to be considered in the main claim and not in this interlocutory application.

[39] I see no reason in law and fairness why costs should not follow the results.

Order

[40] In the circumstances, the third respondent’s preliminary point is dismissed with costs.

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E Molahlehi

Judge of the Labour Court of South Africa

APPEARANCES:

For the Applicant: Advocate M A Lennox

Instructed by: Goldberg Attorneys

For the Respondent: Claudio Bollo of Biccari Bollo Mariano Inc