

**TRANSFER OF BUSINESS, TRADE OR UNDERTAKING AND ITS EFFECTS ON  
CONTRACTS OF EMPLOYMENT**

**By**

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Submitted in fulfilment of the requirements for the degree of

**MASTER OF LAW**

in

**LABOUR LAW**

in the

**FACULTY OF MANAGEMENT SCIENCES AND LAW**

at the

**UNIVERSITY OF LIMPOPO**

**SUPERVISOR: Prof JHL Letsoalo**

**2010**

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## **Declaration by Supervisor**

(i)

I hereby declare that this dissertation by candidate student number 8500393, Glynn Stephen Mabuela Mohlabi, entitled "Transfer of Business, Trade or Undertaking and its Effects on Contracts of Employment", for the degree Master of Laws in the Department of Labour Law, be accepted for examination.

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Professor JLH Letsoalo

### **Declaration by Candidate**

(ii)

I declare that this dissertation for the degree Master of Laws hereby submitted, has not been previously submitted by me for a degree at this or any other university, that it is my work in execution and design and all the material contained has been duly acknowledged.

---

Glynn Stephen Mabuela Mohlabi

## **Acknowledgements**

(iii)

I acknowledge the assistance and guidance of my supervisor, Professor JLH Letsoalo who sacrificed his time to ensure that this dissertation becomes a success. Our academic relationship dates back to 1986 when I was a student in the Constitutional and Administrative Law course he lectured. I am privileged to have completed this dissertation under his supervision. I also acknowledge my family who have been supportive of my quest to improve my studies. I thank God for everything.

## TABLE OF CASES

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1. *AST Holdings (Pty) Ltd v Roos* (2007) 28 ILJ 1988 (LAC)
2. *Aviation Union of South Africa and Another v S.A. Airways (Pty) Ltd and Others* (2008) 29 ILJ 331 (LC)
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4. *Botha v Carapax Shadeports (Pty)Ltd* 1992 (1) SA 202 (A)
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9. *Kebeni and Others v Cementile Products (Ciskei) (Pty)Ltd and Another* (1987) 8 ILJ 442 (IC)
10. *Kgethe and Others v LMK Manufacturing (Pty)Ltd* (1997) 10 BLLR 1303 (LC)
11. *LMK Manufacturing (Pty)Ltd v Kgethe and Others* (1998) 3 BLLR 248 (LAC)
12. *Ndimma and Others v Waverly Blankets Ltd* (1999) 20 ILJ 1563 (LC)
13. *NEHAWU v University of Cape Town and Others* (1)(2000) 7 BLLR 803 (LC)
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15. *NEHAWU v University of Cape Town and Others* (2003) 2 BCLR 154 CC
16. *NUMSA and Another v Success Panelbeaters* (1999) 9 BLLR 970 (LC)
17. *Pama and Others v CCMA and Others* (2001) 9 BLLR 1079 (LC)
18. *PPWAWU and Others v Kayccraft (Pty) Ltd* (1989) 10 ILJ 272 (IC)
19. *Rubin Sportswear v SACTWU and Others* (2004) 25 ILJ 1671 (LAC)

20. *SAAPAWU v HL Hall and Sons (Group Services)* (1999) 2 BLLR 164 (LC)
21. *S.A. Commercial Catering and Allied Workers Union and Others v Western Province Sports Club t/a Kelvin Grove and Another* (2008) 29 ILJ 3038 (LC)
22. *Schutte and Others v Powerplus Performance (Pty) Ltd* (1999) 2 BLLR 169 (LC)
23. *Securicor (SA) (Pty) Ltd and Another v Lotter and Others* (2005) 10 BLLR 1032 (E)
24. *South African National Security Employers Association v TGWU and Others (1)* (1998) 4 BLLR 364 (LAC)
25. *Telkom SA Ltd and Others v Blom* (2003) 7 BLLR 638 (SCA)
26. *TGWU v Putco Ltd* (1987) 8 ILJ 801
27. *Transport Fleet Maintenance and Another v NUMSA* (2003) 10 BLLR 975 (LAC)
28. *Van der Velde Business Design Software (Pty) Ltd and Another* (2006) 27 ILJ 1225 (LC)



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### SOUTH AFRICA

<b>NO</b>	<b>YEAR</b>	<b>SHORT TITLE</b>
75	1997	Basic Conditions of Employment Act
61	1973	Companies Act
108	1996	Constitution of the Republic of South Africa Act
55	1998	Employment Equity Act
24	1936	Insolvency Act
28	1956	Labour Relations Act
66	1995	Labour Relations Act
24	1956	Pensions Act

### OTHERS

<b>NO</b>	<b>YEAR</b>	<b>SHORT TITLE</b>
28	2009	Fair Work Act (Australia)
1794	1981	TUPE Regulations (United Kingdom)

## **CHAPTER 1**

### **INTRODUCTION AND BRIEF HISTORICAL BACKGROUND**

#### **1.1. Introduction**

It often happens that employers for various reasons decide to sell, merge or donate their businesses or are forced by reasons of insolvency to close shop. In such situations the question that normally arises is: "What happens to the contracts of employment of their employees?"

This is also one of the questions the labour law tribunals have had to grapple with over years seemingly with no clear answers on certain aspects raised in transfers of businesses or undertakings. Despite the difficulties encountered, these tribunals have contributed a lot in shaping the law on transfers of businesses, trades or undertakings to what it is today. One appreciates the efforts of all those who have applied their minds positively towards creating certainty on issues of transfers of businesses, trades or undertakings.

#### **1.2. Common law**

At common law the relationship between an employer and an employee is seen as a contract between two parties. The nature of the relationship is such that it inhibits freedom to contract between the two parties as in most cases the parties are not on an equal bargaining footing. The employer is, naturally, more economically powerful and tends to use this as a bargaining tool in as far as the relationship is concerned.

The common law position is that an employee is not obliged to continue his or her contract of employment with the purchaser of the business. On the other hand the purchaser is not obliged to employ the employee. A transfer of a business would most probably mean the termination of contracts of employment.<sup>1</sup>

Basson AC *et al* say:

“When a business is sold, the position of employees in terms of common law is deceptively simple: No employee may be forced to continue his or her contract of employment with the new employer. This, of course, is cold comfort to most of employees who would like to stay on (especially in a country with high unemployment) because the common law also provides that the new employer is not obliged to employ them. A transfer of a business could well mean the termination of existing employment contracts. As far as insolvency is concerned the rule is that insolvency of the employer terminates existing contracts of employment. Despite this, it is a fact of economic life that an insolvent business does not necessarily cease to operate as it may still be bought by another concern and given a life-line, or some arrangement with creditors may ensure its survival.”<sup>2</sup>

### **1.3. Influence of the Industrial Court**

The Labour Relations Act 1956<sup>3</sup> did not have specific provisions regulating transfers of business, trade or undertaking. Despite this deficiency, the Industrial Court adopted an employee protection approach when dealing with transfers of business, trade or undertakings.<sup>4</sup>

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<sup>1</sup> Du Toit D, Bosch D, Woolfrey D, Godfrey S, Rossouw J, Christie S, Cooper C, Giles G with Bosch C *Labour Relations Law: A Comprehensive Guide* 4<sup>th</sup> Lexis Nexis Butterworths (2003) 427.

<sup>2</sup> Basson AC, Christianson MA, Garbers C, Le Roux PAK, Mischke C and Strydom EML *Essential Labour Law: A new combined edition in one volume* Labour Law Publications (2005) 171.

<sup>3</sup> Act No 28 of 1956.

<sup>4</sup> Footnote 1 at 427.

In *Kebebi & Others v Cementile Products (Ciskei) (Pty) Ltd & Another*<sup>5</sup>, where the employer alleged intimidation as the reason for termination of contracts of employment and closing down of business, the Court found that resentment of trade union activities in the factory was the main reason for closure. The Court found that the take-over of the employer's business by a company registered in Ciskei where trade unions might not operate legally, afforded the company an excellent excuse for putting off all discussions with the union. The Court found it strange that no disciplinary action was taken for alleged delinquent behaviour of intimidation.

The Court concluded that the respondent had neglected or failed to observe essential canons of fair play on all key issues relating to retrenchment of its workforce, such as reasonable and sufficient notice, consultations in good faith with employees or their representatives, disclosure to them of the relevant and necessary information, and the adoption of legal measures to ensure that none of the employees would lose their jobs as a result of closure of the factory of the first respondent. The court found that the second respondent had acted unfairly and granted reinstatement. The Court had this to say:

"If it is intended to transfer the undertaking and/or its major assets such as plant and machinery of the employer (transferor), safeguards should be incorporated into the agreement between the parties to ensure that the interests of the workforce are adequately protected. One of the safeguard clauses could for example be that all existing contracts of employment could be deemed to have been transferred to the new employer who would be obliged to retain all existing employees without discrimination, save that an individual employee may have an option not to continue his employment relationship with the transferee."<sup>6</sup>

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<sup>5</sup> (1987) 8 ILJ 442.

<sup>6</sup> At 450. See also *TGWU v Putco Ltd (1987) 8 ILJ 801*, *PPWAWU and Others v Kaycraft (Pty) Ltd (1989) 10 ILJ 272 (IC)*.

This comment confirms the employee protection approach adopted by the Industrial Court.

#### **1.4. The Constitution and other pieces of legislation**

The advent of the Constitution of the Republic of South Africa Act<sup>7</sup> (hereinafter referred to as the 'Constitution') has reinforced the notion of fair labour practices.

Section 23 of the Constitution introduces the right to fair labour practices, to participate in trade union and employers' organisation activities. The section clearly provides that everyone is entitled to these rights. These rights are not limited to South Africans as the section clearly extends the right to everyone. The right to fair labour practices applies equally to both employers and employees.<sup>8</sup> Employers and employees have to comply with this section when transfers are being effected.

Todd *et al* say:

"One of the LRA's purposes is to give content to section 23 of the Constitution. It must therefore be construed and applied consistently with that purpose and in compliance with the Constitution. This means that the proper interpretation and application of the LRA raises a constitutional issue that falls within the jurisdiction of the Constitutional Court."<sup>9</sup>

Ever since the Constitution came into operation, pieces of legislation have been enacted to deal with labour relations matters. Of note are

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<sup>7</sup> Act No 108 of 1996.

<sup>8</sup> Van Niekerk A, Christianson MA, MacGregor M, Smit N and Van Eck BPS *Law @ work* 1<sup>st</sup> ed (2008) 171.

<sup>9</sup> Todd C, Du Toit D, Bosch C *Business Transfers and Employment Rights in South Africa* (2004) 14.

the Labour Relations Act<sup>10</sup>, the Basic Conditions of Employment Act<sup>11</sup> , and Employment Equity Act<sup>12</sup>, to mention a few.

The Labour Relations Act is intended to give effect to and regulate the fundamental rights to fair labour practices conferred by section 23 of the Constitution. It provides a framework within which employees and their trade unions, employers and their employers' organisations can collectively bargain to determine wages, terms and conditions of employment and other matters of mutual interest. It is also aimed at promoting collective bargaining, employee participation in the decision-making in the workplace and effective resolution of labour disputes.

The purpose of the Basic Conditions of Employment Act is to give effect to the right to fair labour practices referred to in section 23 of the Constitution by establishing and making provision for the regulation of basic conditions of employment and thereby to comply with the obligations of the Republic of South Africa as a member state of the International Labour Organisation.

The Employment Equity Act aims at achieving equity in the workplace by promoting equal opportunity and fair treatment in employment by elimination of unfair discrimination and to redress disadvantages created by unfair discrimination.

The common thread in these Acts is that they draw their strength from section 23 of the Constitution.

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<sup>10</sup> Act No 66 of 1995.

<sup>11</sup> Act No 75 of 1997.

<sup>12</sup> Act No 55 of 1998.

### **1.5. International Standards: A comparative analysis**

In the United Kingdom there are the Transfer of Undertakings (Protection of Employment) Regulations of 1981, commonly known as the TUPE regulations, also regulating transfers of employees.

According to David Royden<sup>13</sup> the regulations are designed to preserve the employees' terms and conditions of employment when a business or undertaking, or part of one is transferred to a new employer. The regulations have an effect that employees employed by the previous employer when the undertaking changes hands automatically become employees of the new employer on the same terms and conditions. It is as if their contracts of employment had originally been made with the new employer. The employees' continuity of employment is preserved, as are their terms and conditions of employment. The new employer takes over the contracts of employment of all the employees who were employed in the undertaking immediately before the transfer, or who would have been so employed if they had not been unfairly dismissed for a reason connected with the transfer. The new employer also takes over all rights and obligations from those contracts of employment, except criminal liabilities and rights and obligations relating to provisions about old age, invalidity or survivors connected with the employees' occupational pension schemes. Neither the new employer nor the previous employer may fairly dismiss an employee because of the transfer or a reason connected with it, unless the reason for dismissal is economic, technical, organisational reason entailing changes in the workforce. If there is no such reason, the dismissal will be unfair.

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<sup>13</sup> <http://www.roydens.co.uk/content/13.htm> "Transfer of undertakings" (accessed on 25/07/2007).

Transferred employees who find that there has been a fundamental change for worse in their terms and conditions of employment as a result of the transfer generally have the right to terminate the contract and claim unfair dismissal on the grounds that the action of the employer has forced them to resign. An employee's period of continuous employment is not broken by a transfer, and for purposes of calculating statutory employment rights, the date on which the period of continuous employment started is the date on which the employee started work with the old employer. In the case of a transfer the previous and new employers must inform and consult representatives of employees. The TUPE regulations 1981 were revised in 2006 and now cover, amongst others outsourcing transactions.

In Australia the recently passed Fair Work Act<sup>14</sup> regulates transfer of businesses and other employment relations matters. The Act provides that there is transfer of a business from the old employer to the new employer if the employment of an employee of the old employer has terminated and within three months after termination, the employee becomes employed by the new employer, the work (the transferring work) the employee performs for the new employer is the same or substantially the same, as the work the employee performed for the old employer. If these requirements are met there has been a transfer of the business and an employee in relation to whom these requirements have been satisfied.

A transfer takes place through a transferrable instrument which may be in the form of an enterprise agreement that has been approved in terms of the Act, a workplace determination or a named employer award. If the transferrable instrument covered the transferring employee and the old employer immediately before the termination of

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<sup>14</sup> Act 28 of 2009.



the employee's employment the transferrable instrument covers the new employer and the transferring employee in relation to the transferred work after the transfer of the employee and no further enterprise agreement or named employer award that covers the new employer covers the transferring employee in relation to that work. If the new employer employs a new employee after the transferrable instrument starts to cover the new employer and the new employer employs a non- transferring employee who performs the transferring work and there is no other agreement that covers the non-transferring employee, then the transferrable instrument covers the non-transferring employee. There are specific provisions dealing with circumstances where the old employer had given guarantee of annual earnings for a guaranteed period to a transferring employee<sup>15</sup>.

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<sup>15</sup> Section 328

## CHAPTER 2

### SECTION 197 OF THE LABOUR RELATIONS ACT 66 OF 1995

#### 2.1. The old section 197 of the Labour Relations Act 66 of 1995

The Labour Relations Act of 1956 was replaced by the Labour Relations Act of 1995. The transfer of business, trade or undertaking is now regulated by section 197 of the Labour Relations Act 1995 which was subsequently amended in August 2002. The earlier section 197 started by prohibiting the transfer of a contract of employment from the old employer to the new employer without an employee's consent. It then went on to provide for two scenarios where a business could be transferred without an employee's consent. The first was where the whole or any part of a business was transferred as a going concern. The second was an insolvency transfer where the whole or part of a business was transferred as a going concern if the old employer was insolvent and being wound up or was being sequestrated or some scheme of arrangement was being entered into to avoid being wound up or sequestrated.

The consequences of a transfer in circumstances other than insolvency were that unless otherwise agreed, all rights and obligations between an old employer and each employee at the time of the transfer continue in force as if they had been rights and obligations between the new employer and each employee and anything done before the transfer by or in relation to the old employer would be considered to have been done by or in relation to the new employer. The new employer actually stepped into the shoes of the old employer.

In the case of an insolvency transfer the consequences were that unless agreed otherwise, the contracts of employment of all the employees that were in existence immediately before the winding up or sequestration of the old employer transferred automatically to the new employer. All the rights and obligations between the old employer and each employee, and anything done before the transfer by the old employer in respect of each employee would be considered to have been done by the old employer. In this instance only employees transferred but rights and obligations did not.

An agreement envisaged in subsection 2 of section 197 could be concluded with an appropriate person or body referred to in section 189(1) of the Act to avoid the consequences of subsection 2. This meant that the consequences of subsection 2 of section 197 could be circumvented by concluding an agreement in terms of section 189.

A transfer in terms of the section did not interrupt continuity of employment and employment continued with the new employer as if with the old. The section concluded by exempting liability of any person to be prosecuted for, convicted of, and sentenced, for any offence.

The criticism of this section by the courts and other legal authorities was that it contained words or phrases that were not defined and therefore capable of different interpretations. Words such as “business” and “going concern” were not defined. A further criticism of the section was that it did not address the conflict between itself and section 38 of the Insolvency Act<sup>16</sup> as in terms of the latter contracts of employment terminated on insolvency.<sup>17</sup>

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<sup>16</sup> Act No 24 of 1936.

<sup>17</sup> Grogan J *Dismissal Discrimination and Unfair Labour Practices* 2<sup>nd</sup> ed (2007) 497.

In *Schutte and Others v Powerplus Performance (Pty) Ltd and Another* the court was critical of the draftsmanship of section 197 and had the following to say:

“Given the fundamental conflict of interest addressed in section 197 it is regrettable that its provisions are so terse. Perhaps it is inevitable since the section strikes at the very heart of that conflict and the Act, in its final form, is a product of a negotiated agreement between organised labour and capital, the representatives of conflicting interests. The provisions of section 197 are part of mechanisms designed to provide security of employment in times of change. They give effect to the constitutional right to fair labour practices in situations of business restructuring and reorganisation of employment and must be interpreted in this context.”<sup>18</sup>

## **2.2. The amended section 197**

The old section 197 was widely criticised and some further criticism is found in the statement by Bosch which reads as follows:

“The purpose of this note is to examine the decisions of the Labour Court and the Labour Appeal Court in the matter between the National Education, Health and Allied Workers Union (NEHAWU) and the University of Cape Town (UCT) through a critical lens. They provided an ideal opportunity for the courts to give us guidance on the application of a poorly drafted thus difficult section in a manner that gives effect to its primary purpose.”<sup>19</sup>

The amended section 197 attempts to close the loopholes observed in the old section. The section defines words such as “business” and “transfer” in an attempt to be more precise. Unfortunately one finds the definitions of little help. The word ‘business’ remains undefined save to mention what it includes. The definition of “transfer” is also confusing because it makes reference to ‘business’ which is not properly defined

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<sup>18</sup> (1999) 2 BLLR 169 (LC) at 179 para 31 of the report.

<sup>19</sup> Bosch C “Two wrongs make it more wrong or a case of minority rule” (2002) SALJ 501 at 502.

and 'a going concern' which is also not defined.<sup>20</sup> The amended section 197 makes separate provision for transfers in the normal course and transfer in case of insolvency.

Unlike its predecessor, the amended section 197 provides that the new employer complies with subsection (2) if that employer transfers employees on terms and conditions that are on the whole not less favourable to the employees than those on which they were employed by the old employer. This is a result of difficulties experienced where employees, at times, wanted to be put on exactly the same terms and conditions as with the old employer. This does not apply where there is a collective agreement regulating conditions of employment.

The section permits the transfer of an employee to a pension, provident, retirement or similar fund if the criteria set in section 14(1) (c) of the Pension Funds Act<sup>21</sup> are met.

Any arbitration award made in terms of the Act, the common law or any other law; any collective agreement in terms of section 23 of the Act and any collective agreement binding in terms of section 32 unless a commissioner acting in terms of section 62 decides otherwise, binds the new employer unless otherwise agreed in terms of subsection 6 of section 197.

Subsection 6 of section 197 envisages where an agreement on the terms of the transfer is concluded by the relevant parties and such agreement must be in writing. The employer is required to disclose all the information that will allow effective engagement in negotiations.

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<sup>20</sup> See Du Toit D *et al op cit* 428.

<sup>21</sup> Act No 24 of 1956.

Subsection 7 of section 197 provides that the old employer must agree with the new employer on valuation of leave pay, severance pay and other payments that may have accrued to the transferred employees but have not been paid to employees of the old employer and who of the employers is liable for payment. The terms of such an agreement must be disclosed to each employee who after the transfer becomes employed by the new employer. This literally means that the terms must be disclosed to each employee who after the transfer becomes an employee of the new employer regardless of whether the employee is a transferring employee or not.

The old and new employer are for a period of twelve months after the transfer jointly and severally liable to any employee who becomes entitled to receive payment contemplated in section 7(a) as a result of the employee's dismissal for a reason relating to the employer's operational requirements or the employer's liquidation or sequestration, unless the old employer is able to show that it has complied with the provisions of this section. This is a further safeguard for the interests of an employee.

Subsection 9 of section 197 provides that the old and new employer are jointly and severally liable in respect of any claim concerning any term or condition of employment that arose prior to the transfer. Todd *et al*<sup>22</sup> say that it is not immediately clear whether or not claims arising from acts described in section 197(2)(c) may properly be described as claims "concerning any term or condition of employment."

Like the old section 197 this section does not affect liability of any person to be prosecuted for, convicted of, and sentenced for, any offence.

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<sup>22</sup> Footnote 9 at 89.

### **2.3. Section 197A**

This section was introduced with the amendment of section 197 in August 2002. It deals with transfers of business in cases of insolvency of the old employer; or if a scheme of arrangement or compromise is being entered into to avoid winding up or sequestration for reasons of insolvency. The section commences by declaring its independence of the Insolvency Act and provides that if a transfer of a business takes place in circumstances contemplated in subsection (1) unless otherwise agreed in terms of section 197(6) the new employer automatically substitutes the old employer in respect of all contracts of employment in existence immediately before the old employer's provisional winding up or sequestration. The rights and obligations between the old employer and each employee at the time of the transfer remain the same between the old employer and each employee. Anything done by the old employer in respect of each employee is considered to have been done by the old employer. The transfer does not interrupt continuity of employment. Section 197(3), (4), (5) and (10) applies to a transfer in terms of this section.

### **2.4. Section 197B**

Importantly, section 197B places an obligation on an employer facing financial difficulties that might reasonably result in winding up or sequestration to advise the consulting party in terms of section 189(1) and an employer that applies to be sequestered, whether in terms of the Insolvency Act, 1936 or any other law, must at the time of making the application, provide the consulting party in section 189(1) with a copy of the application. An employer who receives an application for its winding up or sequestration must supply a copy of the application to the consulting party within two days of receipt.

## 2.5. Interpretation of section 197

### 2.5.1. Transfers in the normal course

#### 2.5.1.1. Transfer

The word 'transfer' is not defined in both the old and amended section 197. In *Schutte and Others*<sup>23</sup> the court was of the view that the issue to be decided was whether the second respondent transferred any part of its business, trade or undertaking to the first respondent as a going concern, as contemplated in the old section 197(1) (a) of the Act. It concluded that the Act must be read in a constitutional context and that sections 1(a) and 3(b) of the Act required the Labour Appeal Court to follow this approach.<sup>24</sup> The court also found that a transfer does not take place only in the case of a sale transaction. It found that a transfer can take place in the context of restructuring, merger and other forms. This seems to me to be the correct approach.

Van Niekerk *et al* say:

"The concept of 'transfer' thus relates to the method of transfer of a business.

Business transfers occur most often consequent to a sale, but the reach of section 197 clearly extends beyond transfers effected in these circumstances. Any corporate event such as a merger, take over, or other restructuring potentially falls within the ambit of section 197, as does an exchange of assets, a donation and outsourcing of non-core functions or business activities. For there to be a transfer, there must be a shifting of a business entity by one employer to another. This assumes that there must be at least two distinct employers involved in the transaction."<sup>25</sup>

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<sup>23</sup> Footnote 18.

<sup>24</sup> See also *South African National Security Employers Association v TGWU and Others* (1) (1998) (4) BLLR 364 at para 21, *Ceramic Industries and Another v NCBAWU and Others* (1997) 6 BLLR 697 (LAC) at 699-709D.

<sup>25</sup> Footnote 8 at 303.



I agree with this statement to the extent it does not include outsourcing and I will provide reasons why outsourcing should not be included within the meaning of section 197 at the conclusion of this dissertation.

### **2.5.1.2. Business**

The section defines 'business' as including the whole or a part of any business, trade, undertaking or service. As indicated earlier it does not actually define 'business' but rather states what it includes. 'Business' was not defined in the old section 197.

Todd *et al* correctly point out as follows:

“According to section 197(1) (a) a “business” includes the “whole or a part of any business, trade, undertaking or service”. “Business” and “trade” could be taken to indicate a commercial enterprise aimed at the generation of profit. But “undertaking” and “service” could also refer to entities of a non-commercial nature. The fact that section 197 is not limited in its scope to commercial ventures is reinforced by the fact that it applies to both private and public sector transfers. The scope of the definition of “business” is extended by the fact that what might constitute business for purposes of section 197 is not limited to the entities listed in section 197(1)(a). That much is apparent from the fact that for the purposes of section 197 a “business” *includes*, but is by implication not limited to, the entities specifically mentioned. The ambit of section 197 is further extended by the fact that it will not only apply to the transfer of the whole of a business, trade, undertaking or service, but also any part thereof.

“Business” is a rather chameleon-like word, “notorious for taking its colour and its content from its surroundings”. What will constitute a business for the purposes of the application of section 197 necessarily relate to the particular facts of each case.”<sup>26</sup>

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<sup>26</sup> Footnote 9 at 32.

I agree with this view.

### **2.5.1.3. Going concern**

No attempt was made in both the old and amended section 197 to define the phrase “going concern” yet it is an important aspect of transfers in terms of section 197.

In *Kgethe & Others v LMK Manufacturing (Pty) Ltd*<sup>27</sup> the first respondent, after experiencing economic difficulties, decided to sell a portion of its assets to the fourth respondent. The applicants wanted the disclosure of certain information related to the sale disclosed so as to enable them to determine whether a transfer in terms of section 197 had taken place or not. The court concluded that the first respondent was obliged to terminate the services of the applicants and that what had happened was a sale of the first respondent's assets and consequently section 197 was of no application and therefore no entitlement to information bearing on non-compliance with the provisions of the section. It is submitted that the importance of the disclosure of the required information would put the applicants in a position to determine whether the sale fell within the scope of section 197 and thereafter decide whether to exercise their rights or not.

What is puzzling is the following statement by the court:

“In this case it is clear to me that the business of the first respondent has not been transferred as a going concern to the fourth respondent. Consequently section 197(1) is of no application. This means that the first respondent is correct in arguing that it is obliged to terminate the services of the applicants with effect from 30 June 1997. There may, of course, be an argument that this dismissal was unfair but this is not an appropriate forum to consider the fairness

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<sup>27</sup> (1997) 10 BLLR 1303 (LC).

of those dismissals. The purchaser had indicated that it had wished to employ at least the permanent employees of the first respondent. As there had been no cession or transfer of contracts, the respondent is entitled to bargain for new terms and conditions of employment. It may be that the fourth respondent has made certain representations as to what will be contained in those contracts in comparison to the contracts which existed between the first respondent and the applicants or some of them. If that is the case civil proceedings may be warranted but that is no business of this court."<sup>28</sup>

The court's approach appears to me to have been a bit simplistic. It came to the conclusion that the first respondent's business had not transferred as a going concern without taking into account factors such as offers of re-employment, undertakings to jobs of permanent staff and the nature of the sale agreement as relevant.

Not surprisingly, applicants appealed to the Labour Appeal Court<sup>29</sup> which found that without the alleged agreement between the respondents and certain documentation being placed before the court *a quo* it was not permissible for that court to determine if and when an agreement was concluded or what the effect of the agreement was. The Labour Appeal Court went on to state that a number of reasons were present why the appellants legitimately apprehended that the agreement concluded by the respondents might in fact have had the effect of transfer of the first respondent or part thereof as a going concern. The Labour Appeal Court found that on a number of occasions various descriptions were applied to the agreement and its effects which were quite appropriate if in fact a transfer as a going concern had been effected. At one stage the union was advised that not only were the first respondent's assets being acquired but that its liabilities would be discharged and business was immediately commenced on the same premises where the first

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<sup>28</sup> Footnote 27 at 1309.

<sup>29</sup> (1998) 3 BLLR 248 (LAC).

respondent conducted its operations. The Labour Appeal Court concluded in such circumstances and in order to enable effective exercise of its jurisdiction to the declarators referred to, the Labour Court had the power to order disclosure of information on the exercise or otherwise of those rights and that section 158(1) (j) of the Act empowers the Labour Court to deal with all matters incidental to performing its functions in terms of the Act or any other law.

In attempting to give meaning to the concept of going concern the court in *Schutte*<sup>30</sup> concluded that in determining a going concern, regard had to be had to the substance rather than the form of the transaction. The court found that a number of factors have to be considered and none is conclusive on its own. For example the transfer of a significant number of employees and the immediate continuation or resumption of service or function is indicative but not conclusive. In the particular case the court found the existence of a relationship between the second and first respondents, the in 'principle agreement' to sell the workshops, the terms of the working agreement, the first respondent's employment of the majority of the workshop employees, the use of the same premises, the continuation of the same activities without interruption and the intended transfer of assets and equipment indicated that there was a transfer within the meaning of section 197.

The meaning of the phrase 'going concern' resulted in a divided bench in the case of *NEHAWU v University of Cape Town*.<sup>31</sup> The accepted position before this decision was that in the case of a transfer as a going concern in terms of section 197 the new employer also takes over the employees and that is not a matter of choice. One of the questions the Labour Appeal Court had to deal with was

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<sup>30</sup> Footnote 18 at 180-183.

<sup>31</sup> *University of Cape Town and Others v NEHAWU* (2002) 4 BLLR 311 (LAC)

whether employers transferring a business as a going concern could agree not to transfer the affected employees.

Van Dijkhorst AJA, when delivering the majority judgment, was of the view that as subsection 2(b) of the old section 197 made reference to automatic transfers and subsection 2(a) of the same section dealing with solvent business entities did not, it meant that there could be no automatic of solvent business entities. According to the learned judge, to say that there could be a sale of a business as a going concern without all or most of the employees going over, was to equate a bleached skeleton with a vibrant horse. His view was that a going concern is one in actual operation and that could not be the case where there is no workforce.

Zondo JP dissented. He was of the view that the determining factor was whether there had been interruption of the operation of the business. The Judge President was of the view that there were circumstances where a business could transfer as a going concern without employees transferring. Such cases could be where, for example, the employer sells a filling station with its stock-in-trade and goodwill but does not transfer the two petrol attendants to the purchaser who brings in his or her own staff who start with the operations immediately upon the transfer. Zondo JP concluded that when a solvent business is transferred as a going concern from one employer to another there is no need for consent of either the employees or that of business transferor and the transferee, before contracts of employment of the employees become contracts between each employee and the new employer unless there is an agreement between the workers or their representatives to the contrary, the new employer assumes liability for all the actions done by the old employer in relation to each employee and also acquires rights

and obligations that the old employer may have had in relation to each employee.

What Zondo JP appears to mean is that when a business is transferred it is not necessary to obtain consent of the employees but when contracts of employment are to be transferred consent of the employees or their representatives is required otherwise the new employer steps into the shoes of the old employer. These different views could be a result of the fact that subsection (2) (a) only provided that 'unless otherwise agreed' but did not say between who and who. The challenge posed by the fact that the phrase 'going concern' was not defined, is seen in Van Dijkorst AJA's defining it as 'one in actual operation' and that which cannot be transferred without all or most of its workforce while for Zondo JP the important factor is 'whether there was an interruption of the operation of the business'. My view is that a going concern is an entity that is in a state of readiness to function substantially in the manner it was immediately before the transfer. I agree with the view expressed by Zondo JP that the transferor needs not transfer the workforce or part thereof to make the transfer a going concern transfer. Actually, the old section 197 wanted the workforce to be transferred in the event a going concern was transferred and this is the case with the amended version. This recognises that a going concern could be transferred without the workforce but for the provisions of section 197.

In the appeal of *NEHAWU v University of Cape Town*, the Labour Appeal Court had the following to say:

"Furthermore, I am of the view that the question whether in a particular case a business has been transferred as a going concern is a matter of objective determination. This does not mean that the intentions of the parties are irrelevant but it does mean that the say-so of the parties cannot be

conclusive. In my view there are a number of factors that are relevant in determining whether or not a business has been transferred as a going concern. These may include what will happen to the goodwill of the business, the stock-in-trade, the premises of the business, contracts with clients or customers, the workforce, the assets of the business, the debts of the business, whether there has been interruption of the operation of the business and, if so, the duration thereof, whether the same or similar activities are continued after the transfer or not and others. I do not think the absence of anyone of them will on its own mean that the transfer of the business has not been one as a going concern."<sup>32</sup>

The Constitutional Court in the same case of *NEHAWU v University of Cape Town and Others* said:

"The phrase 'going concern' is not defined in the LRA. It must therefore be given its ordinary meaning unless the context indicates otherwise. What is transferred must be a business in operation "so that the business remains the same but in different hands". Whether that has happened must be determined objectively in light of the circumstances of each transaction."<sup>33</sup>

I subscribe to this view.

#### **2.5.1.4. Outsourcing**

The question whether outsourcing of a part of a business trade or undertaking amounts to a transfer as contemplated in section 197(1)(a) was addressed in the case of *NEHAWU v University of Cape Town and Another*.<sup>34</sup> The first respondent outsourced non-core business services to the second respondent. The applicant argued that outsourcing of the affected services was a transfer of a part of the first respondent's business, trade or undertaking as a going concern as contemplated in section 197(1) (a). The first respondent's contention

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<sup>32</sup> Footnote 31 at 332 para 64.

<sup>33</sup> 2003 (2) BCLR 154 CC at 173 para 56.

<sup>34</sup> (1) (2000) 7 BLLR 803 (LC).

was that outsourcing of the affected services did not amount to a transfer as envisaged in section 197(1) (a). The second respondent argued that in terms of section 197 when the whole or any part of a business trade or undertaking is transferred as a going concern the contracts of employment of the employees engaged in the business or part thereof, and the rights and obligations arising from those contracts are transferred only if the transferor and the transferee agree that the transfer will involve employees.

The court concluded that the outsourcing did not amount to a transfer in terms of section 197 and in differentiating outsourcing from a permanent transfer in terms of section 197 said the following:

“In my view the sale of a business, legal transfer thereof to another employer or merger is markedly different to outsourcing. Outsourcing means putting out to tender certain services for a fee. The contractor performs the outsourced services and in return is paid a fee for its troubles by the employer. Where outsourcing occurs the employer pays the contractor a fee to render the services outsourced as opposed to paying salaries or wages to a group of employees to render the outsourced service. An outsourcing transaction is usually for a fixed period of time at the end of which it again goes to tender and the existing contractor could lose the contract to another contractor”<sup>35</sup>

Having said that, the court went on to acknowledge that there could be outsourcing transactions that amount to transfers as contemplated in section 197. The court said that that could happen where the outsourcing transaction was of a permanent nature.

The Constitutional Court<sup>36</sup> in the same matter between the same parties found that upon transfer of a business as going concern as contemplated in section 197(1)(a), the workers are transferred to the

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<sup>35</sup> Footnote 34 at 816 para 30.

<sup>36</sup> Footnote 33.



new owner. It further found that the fact that there was no agreement to transfer the workforce or part of it between the University and the contractors did not, as a matter of law, prevent a finding that outsourcing was transfer as going concern. The court did not decide whether in this case outsourcing amounted to transfer of the business as envisaged by section 197.

The Labour Court in the same matter spoke about outsourcing of a permanent nature that could amount to transfer in terms of section 197 and the Constitutional Court found that there was nothing in law which prevented a finding that outsourcing could amount to a transfer in terms of section 197. My difficulty with this view is, at what point can outsourcing be said to have amounted to a transfer? When can one say an outsourcing transaction has acquired a degree of permanence to assume the status of a transfer in terms of section 197?

Grogan has the following to say about second generation outsourcing:

“This is the process that takes place when an outsourced part of a business passes out of the hands of the first subcontractor and is taken over by another. First-generation outsourcing differs from second- (or later) generation outsourcing in that the business of the primary employer has been transferred twice or more, and in the second transaction the employees transfer not from the principal to the contractor, from contractor to contractor.”<sup>37</sup>

The important question to me is whether outsourcing can amount to transfer of a business as a going concern within the meaning of section 197. Grogan<sup>38</sup> quotes the Labour Court case of *NEHAWU v University of Cape Town* and makes an interesting analogy. For convenience I repeat the quote which is as follows:

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<sup>37</sup> Footnote 17 at 490.

<sup>38</sup> Footnote 17 at 491.

"It appears therefore that the fact that in a legal transfer or a sale the fact that there is a permanent transfer of a business or a part thereof must mean that in outsourcing what is transferred is nothing more than an opportunity to perform the so-called outsourced services. In my view it remains the prerogative of the outsourcing party to decide who gets the contract to perform the outsourced services."<sup>39</sup>

Grogan<sup>40</sup> says that implicit in this reasoning is that outsourcing cannot constitute a transfer of business because when the service is outsourced, the contractor does not gain control over the ultimate fate of the contract – control remains in the hands of the principal. I subscribe to the views as expressed in the analogy. Even though the Constitutional Court did not make a ruling on this particular aspect, I am of the view that outsourcing cannot amount to transfer of a business within the meaning of section 197. It appears to me it is either one has a transfer in terms of section 197 or an outsourcing transaction. The wording of section 197 is clear on this aspect. It talks about transfer and not outsourcing.

The question whether second generation contracting out constitutes transfer within the meaning of section 197 was answered in the case of *Aviation Union of South Africa and Others v S.A. Airways (Pty) Ltd and Others*<sup>41</sup> where the Labour Court found that section 197(1) (b) is unambiguous and that second generation contracting does not constitute a transfer within the meaning of section 197. The section specifically identifies the old employer and the new employer.<sup>42</sup> This decision was recently overturned by the Labour Appeal Court.<sup>43</sup> The Labour Appeal Court based its decision on section 233 of the

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<sup>39</sup> Footnote 34 at 816 para 32.

<sup>40</sup> Footnote 17 at 492.

<sup>41</sup> (2008) 29 ILJ 331 (LC).

<sup>42</sup> See also *Crossroads Distribution (Pty) Ltd v Clover SA (Pty) Ltd t/a Jowells Transport and Others* (2008) 29 1013 (LC).

<sup>43</sup> *Aviation Union of South Africa and Another v South African Airways (Pty) Ltd* (2010) 1 BLLR 14 (LAC).

Constitution which provides that when interpreting any legislation, every court must prefer any reasonable interpretation of the legislation that is consistent with international law over any alternative interpretation that is inconsistent with international law. The court then found that Council Directive 77/187/EEC of 14 February 1977 covered an outsourcing transaction in circumstances similar to section 197. As earlier indicated I do not agree with the view that outsourcing falls within the meaning of section 197.

#### **2.5.1.5. Date of transfer**

The date of transfer may at times be of relevance in determining who of the employers is liable to an employee. In *Van der Velde v Business Design Software (Pty) Ltd & Another*<sup>44</sup> where the transferring employer and the transferee employer agreed and signed that the transfer agreement takes effect on a date earlier than the signature date and the fulfilment of suspensive conditions the court held that the date of transfer for the purposes of section 197 was the date on which the sale of the business became unconditional and the second respondent assumed full control of the business bundle that is the subject of the transfer.<sup>45</sup>

#### **2.5.1.6. Consultation**

In *S.A. Commercial Catering and Allied Workers Union and Others v Western Province Sports Club t/a Kelvin Grove Club and Another*<sup>46</sup>, the court correctly found that whenever there is a transfer of a business as a going concern in terms of section 197 the general rule is that the old employer is automatically substituted by the new employer and the

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<sup>44</sup> (2006) 27 ILJ 1225 (LC).

<sup>45</sup> See also Grogan J *Workplace Law* 10<sup>th</sup> ed (2009) Juta 299.

<sup>46</sup> (2008) 29 ILJ 3038 (LC).

employees are protected from losing their jobs. In such cases, the court found that employees do not have a right to be consulted. An exception happens in section 197(6) which permits the old and new employers to consult any of the parties contemplated in section 189(1) of the Labour Relations Act.

### **2.5.2. Transfers in cases of insolvency**

Before the amendments of 2002 section 38 of the Insolvency Act provided that contracts of employment came to an end upon order of insolvency by court. A provisional order had the effect of terminating contracts of employment. It could at times happen that an employer is provisionally liquidated but the employer gets saved from liquidation before the final order of liquidation. The terminated employees could not just continue with employment after the employer was saved from liquidation.

A case in point is that matter of *Ndimma and Others v Waverly Blankets Ltd*<sup>47</sup> where the respondent company was placed under provisional liquidation and liquidators appointed to run the business of the respondent pending either disposition of assets or pending a scheme of arrangement as contemplated in section 311 of the Companies Act.<sup>48</sup> The respondent informed its employees, including the applicants that their contracts of employment were terminated. A scheme of arrangement was later sanctioned by the court after which the applicants tendered their services but respondent refused to take them in its employment. The Court concluded that the contracts of employment were terminated by virtue of the application of section 38 of the Insolvency Act and suggested that section 197 of the Labour Relations Act and section 38 of the Insolvency Act needed to be

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<sup>47</sup> (1999) 20 ILJ 1563 (LC).

<sup>48</sup> Act No 61 of 1973.

amended. It suggested that section 38 of the Insolvency Act could be amended to say that upon the granting of a provisional liquidation order, existing contracts of employment are suspended pending the discharge of the rule or the granting of the final liquidation order. This suggestion by the court is now seen in the amended section 38 of the Insolvency Act. The court made a similar finding in the case of *SAAPAWU v HL Hall & Sons (Group Services)*.<sup>49</sup>

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<sup>49</sup> (1999) 2 BLLR 164 (LC).

## CHAPTER 3

### EFFECT ON CONTRACTS OF EMPLOYMENT

#### 3.1. Transfers in the normal course

Transfers of contracts of employment normally bring with them certain effects or consequences for both employers and employees. Basson *et al* say:

“As mentioned earlier, the purpose of section 197 is to protect employment security during transfers. Not surprisingly then, sub-section 197(2) lists the following four consequences of a transfer:

- the new employer is substituted in the place of the old employer in respect of all contracts of employment in existence just prior to the transfer
- the rights and obligations in terms of those pre-existing contracts of employment continue between the new employer and employees
- all obligations of the old employer arising from the old employer's actions prior to the transfer become obligations of the new employer
- continuity of employment is maintained.”<sup>50</sup>

The authors state that these are the principles for the new employer who may well want to restructure the business and, possibly, retrench employees. They further state that if the new employer decides to retrench employees taken from the old employer, severance pay will be calculated on the basis of service with the old and new employer (years of service affect the level of obligation to pay severance pay in terms of section 41(1) of the Basic Conditions of Employment Act, 1997.) The authors say that by the same token, remuneration and

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<sup>50</sup> Footnote 2 at 177.

benefits may, in some way be linked to the years of service (such as leave and leave pay, which may also place financial burden on the new employer (in terms of contractual entitlements) should it decide to terminate the service of the employees taken over from the old employer.<sup>51</sup> They also point out that section 197 may affect the freedom of the new employer to apply certain selection criteria in case of retrenchment. The new employer will also be expected to pay for what they refer to as the 'sins' of the old employer as was the case in *NUMSA & Another v Success Panelbeaters*.<sup>52</sup>

### 3.1.1. Retirement age

Grogan has the following to say about consequences of a transfer:

"It means, quite simply, that once such a transfer of business occurs, the new employer becomes the employer of the transferred employees, and that subject to the new employer's right to effect minor amendments, the employee's terms and conditions of employment remain unchanged."<sup>53</sup>

He points to the case of *Rubin Sportswear v SACTWU and Others*<sup>54</sup> where after the transfer of business as a going concern the new employer wanted to change the retirement age agreed to between the old employer and the transferred employees contrary to the agreement with the union. The Labour and Labour Appeal Courts came to the conclusion that the variation was in conflict with the Labour Relations Act and the agreement with the union. He further observes that unlike the old section 197, the current version permits employers to vary the terms and conditions of employment of transferred employees if the new terms and conditions are 'on the

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<sup>51</sup> Footnote 45 at 251, See also Van Jaarsveld SR, Fourie JD and Olivier MP *Principles and Practice of Labour Law* (2008) at para 901.

<sup>52</sup> (1999) 9 BLLR 970 (LC).

<sup>53</sup> Footnote 17 at 493.

<sup>54</sup> (2004) 25 ILJ 1671.

whole not less favourable to the employees than those on which they were employed by the old employer' and this will probably allow the new employer to amend working hours and shift arrangements if the change is operationally justified.

### **3.1.2. Restraint of trade**

Todd *et al*<sup>55</sup> say that a restraint of trade agreement that is enforceable as between the old employer and a particular employee will, it seems clear, be enforceable as between the new employer and that employee. Even in the absence of section 197, the benefit of restraint of trade agreement has in South Africa been held to form part of the goodwill of a business transferred from one owner to another. They also refer to *Botha v Carapax Shadeports (Pty) Ltd*<sup>56</sup> wherein the benefit of an agreement in restraint of trade was held to form part of the goodwill that had been transferred under the sale of business agreement.

In *Securicor (SA)(Pty)Ltd and Another v Lotter and Others*<sup>57</sup> the appeal court had to decide whether restraint of trade agreements survived the transfer under the provisions of section 197 of the Labour Relations Act. The court disagreed with the trial court's finding that restraint continued operating only in respect of the old employer's customers and that its termination had to be determined with reference to whether employee's contractual relationship with the old employer came to an end. The court found that the effect of section 197 is that the new employer is automatically substituted in the place of the old employer in respect of all contracts of employment and that rights and obligations between the old employer and the worker are transferred to the new owner as such where section 197 applies to a transfer, any

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<sup>55</sup> Footnote 9 at 91.

<sup>56</sup> 1992 (1) SA 202 A.

<sup>57</sup> (2005) 10 BLLR 1032 (E).



restraint of trade is also transferred as part of the goodwill of the business.

### 3.1.3. Severance Pay

Employers at times dismiss employees for reasons related to operational requirements. In *Keil v Foodgro (A division of Leisurenet Ltd)*<sup>58</sup> the applicant was dismissed by the respondent for reasons of operational requirements after having been transferred to the respondent by her previous employer. In dismissing the applicant it appears the respondent used the last-in-first-out method and in doing so did not take into account the applicant's length of service with the previous employer. The court considered the provisions of section 197 particularly sub-section 2 and came to the conclusion that one of the rights of employees at the time of transfer is the right accruing by virtue of the length of service. The respondent therefore had an obligation to recognise the length of service especially where it decides to retrench an employee. On appeal to the Labour Appeal Court<sup>59</sup>, *Foodgro* argued that the 'letter of appointment' replaced the contract between itself and the respondent and that that affected the respondent's length of service with the appellant. The respondent argued that her length of service could not be altered by agreement as that would fall foul of the provisions of section 197(4). In finding in favour of the respondent the court had this to say:

"Section 197(1) (a) and (b) provides for the automatic transfer of an employee's contract of employment upon transfer of the business, trade or undertaking in the circumstances set out in the section. Section 197(2) (b) allows the contracting out of the transfer of the contract of employment itself, but section 197(2) (a) does not. Under section 197(2) (a) the relevant parties may alter the terms of the transferred contract, but they cannot escape the

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<sup>58</sup> (1999) 4 BLLR 345 (LC).

<sup>59</sup> *Foodgro (A division of Leisurenet Ltd)* (1999) 9 BLLR 875 (LAC).

fact of its existence. Because an employee's continuity of employment is not a right or an obligation, or a term or condition of the employment contract, express provision was made in section 197(4) that the transfer of the employment contract would not interrupt that continuity. There is no provision in it, similar to section 197(2), which allows the parties to alter an employee's continuity of employment by agreement."<sup>60</sup>

The *Foodgro* appeal ruling was also confirmed in the case of *AST Holdings (Pty) Ltd v Roos*.<sup>61</sup>

An employer that transfers business as a going concern need not pay severance pay to the employees if the purchaser offers them adequate alternative employment. This is the decision in the case of *Pama and Others v CCMA & Others*<sup>62</sup> where the respondent employer sold its business as a going concern and contracts of employment, including those of the applicants, were transferred to the purchaser. Applicants referred the matter for arbitration claiming payment of severance pay. The Commission for Conciliation Mediation and Arbitration ruled in favour of the respondent employer whereafter the matter was referred to the Labour Court for review.

The applicants relied on section 41 of the Basic Conditions of Employment Act which provides as follows:

"(2). An employer must pay an employee who is dismissed for reasons based on the employer's operational requirements severance pay equal to at least one week's remuneration for each completed year of continuous service with that employer calculated in accordance with section 35.

(3).....

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<sup>60</sup> Footnote 59 at 882 para 25. See also Grogan J "Transferring Workers: Section 197 of the LRA" *Employment Law Journal* (October 1999).

<sup>61</sup> (2007) 28 ILJ 1988 (LAC).

<sup>62</sup> (2001) 9 BLLR 1079 (LC).

(4). An employee who unreasonably refuses to accept the employer's offer of alternative employment with that employer or any other employer is not entitled to severance package in terms of subsection (2)".

Applicants contended that as they did not refuse alternative employment they should not be denied severance pay. The court reasoned that an employer engaged in restructuring is unlikely to be in a position to offer alternative employment, especially if the business is sold. It further reasoned that as in terms of section 41(1) of the Basic Conditions of Employment Act the alternative employment may be with "that employer or any other employer", the legislature clearly contemplated that the offer of employment may emanate from another employer. The court went further and stated that the dismissing employer would have complied with section 41(1) of the Basic Conditions of Employment Act if it facilitated employment with the new employer. It came to the conclusion that strict interpretation of the subsection could lead to the conclusion that severance pay is not forfeited if alternative employment is accepted. It found that applying a purposive approach, subsection (4) lends itself to the interpretation that as an incentive for employers to find employment for employees to take up employment, severance pay should only be payable if there is no offer of alternative employment or if the refusal of alternative employment is reasonable. The application was correctly dismissed with costs.

Grogan has this to say:

"When employees have good reason to refuse offers of transfer which are necessary for the restructuring of the company, their cases should probably be treated as redundancies, and the requirements for retrenchment should be followed. Section 41(4) of the BCEA expressly disentitles employees to

severance benefits if they unreasonably refuse their employer's offer of alternative employment with the same employer or any other employer."<sup>63</sup>

This comment is in line with the finding of the court in the *Pama* case.

### **3.1.4. Pensions**

The old section 197 did not make provision for the status of pensions or provident fund benefits on transfer. In *Telkom SA Ltd & Others v Blom*<sup>64</sup> a division of Telkom was sold as a going concern to third respondent. In terms of the agreement of sale, Telkom transferred its contracts of employment with its employees to Molapo without their consent, which act brought the provisions of section 197 into the picture. The respondents' contention was that the effect of the transfer was to bring about termination of their employment with Telkom as a result of the abolition of their posts and reorganisation of Telkom's activities. This, according to them, in turn brought about termination of their membership of the Fund and entitled them to the benefits from the Fund in terms of the statutes and the rules. The Court after considering the relevant rules concluded that the operative clause was the one that provided that if the services of an A-member are terminated by the employer as a result of the abolition of his post or reorganisation of the employer's activities, certain specified pension and gratuity benefits shall be paid to the member.<sup>65</sup>

Following the Labour Relations Act amendments in 2002, the position with regard to pensions is catered for in section 197(4) which provides that an employee may be transferred to a pension, provident, retirement, or similar fund other than the fund to which an employee

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<sup>63</sup> Footnote 17 at 94.

<sup>64</sup> (2003) 7 BLLR 638 SCA.

<sup>65</sup> See also footnote 9 at 104, Grogan J "Transfer of Pension Funds" *Employment Law Journal* (August 2003).

belonged prior to the transfer provided the criteria in section 14(1) of the Pension Funds Act are satisfied.

### **3.1.5. Awards and Collective Agreements**

The amended section 197 provides that unless there is an agreement in terms of subsection (6) the new employer is bound by collective agreements and arbitration awards that bound the old employer in respect of the employees to be transferred, immediately before the date of transfer.

The effect of section 197 on arbitration awards and collective agreements was dealt with in the case of *Transport Fleet Maintenance and Another v NUMSA*<sup>66</sup>. After having dismissed its employees, the second appellant sold its business as a going concern to the first appellant. The second appellant's management did not inform the respondents and the commissioner about the sale and transfer of the business. The commissioner handed down his arbitration award which was to the effect that the second and further respondents' dismissal by the second appellant was unfair and that the second appellant should reinstate the respondents. A dispute arose between appellants and respondents on which of the two appellants had an obligation to give effect to the arbitration award. The respondents brought an application to the Labour Court for, amongst others, an order that the first appellant give effect to the award which meant that it should reinstate them with effect from the date on which they reported for duty. The respondents were of the view that the business was transferred in terms of section 197(2)(a) of the Act and that all rights that they had against the second appellant at the time of the transfer and all the obligations which the second appellant had towards them

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<sup>66</sup> (2003)10 BLLR 975 (LAC).

were transferred by operation of the law to the first appellant. This, in the view of the respondents, included arbitration awards. The Labour Court confirmed the respondents' contention and refused to grant leave to appeal to the Labour Appeal Court. The appellants petitioned the Labour Appeal Court but their petition was also dismissed.

Todd *et al*<sup>67</sup> say that all the consequences of employment under section 197 may be varied by agreement as contemplated in subsection (6) of the same section. The employers have further obligations in terms of sub-section (7) of section 197 that include valuation of leave pay as accrued to transferred employees of the old employer in the event of a dismissal by reason of operational requirements and any other payments that have accrued to the transferred employees but have not been paid to the employees of the old employer. The employers must conclude a written agreement that specifies which is liable for what amount and they must disclose the terms of such agreement to each employee who becomes employed by the new employer.

### **3.2. Transfers in cases of insolvency**

Basson *et al*<sup>68</sup> say that the earlier approach was that in case of insolvency all contracts of employment between the insolvent employer and its employees terminate automatically. Not only did these employees lose their jobs, but as far as unpaid wages are concerned, they became creditors of the insolvent estate of the employer and, if they were lucky, actually received some fraction of those unpaid wages. The authors say that to appreciate how this principle affected employees one has to bear in mind the actual process preceding any final order of insolvency.

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<sup>67</sup> Footnote 9 at 84 para 3.15.

<sup>68</sup> Footnote 2 at 181 para 9.4.

Companies and close-corporations can only be declared insolvent by a court order, on application of either the company or close corporation (employer itself) or on application of the creditors. This, they say, already shows how an employer can manipulate the processes to get rid of employees by liquidating themselves. Once the application proceeds in court, the court will first place the entity under provisional liquidation. This in practice means that there is still time to come to some kind of arrangement with the prospective buyer or with the creditors of the employer to ensure survival or continuation of the operations of the old employer. However the automatic termination of contracts of employment kicks in as soon as the provisional winding up order is made. This could lead to a situation where the employer actually continued, but the employees lost their jobs.

The effect of section 197A (the amendment) is that all employees of the insolvent employer become employees of the new employer and the continuity of employment is preserved. These consequences are made subject to agreement between the employees and the new or old employer or both to the contrary. Rights and obligations between the old employer and the employees at the time of transfer remain the rights and obligations between the old employer and the employees in the case of transfer in circumstances of insolvency. Anything done by the old employer in respect of an employee (such as unfair dismissal, unfair labour practice or unfair discrimination) remains to be sorted out between employees and the old employer.

Subsections 197(7)-(9) which provide for valuation and provision of accrued benefits in case of ordinary transfers, do not apply to transfers in circumstances of insolvency. Section 197B places an obligation on an employer that is facing sequestration or intending to apply for

winding up to advise and provide the consulting party in section 189(1) with copy of the application. These provisions are clearly intended to protect employees in that the employees will be furnished with information regarding the insolvency application as was stated earlier that there could at times be cases of manufactured insolvencies.



## CHAPTER 4

### 4.1. CONCLUSION

The Constitution is the supreme law of the Republic and section 23 thereof provides that everyone has the right to fair labour practices. This means that fair labour practices should be applied to employers and employees alike. This position was confirmed by the Constitutional Court in the case of *NEHAWU v University of Cape Town and Others*<sup>69</sup> where the court found that the main purpose of section 197 is to protect workers against loss of employment in the event of transfer of business as a going concern. The court went further to state that section 197 is for the benefit of both employers and employees as it facilitates transfers while protecting employees. According to the court, upon the transfer of a business as a going concern as contemplated in section 197, employees are transferred without need for prior agreement between the old and new employer. The effect of a transfer as a going concern in terms of section 197 is that the new employer takes over the workforce unless agreed otherwise in terms of subsection (6).

A major challenge with the section is that some important words and clauses remain undefined or are not properly defined despite the 2002 Labour Relations Act amendments. An example of a word that is not properly defined is 'transfer'. In the *Schutte* case the court found that a transfer can take place in the context of restructuring, merger and other forms. As a result of the word 'transfer' not being properly defined, courts have tended to equate it to outsourcing. The Constitutional Court in the *NEHAWU* case found that there was nothing in law which prevented a finding that outsourcing could amount to a transfer as a going concern as contemplated in section 197.

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<sup>69</sup> Footnote 33.

In the *Aviation Union of South Africa*<sup>70</sup> case the Labour Appeal Court found that second generation outsourcing amounted to a transfer of a business as a going concern by relying on the purposive approach of interpretation. The court premised its finding on section 39(2) of the Constitution which provides that in interpreting any legislation, and when developing common law or customary law, every court tribunal or forum must promote the spirit, purport and objects of the Bill of Rights. It further premised its finding on section 233 of the Constitution which provides that in interpreting any legislation, every court must prefer any reasonable interpretation of the legislation that is consistent with international law over any alternative interpretation that is inconsistent with international law. It is submitted that this kind of approach is unfortunate, not because recourse should not be had to the Constitution and international law, but because it misses the initial important enquiry.

Section 197 refers to a transfer of a business from one employer (being the old employer) to another employer (being the new employer) as a going concern. It is clear from the wording that only a permanent transfer is envisaged. The words 'old employer' and 'new employer' envisage a permanent transfer and outsourcing does not come into the picture. The initial important enquiry should then be whether the transaction is a permanent transfer or outsourcing. If the transaction is a permanent transfer then section 197 becomes applicable. If the transaction is one of outsourcing, section 197 is not applicable and that should be the end of the matter.

It is submitted that before regard can be had to anything the literal rule requires words to be given their ordinary grammatical meaning. It is

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<sup>70</sup> Footnote 43.

only when this would lead to absurdity that other rules of interpretation can be resorted to. In this instance it is clear from the wording of section 197 that outsourcing is not one of the transactions covered by the provisions of the section. Wallis<sup>71</sup> correctly points out that, bearing in mind that the purpose of section is to balance and protect the interests of both the employee and employer, it is a perfectly reasonable hypothesis that the legislature deliberately decided to limit the scope of the section to those transactions where two parties decide to bring about change of ownership by whatever means, but not to extend the section to more remote situations. In support of the literal rule of interpretation, Wallis says:

“We know from the *NEHAWU* case that the contents of the LRA, which was passed to give content to the constitutional right to fair labour practices, is a constitutional matter. Recently the court has made the point that in case of such statutes it is inappropriate to seek to avoid the application of the plain language of such a statute by way of an interpretation allegedly based on the Constitution. If there is in truth some anomaly in section 197 of the LRA then the proper way to deal with that anomaly is not by a judge amending the section in the guise of interpretation but by way of an amendment or constitutional challenge on the basis that the LRA does not sufficiently protect employees against unfair labour practices in section 197. In that way the pros and cons of the section can be properly considered without introducing into our law foreign jurisprudence that does not belong here”.<sup>72</sup>

I am of the view that the Labour Appeal Court erred in its interpretation of section 233 of the Constitution. The section envisages a situation where legislation or a provision thereof is capable of more than one interpretation and in such situations a court must prefer the interpretation that is consistent with international law. Now, in the present case section 197 refers to transfers of a permanent nature only and as such there is no need to seek assistance of section 233 of the

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<sup>71</sup> Wallis MJD “Is outsourcing in? An Ongoing Concern” (2006) 27 ILJ 1 at 13.

<sup>72</sup> Footnote 71 at 16.

Constitution. The inclusion of outsourcing by way of interpretation by the court amounts to amendment of the section. In advancing the purposive theory, the court is saying that the legislature intended to include 'outsourcing' in section 197 but omitted to do so. It does not say that the section, as it stands on transfers, is capable of more than one meaning in which case one has to be preferred over the other in compliance with section 233 of the Constitution.

The court was also of the view that the inclusion of outsourcing within the meaning of section 197 would protect employees as unscrupulous employers who wanted to get rid of their employees would do so under the guise of outsourcing knowing that when the business transferred in circumstances of outsourcing no protection would be available to employees. It is submitted that this argument or view cannot be sustained because in an outsourcing transaction, employees remain employees of the outsourcer and the need for protection therefore does not arise in this context. It should be stated that while the parties in the present case had agreed that the employees in the outsourcing agreement would transfer to the contractor in terms of section 197, the truth is that in law the transaction was not a transfer in terms of section 197. It is further submitted that it is not for the parties to determine whether a transaction falls within the ambit of section 197 or not but it is the nature of the transaction that determines whether it is a section 197 transfer.

The wording of the amended section 197 is in some respects confusing. This can be seen in the words 'immediately before' in subsection 2(a). Du Toit *et al* have this to say about section 197(2) (a):

"Less clear is the meaning of the term 'immediately before' the transfer. This could be interpreted as including contracts that were in existence prior to the transfer but are no longer in existence at the time of the transfer. If so, the

effect would be that contracts which were terminated in the period 'immediately before' the transfer would 'revive' with the new employer. It is submitted that this could not have been intended and that, for practical purposes, the term should be taken to mean contracts that are still in existence at the time of transfer."<sup>73</sup>

Bosch questions the construction of the same section as follows:

"An additional, important question in relation to the proposed s 197(2)(a) is whether all the contracts in existence immediately before the transfer will revive or whether the section only relates only to those that were terminated contrary to the purpose of the section? It would seem contrary to the purpose of the section effectively to nullify every dismissal that happened to occur in the period immediately before the transfer and that may be completely unrelated to the transfer of the business or based on related, but permissible, grounds like operational requirements. The impact of the proposed s 197(2)(a) should thus be limited to instances where contracts were terminated contrary to the purpose of the section, the classic example being whether the dismissal was utilized in an attempt by employers to escape their obligations in terms of s 197, to provide additional protection to affected employees."<sup>74</sup>

It is clear from the above quotes that the literal interpretation of words 'immediately before' would lead to absurdity. I agree with the view that the words 'immediately before' should be understood to mean contracts that are still in existence at the time of the transfer because a contract that was not in existence before the transfer cannot be transferred but rights and obligations flowing from such a contract can. It appears to me such rights and obligations are covered by section 197(2) (a) and (b).

The section provides that anything done before the transfer by or in relation to the old employer, including the dismissal of an employee or

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<sup>73</sup> Footnote 1 at 432.

<sup>74</sup> Bosch C "Operational Dismissals and Section 197 of the Labour Relations Act: Problems and Possibilities" (2002) 23 ILJ 641 at 655.

the commission of an unfair labour practice or an act of unfair discrimination, is considered to have been done in relation to the new employer. One wonders if there is a need for this subsection as subsection 197(2)(b) provides that all rights and obligations between the old 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. *Du Toit et al*<sup>75</sup> also correctly point to the redundancy of section 197(5) (a) in light of section 197(2) (b). They also question the singling out of collective agreements while other sources of rights and obligations such as court orders are not mentioned.

As already stated, the subsection permits the transfer of an employee to a pension, provident, retirement or similar fund other than to which an employee belonged, subject to section 14(1) of the Pension Funds Act. The subsection is only permissive and does not provide that the pensions automatically transfer with the contracts of employment. This means that should situations as in the *Telkom* case arise, they will not find an answer in the subsection.

*Todd et al*<sup>76</sup> raise an interesting subject on whether the contracts of transferred employees are new contracts or old contracts. According to them, the transfer of contracts of employment as contemplated in section 197, has the effect that the existing contract of employment is preserved while the employer party to the contract is substituted. They contend that in those circumstances the contract of employment with the old employer does not “terminate” despite the fact that the old employer ceases to be the employer and is released from its obligations under the contract. Their view is that no new contract of employment comes into existence following the transfer, and that the new employer simply becomes party to an existing contract, which

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<sup>75</sup> Footnote 1 at 435.

<sup>76</sup> Footnote 9 at 66.

continues to exist. They point that the establishment of the notion of transferability of the employment relationship by providing for the substitution of one employer by another (irrespective of consent of either employer or employee) does give rise to significant practical and conceptual difficulties. They make reference to the case of *Telkom v Blom*<sup>77</sup> where the Court found that the old employer “falls out of the picture” and as between the old employer and each employee, the contract is “extinguished”. They have a difficulty with this view that the contract is ‘extinguished’ but my view is that it is.

In the *Telkom* case Jones AJA had the following to say about the effect of a transfer in terms of section 197 making reference to the Constitutional Court case of *NEHAWU v University of Cape Town and Others*:

“ Ncgobo J did not make use of the word “ assignment”, but his description of the nature and effect of the transfer of an employment contract contemplated by the Act leaves me in no doubt that an assignment takes place. In legislating that all rights and obligations between the old employer and each employee at the time of the transfer continue in force as if they were rights and obligations between the new employer and each employee, and that the transfer of business does not interrupt the workers' continuity of employment, the lawgiver makes its intention plain. In the words of Ncgobo J, the inference is irresistible that the new employer takes over the workers and is by operation of law substituted in the place of the old employer. This is what happens on assignment. In my view the further inference is also irresistible that in the course of this process the contractual relationship between the old employer and each employee; i.e. the employment contract between them is brought to an end. This is a natural result of an assignment; the original employer falls out of the picture, and, as between him and the employees, the contract is extinguished.”<sup>78</sup>

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<sup>77</sup> Footnote 64.

<sup>78</sup> Footnote 64 at 643 para 10.

This view, to which I subscribe, is confirmed by Du Toit *et al*<sup>79</sup> who say that the effect of section 197 is that the new employer steps into the shoes of the old employer not only in respect of the employees' terms and conditions of employment but also in respect of disciplinary records, contractual claims and other reciprocal obligations arising from the employment relationship.

Todd *et al*<sup>80</sup> say that the very purpose of section 197 is to achieve continuity of the employment contract despite change in the identity of the employer. I agree with this view but would want to say that continuity of employment does not mean that the contract of employment with the old employer is not terminated. What to me appears to be one of the purposes of section 197 is that after termination of employment with the old employer by transfer the employee remains employed on the same or on the whole not less favourable terms and conditions. It would be incorrect to say that a contract of employment is not terminated on transfer. A transfer in the context of section 197 brings about change of parties to a contract. Once the parties to a contract change, it cannot be the same. It is rather terms and conditions of employment with the new employer that can remain the same or on the whole not less favourable to those in the old contract.

The fact that employees no longer look up to the old employer for the enforcement of their rights or for the carrying out of their obligations means that the contracts of employment between the old employer and the employees have come to an end. I submit that even section 197 recognizes this fact and seeks to provide protection for employees in the circumstances. Clearly, what the new employer takes over are rights and obligations of the old employer and the employees' service

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<sup>79</sup> Footnote 1 at 432.

<sup>80</sup> Footnote 9 at 17.



with the old employer. The use of the words “as if” and “is considered to have been done” denotes acknowledgment that the contract with the old employer has come to an end. What is preserved or assigned are the rights and obligations flowing from the old contract.

Todd *et al*, in attempting to show that the contract is not extinguished, argue that an employer who terminates a contract of employment dismisses an employee. They rely further on section 186(1) (a) of the Labour Relations Act. That part of the section provides as follows:

“Dismissal means that-  
an employer has terminated a contract of employment with or without notice;”

The authors argue that the contract is rather preserved and transferred and they say that:

“This conclusion is re-inforced by a consideration of the provisions of section 186 and 187 of the LRA. Section 187 provides that a dismissal is automatically unfair if the reason for the dismissal is a transfer, or a reason related to the transfer, contemplated in section 197. It would be automatically unfair for the old employer to dismiss its employees on transfer of its business to the new employer. If the old employer terminated the contracts of its employees, this would constitute a dismissal. If an old employer may properly be said to terminate the contracts of employment of transferring employees when it transfers its business as a going concern, the provisions of section 197 and 187 of the LRA (after the 2002 amendments) would be completely at odds with one another.”<sup>81</sup>

Section 187 provides that a dismissal is automatically unfair if the employer, in dismissing the employee, acts contrary to section 5 or, if the reason for the dismissal is, amongst others, a transfer or a reason related to a transfer, contemplated in section 197 or 197A.

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<sup>81</sup> Footnote 9 at 67.

Let us say an employer wants to transfer a business as a going concern in terms of section 197 and the new employer offers slightly improved terms and conditions of employment but the employee refuses to transfer. Can that employee not be dismissed? If the employee can be dismissed, would that dismissal not be automatically unfair as contemplated in section 187 because the reason for the dismissal is connected to the transfer? By these questions one wants to bring into light the construction of section 187(g) as it relates to section 197. It seems to me the legislature wanted to protect employees from being treated unfairly during transfer processes, for instance, where an employer in contemplation of a transfer, retrenches certain employees who the prospective employer does not want to take over for reasons of their participation in union activities in so doing avoiding compliance with section 197 or to avoid its consequences.<sup>82</sup> It is my submission that it would be more clearer to say, for instance, a dismissal is automatically unfair if the employer in dismissing the employee acts contrary to sections 5 and 197.

It is my submission that the provisions of the sections 187 and 197 read with section 186(1)(a) are at odds with one another. We should not allow this oddness to create further confusion that contracts that have been terminated are preserved. The reasoning cannot be correct. My view is that after the transfer the employees are protected by section 186(1) (f). Section 187(1) (g), if amended as suggested, would protect employees both before and after the transfer.

It is clear from the above discussions that the meaning of section 197 is not so clear from its wording as not to be given the meaning that was not intended by the legislature. It is also the courts that have given

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<sup>82</sup> Footnote 1 at 436.

different meanings to the provisions of the section despite the clear wording. The courts need to draw a clear line between legislating and interpreting. I submit that in the *Aviation Union of South Africa* case the Labour Appeal Court went beyond its mandate. Taking into account the importance of this section in labour relations matters, one is prompted to suggest that the section be reviewed. The same holds true with related sections such as 186 and 187 as this review would create harmony.



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