

Labour Outsourcing in South Africa

Mendel Yriel Sass



Labour Outsourcing in South Africa

Working definition of outsourcing

- agreement between two or more parties
- in terms of which a party is or parties are hired
- to perform a planned or existing activity
- that is or could be done internally
- sometimes involves the transfer of assets, employees etc.

Labour Outsourcing in South Africa

Regulatory framework

- generally: no national laws regulating outsourcing
- exceptions:
 - suppliers to government or public sector bodies (statutory creations and different private sector where only commercial considerations)
 - tenders processes/bid evaluations – consider public sector legislation which may impose some constraints (enacted to regulate these activities)
 - procurement must be fair, equitable, transparent, competitive and cost effective (Constitution of the Republic of South Africa)

Labour Outsourcing in South Africa

- Public Finance Management Act; Municipal Finance Management Act; Municipal Systems Act; Broad Based Black Economic Empowerment Act; Promotion of Administrative Justice Act; Preferential Procurement Policy Framework Act; general rules applicable to Administrative Law and Constitutional Law
 - some industry/sector specific regulations (medical aid, airlines, banking & financial services, telecommunications etc.)
- Section 197 of the Labour Relations Act – possible legal consequences of outsourcing (not regulatory *per se*)

Labour Outsourcing in South Africa

Commercial arrangements

- Single supplier outsourcing
 - entire service to one supplier
 - supplier can subcontract but client not a party to that
 - supplier carries full responsibility for service levels
- Multiple vendor outsourcing
 - technical, strategic or other reasons
 - separate agreements

Labour Outsourcing in South Africa

- stringent provisions for full co-operation and appropriate accountability
- Joint ventures
 - Setting up a separate company in which both the client and the supplier has an interest
 - Allows the client to exercise greater control and direction in the management of the supplier (and the service itself therefore)
 - Service agreement with schedules/annexure OR master services agreement with statements of work

Labour Outsourcing in South Africa

Types of outsourcing

- Initial Outsourcing
- Second (and later) Generation Outsourcing / change of supplier

Section 197 of the Labour Relations Act

- section 197 of the LRA is applicable to an outsourcing if that outsourcing amounts to a transfer of a business as a going concern from an 'old employer' to a 'new employer'
- 3 elements which must be proven

Labour Outsourcing in South Africa

- Firstly, the relevant transaction (i.e. the outsourcing) must be a transfer as envisaged by section 197 of the LRA (a wide range of transactions may fall within the ambit of a transfer including a sale, merger, take-over, outsourcing etc. - not a closed list)
- Secondly, the entity being transferred must be a business or part of a business ('business' includes a service, undertaking or trade)
- Thirdly, the business (i.e. entity) must be transferred as a going concern.

Labour Outsourcing in South Africa

Consequences if the outsourcing falls within the ambit of section 197

- the new employer is automatically substituted in the place of the old employer in respect of all contracts of employment in existence immediately before the date of transfer
- all the rights and obligations between the old employer and an employee at the time of the transfer continue in force as if they have been rights and obligations between the new employer and the employee
- anything done before the transfer by or in relation to the old employer, including the dismissal of an employee or the commission of an unfair labour practice or act of unfair discrimination is considered to have been done by or in relation to the new employer
- the transfer does not interrupt the employee's continuity of employment and an employee's contract of employment continues with the new employer as if with the old employer

Labour Outsourcing in South Africa

When does section 197 apply – the applicable legal principles

Introduction

- focus is on continuity and security of employment
- applicability of section 197 and its consequences are fact/circumstance specific
- courts have regard to substance over form (nothing turns on the label given to it by the parties)
- an outsourcing / change in service provider can sometimes trigger section 197 and other times not
- the ‘generation’ of the outsourcing makes no difference

Labour Outsourcing in South Africa

Transfer

- the mechanism/transaction is of no real significance
- the substance of what is happening is important and must be interrogated

Business

- a “business” or an “economic entity” must transfer to the supplier
- a “*business*” is defined as “*the whole or a part of any business, trade, undertaking or service*”
- not much difficulty in identifying the “business” when the whole of an undertaking is transferred

Labour Outsourcing in South Africa

- more complicated when the transfer relates to a part of the business or a service
- where there is a transfer of a service, the business that supplies the service must transfer, not merely the service (i.e. the activity) itself
- the enquiry therefore extends beyond the function being performed
- all the various components that constitute the “business” are relevant - e.g. the fixed and movable assets, its goodwill, the workforce, premises, name, contracts with clients or suppliers, and the activity the business performs
- the entity being transferred would necessarily contain all or some of these features

Labour Outsourcing in South Africa

- not sufficient that the entity must merely contain those things – the various components must be sufficiently linked and structured so as to be identifiable as an “entity”
- based on a European Court of Justice case, in order for a going concern transfer to take place, the “economic entity” being transferred must be “*an organised grouping of persons and assets enabling or facilitating the exercise of an economic activity which pursues a specific objective*”
- a “*business*” for the purposes of section 197 must therefore be a coherent grouping of the various elements referred to above
- there is coherence where the entity is sufficiently organised, or structured, and identifiable in relation to the rest of the business of the transferor/client

Labour Outsourcing in South Africa

Going Concern

- the prevailing authority on what constitutes a “going concern” is a decision involving a university and the outsourcing of certain support services, such as the gardening and cleaning services
- according to the Constitutional Court the test for a “going concern” is as follows - *“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 occurred is a matter of fact which must be determined objectively in the light of the circumstances of each transaction. In deciding whether a business has been transferred as a going concern regard must be had to the substance and not the form of the transaction.*

Labour Outsourcing in South Africa

A number of factors will be relevant to the question whether a transfer of a business as a going concern has occurred, such as the transfer or otherwise of assets both tangible and intangible, whether or not workers are taken over by the new employer, whether customers are transferred and whether or not the same business is being carried on by the new employer. What must be stressed is that this list of factors is not exhaustive and none of them is decisive individually. They must all be considered in the overall assessment and therefore should not be considered in isolation.”

Labour Outsourcing in South Africa

- what this amounts to is – (i) taking a “snapshot” of the entity prior to the transfer and assessing its components; (ii) that picture is then compared with the one of the entity after the transfer in order to establish whether it is substantially “*the same business but in different hands*”.
- the decisive criterion is whether the entity in question retained its identity
- generally speaking, it is accepted that minor changes in the manner in which a service is carried out or work is organised post-transfer does not change the fundamental identity of the undertaking that is transferred
- in order to retain its identity, an important identifying feature of the business (e.g. significant assets or a substantial number of employees) must be transferred.
- no factor is more important than any other in determining whether a business has been transferred as a going concern

Labour Outsourcing in South Africa

- the degree of importance to be attached to the various factors will necessarily vary according to the activity carried on and the production or operating methods employed in the relevant business/undertaking

Warning signs/relevant factors

- If the assets, tangible and/or intangible, necessary to run the business (or provide the service) are taken over by the supplier, whether by transfer of ownership or even just right of use (e.g. use of space, inventory, computers, computer network services necessary to conduct the service, vending platform and servers, telecommunication platform, sim cards, etc.)

Labour Outsourcing in South Africa

- If the supplier performs the services in a manner that is substantially similar to how they have been performed previously by the client or a previous supplier
- If employees are taken over by the supplier
- If customers/customer contracts/customer databases are transferred to the supplier
- If the same business or a substantially similar business is carried on by the supplier

Labour Outsourcing in South Africa

Conclusion

- the mere termination of a service contract does not trigger the application of section 197
- the label attached to the transaction (insourcing, outsourcing, a change in service provider) is irrelevant
- the three requirements listed in section 197 must be satisfied
- in the case of labour-intensive businesses, it is unlikely that a transfer only of employees will trigger section 197: South African courts appear to require a transfer at least of some of the means to do the work the employees performed at the outgoing contractor
- the applicability of the section is very fact/circumstance dependent - the factual matrix of the specific case may tip the scales either way in relation to whether section 197 of the LRA may be applicable to an initial or second (or later) generation outsourcing arrangement