Numsa vs SAA - death knell to successful business rescue?

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On Friday, 8 May 2020, the Labour Court upheld an urgent application by Numsa and the SA Cabin Crew Association (the Unions) against South African Airways (SAA) and its business rescue practitioners (BRPs) and ordered that it was procedurally unfair to retrench employees *before* a business rescue plan contemplating such retrenchments was published and adopted.

It is by no means an overstatement that the effect of this judgment, if not urgently overturned on appeal, may render the majority of business rescues unlikely to succeed. At a time when it is reasonable to expect that many businesses may become financially distressed as we grapple with the impacts of Covid-19, this is another disruption-event to contend with that may inadvertently prejudice employees' rights rather than protect them.

Business rescue has, as its purpose, the recovery of financially distressed companies in a manner that balances the rights and interests of *all* stakeholders, being creditors, shareholders, employees and registered trade unions. Where it is impossible to return the company in business rescue to solvency, the secondary aim is to achieve a better return for stakeholders, including employees, than the immediate liquidation of the company would have yielded.

Two options

The future looks undeniably bleak for SAA. The SAA BRPs say that there are only two options left – a structured wind-down which will involve the termination of employment by agreement, or SAA's liquidation. To this end, the SAA BRPs issued notice to employees in terms of section 189(3) of the Labour Relations Act 66 of 1995 (the LRA) to consult and reach agreement on the retrenchment of all employees of SAA. At the conclusion of the consultative process, it is envisaged that the SAA BRPs will have the right to retrench all of the employees.

The Unions argued that section 136(1)(b) of the Companies Act 71 of 2008 (the Companies Act) only empowers the SAA BRPs to commence with and effect retrenchments if such retrenchments were *"contemplated in the company's business rescue plan"*. Since the SAA business rescue plan had not yet been published or adopted, any attempt to retrench employees was found to be in breach of section 136(1)(b) of the Companies Act.

The Labour Court considered the matter from the vantage point of the Constitutional right to fair labour practices, which is embodied in the LRA. The Labour Court reasoned that if there was an interpretation of section 136(1)(b) that better promotes the preservation of work security, then that interpretation ought to be preferred. Although this is a laudable ideal, it is (in our view) wrong in law. The real question should be whether section 136(1)(b) could be interpreted in line with the LRA and if not, whether a limitation of the Constitutional protections were reasonable (an inquiry which the Labour Court did not make).

The Labour Court held that the Companies Act and section 136(1)(b) did not give the SAA BRPs the right to retrench employees *before* such retrenchments were contemplated in the business rescue plan.

Procedural fairness

The Labour Court's jurisdiction extended no further than to determine whether the intended retrenchments were procedurally unfair. Although there was some procedural wrangling during the SAA retrenchment consultation process (such as the Unions refusing to participate in virtual consultation meetings) this was not the basis of the complaint of procedural unfairness.

The underlying legal issue was that, if the retrenchments were in breach of section 136(1)(b) of the Companies Act, then the SAA BRPs did not have the power to retrench, making their actions unlawful, which would consequently render the retrenchments procedurally unfair.

It was not considered by the Labour Court that, per section 140(1)(a) of the Companies Act, the SAA BRPs have full managerial control of SAA in substitution of its board of directors and pre-existing management, and this is *in addition* to any powers given to them under the Companies Act. As such, unless the Companies Act expressly provided to the contrary, the SAA BRPs could, just like the SAA board of directors, commence and implement retrenchments, provided that they comply with the LRA when doing so.

Employee protection

Why then would section 136(1)(b) prohibit retrenchments *before* a business rescue plan is adopted? In doing so, it would give employees more protection and better rights than they had before business rescue commenced. If one considers that neither creditors nor shareholders who are owed money when business rescue commences can enforce payment of their claims unless through the adopted business rescue plan, why should employees' rights be enhanced over the rights of other affected persons? Such an interpretation runs counter to the notion of balancing the rights of *all* affected persons in business rescue, which is ultimately the cornerstone of any successful business rescue process.

In our view, section 136(1)(b) does no more than to state the obvious. Since an adopted business rescue plan is binding on

all affected persons (whether they voted for or against the plan or did not vote at all - the so-called cram-down provisions in sections 152(4) and 154(2) of the Companies Act), section 136(1)(b) simply wanted to ensure that the adopted business rescue plan did not give the company the right to retrench employees without following the procedures set out in the LRA.

In other words, it merely reaffirms and embeds the right to fair retrenchments, and in this regard limits what the business rescue plan can achieve. It does not create a moratorium on retrenchments before the business rescue plan is published and adopted.

BRP details

This is underscored by section 150 of the Companies Act, which sets out what information a business rescue plan must contain so that affected persons can decide whether or not to accept or reject the proposed business rescue plan. Section 150(2)(c)(ii) of the Companies Act provides specifically that the proposed business rescue plan must state the effect, if any, that the business rescue plan contemplates on the number of employees and their terms and conditions of employment (which could include possible retrenchments).

There was no intention in section 136(1)(b) to create a moratorium on retrenchments *before* the publication and adoption of the business rescue plan, but rather to ensure that the effect of an adopted business rescue plan does not give rise to any unfair or unlawful retrenchments.

Impact of Covid-19

When one considers that the ramifications of Covid-19 may cause many businesses to become financially distressed and that they may have to file for business rescue, this judgment then also puts many of those rescues at risk of failure.

If, for example, a mine becomes distressed and commences business rescue, the complexity of mining operations and the need to secure capital or post commencement finance to restructure the business affairs of mines make it unrealistic to expect a business rescue plan to be published in 25 days from the date of the appointment of a BRP. If mines cannot operate in business rescue because of financial distress, very often their only option is to retrench some (if not all) employees, place the operations on care and maintenance and then develop a business rescue plan for its restructure and continued solvency.

It will, in most cases, be financially impossible for a company and the BRP to pay employees until a business rescue plan is published and adopted, exacerbated by the costs of paying such employees for the 60-day period of consultation, which would only commence on the adoption of the business rescue plan.

If this is not the death knell to successful business rescues, it is at the very least a significant complication to the development of a successful business rescue plan.

The effect of this judgment is to strip the BRP of one of the options in the interim to preserve the viability of the business by reducing expenses, one such expense often being a bloated salary and wage bill (as was contended for in the case of SAA). It adds more pressure on the distressed business to produce commercially sound proposals to affected persons in a business rescue plan.

It ignores and further undermines the statutory prescript of section 141(2) that if the BRP at any time determines that the company cannot be rescued, the BRP must apply for the liquidation of the company (a scenario in terms of which the business and any hope of future re-employment comes to an end). This judgment makes this more likely, not only for SAA, but also for other companies in business rescue and in doing so it undermines one of the fundamental tenets of business rescue.

Voluntary severance packages

The Labour Court also confirmed that nothing prevents a BRP from offering voluntary severance packages to avoid retrenchment before the business rescue plan is published. This does not make sense, because in the context of business rescue, the mere fact that voluntary severance packages have been offered (as an alternative to retrenchment) is indicative that retrenchments were already contemplated. It is difficult to comprehend that a voluntary severance package could be offered prior to the adoption of the business rescue plan, but a section 189 consultation process could not commence, as this interpretation by the Labour Court suggests.

The Labour Court's interpretation of section 136(1)(b), as one of its unintentional consequences, may very well prejudice the rights of employees to participate in meaningful consultations with a view to finding alternatives to their retrenchment (as the delay in doing so, may overtake the available options).

In our opinion, this judgment unfortunately gets it wrong. Employees are still protected against unfair retrenchments but such protection does not equate to a moratorium against retrenchments until such time as the business rescue plan (expressly including retrenchments) is adopted.

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