MEMORANDUM: LIMITATIONS ON THE APPLICATION OF UNFAIR DISMISSAL LAW TO HIGH-EARNING EMPLOYEES

1. The purpose of this memorandum is to provide a brief justification for proposed amendments to the Labour Relations Act 66 of 1995 (LRA) which would limit the application of section 188 containing the Act's protections against "ordinary" unfair dismissal to high-paid employees. The Bill tabled in Parliament proposes to include a new section 188B in the Act for this purposes. (These employees would remain fully entitled to the protections against "automatic" unfair dismissal on a range of grounds, including discrimination, set out in section 187(1)).

2. This memorandum briefly discusses the purpose of the proposed amendments; sets out the applicable international standard; summarises the laws of various jurisdictions where similar exclusions apply and addresses the constitutionality of the exclusion.

Purpose of the LRA and the amendment

3. The primary rationale behind the LRA's unfair dismissal provisions is to protect vulnerable employees in light of the inequality in the bargaining positions of the parties to most employment contracts.

4. In the Constitutional Court case of *Sidumo v Rustenberg Platinum Mines*,[1] Judge Navsa explained:[2]

> *"...security of employment is a core value of the Constitution which has been given effect to by the LRA. This is a protection afforded to employees who are vulnerable. Their vulnerability flows from the inequality that characterises employment in modern developing economies. The relationship between employer and an isolated employee and the main object of labour law is set out in the now famous dictum of Otto Kahn-Freund:*

[1] 2008 (2) SA 24 (CC)
[2] At paragraph [72].

'(T)he relation between an employer and an isolated employee or worker is typically a relation between a bearer of power and one who is not a bearer of power. In its inception it is an act of submission, in its operation it is a condition of subordination, however much the submission and the subordination may be concealed by that indispensable figment of the legal mind known as the 'contract of employment'. The main object of labour law has always been, and we venture to say will always be, to be a countervailing force to counteract the inequality of bargaining power which is inherent and must be inherent in the employment relationship.'"

5. The conclusion of employment contracts by senior executives and other well-paid employees is not characterised by the same inequality of bargaining power. The leading labour lawyer Andre van Niekerk (now a Judge of the Labour Court) notes in a widely-cited paper written in 2007:

> *"[M]ost supervisory and managerial employees are excluded from the hours of work provision in the Basic Conditions of Employment Act. The rationale for this exclusion is the bargaining power generally enjoyed by the class of employees able to negotiate the terms of their employment contracts. That being so, why should the same exclusion not apply to unfair labour practices, or to unfair dismissal laws? Employees who are able to negotiate their hours of work and rights to any payment for overtime work ought to be capable of negotiating rights to security of employment."*[3]

6. Terminating the services of senior, highly-paid employees has proved disproportionately expensive, time-consuming and prejudicial to the operations of employers. Not only do such employees often occupy special positions in relation to their employers, so that there may be legitimate reasons to wish to terminate their services which do not fit comfortably within the LRA's grounds for a fair dismissal. There is also a growing perception[4] that they have the resources to draw out dismissal disputes in order to pressure their employers into substantial settlements.[5] Often this has the

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[3] Andre van Niekerk *Regulating Flexibility and Small Business: Revisiting the LRA and BCEA* DPRU Working Paper, March 2007, at page 2.

[4] Comments to this effect are contained in both the National Development Plan and the New Growth Path.

[5] The case of *Brereton v Bateman Industrial Corporation Ltd* (2000) 21 ILJ 442 (IC), although decided under the pre-1995 LRA, is an excellent example of the kinds of abuse which the amendment seeks

result that where a new managerial team takes over a company, it is required to spend a considerable period of time dealing with disputes with the previous managers, rather than being able to focus on the future direction of the business.

International standards and comparative law

7. The international standard informing South Africa's employment protection legislation is the International Labour Organisation's Convention on Termination of Employment (Convention 158 of 1982). Although South Africa has not ratified Convention 158, the Constitutional Court has acknowledged that Article 4 of the Convention (regarding justification for termination of employment), lays the foundation for the LRA's provision that a dismissal may only be effected for a fair reason relating to the employee's conduct or capacity or the employer's operational requirements.[6]

8. Article 2(5) of the Convention contemplates that measures may be taken:

> *"to exclude from the application of this Convention or certain provisions thereof ...limited categories of employed persons in respect of which special problems of a substantial nature arise in the light of the particular conditions of employment of the workers concerned or the size or nature of the undertaking that employs them."*

9. The ILO's General Survey on Convention 158 makes it clear that one of the categories of employees whose possible exclusion is envisaged by this clause is managerial staff.

> *"During the drafting of the Convention, it was considered that a certain amount of flexibility was required, in particular to allow member States to exclude certain categories of workers to whom it was particularly difficult to extend certain aspects of the protection afforded by the*

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to counter. The Applicant claimed millions in a trial lasting 120 court days and involving five advocates, including Senior Counsel on both sides. The Applicant's claim was eventually dismissed with costs. See also van Niekerk *Regulating Flexibility* (2007) at page 15.

[6] *Equity Aviation Services (Pty) Ltd v Commission for Conciliation, Mediation and Arbitration and Others* (2008) 29 ILJ 2507 (CC).

Convention. The examples mentioned in this context included...managerial staff...[7]

10. In commenting on this provision of Convention 158, van Niekerk notes:

> *"Contrary to the flexibility recognised and extended by international standards through the mechanism of selective application, protection against unfair dismissal in South Africa extends to all workers, except those limited categories of persons excluded from the Act itself....[I]n South Africa...no categories of workers are excluded on the basis of special problems arising out of their conditions of employment."*[8]

11. The author goes on to observe that many other jurisdictions exclude categories of employees, including managerial staff, from the application of unfair dismissal laws, and concludes:

> *"In terms of international norms it is not uncommon to exclude senior managerial employees... These exclusions are premised on the basis that employees in these categories are able to negotiate adequate protections in terms of the contractual arrangements that they conclude with their employers. The limitation of work security rights by reference to an earning threshold should be further considered."*[9]

12. The table attached to this memorandum summarises the legal position some 20 countries in which executive, managerial or highly-paid employees are excluded, to a greater or lesser extent, from the ambit of employment protection laws.[10] In summary, the table shows that such exclusions are common internationally and that there are three primary mechanisms: excluding specifically defined categories of employees (eg: managers), excluding employees above an earnings threshold and limiting their remdies by, for example, capping compensation awards.

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[7] Paragraph 67.
[8] *Regulating Flexibility* (2007), page 15.
[9] Van Niekerk *Regulating Flexibility* (2007), page 15.
[10] The table is not an exhaustive summary of the position in other countries and was prepared from material accessible through the ILO web-site in a short period of time.

Reasonable and justifiable limitation on the right to fair labour practices

13. In accordance with the Constitutional Court's jurisprudence, assessing the constitutionality of the exclusion of highly-paid employees from the LRA's "ordinary" unfair dismissal protections involves a two-stage analysis:
    a. does the exclusion amount to a limitation of the right to fair labour practices entrenched in section 23 of the Constitution?
    b. if it does, is the limitation justifiable under the limitations clause, section 36?

14. Assuming, for present purposes, that the exclusion constitutes a limitation of high-earning employees' rights to fair labour practices, the question is then whether the limitation meets the requirements of the limitations clause.

15. In terms of section 36, a constitutional right may only be limited by a law of general application to the extent that the limitation is reasonable and justifiable in an open and democratic society based on human dignity, equality and freedom, taking into account all relevant factors, including: the nature of the right; the importance of the purpose of the limitation; the nature and extent of the limitation; the relation between the limitation and its purpose; and less restrictive means to achieve that purpose.

16. Determining whether or not a limitation is reasonable and justifiable for these purposes "involves the weighing up of competing values, and ultimately an assessment based on proportionality."[11] Thus: "the Court places the purpose, effects and importance of the infringing legislation on one side of the scales and the nature and effect of the infringement caused by the legislation on the other. The more substantial the inroad into fundamental rights, the more persuasive the grounds of justification must be."[12] It should also be borne in mind that the Constitutional Court takes care not to second-guess the legislature on questions of policy.

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[11] *S v Makwanyane* 1995 (3) SA 391 (CC) para [149].
[12] *S v Bhulwana* 1996 (1) SA 388 (CC) para [18].

17. Applying these principles to the present issue: the proposed amendments are intended to address a situation where terminating the employment of high-earning employees is notoriously and disproportionately time-consuming, difficult and expensive. The amendments are further intended to prevent the wasteful abuse of the CCMA's resources; allow employers greater flexibility in dealing with senior employees; and generally increase efficiency, with significant social and economic benefits. This important purpose could not be properly achieved by any less restrictive means.

18. As has been pointed out above that the primary rationale behind unfair dismissal legislation is to protect vulnerable employees in light of the inequality of bargaining power which characterises their employment relationships. This is explicitly recognised in the clause which requires the Minister of Labour to take into account "the extent to which employees, by reason of their earnings level, level of skill or position, have sufficient bargaining power to ensure that adequate provision may be made in their contracts of employment for protection against unfair dismissal." This will ensure that the threshold cannot be set inappropriately low. (It should be noted that the advantage of a threshold is that it provides greater certainty than the use of a term such as "manager" or "supervisor" which be subject to different interpretations.

19. Employees earning above the threshold set by the Minister would remain entitled to protection against unfair dismissal on the grounds listed in section 187(1) (a) to (f) and (h) of the LRA as well as unfair labour practices. In addition, they would be able to negotiate protections in their contracts of employment and challenge any breach of these in either the Labour Court or the High Court. In balancing the competing interests involved, it should also be borne in mind that employers as well as employees enjoy the right to fair labour practices (albeit to a lesser extent).

20. Recent debates have focussed on the role of the high level of earnings inequality in South Africa as a factor contributing to the increase in strike action and the recent unprocedural industrial action that emerged in the

mining sector and other industries. It is arguable that the fact that high-paid employees have full protection against unfair dismissal has increased their bargaining power when negotiating terms and conditions of employment with their employers and that this has contributed to earnings inequality.

21. The principle of limiting the application of labour law provisions to certain categories of employees earning above a remuneration threshold is well-established in South African law. These include the exclusion of employees above a threshold from certain provisions of the BCEA dealing with hours of work; the fact that the presumption of employment in section 200A of the LRA and section 89A of the BCEA does not apply to employees above a threshold and the caps on the benefits that high-earning employees can receive under the Unemployment Insurance Act, 2001 and the Compensation for Occupational Injuries and Diseases Act, 1993.

22. The fact that a large number of the countries, as indicated by the attached table, to a greater or lesser degree exclude managerial, executive or high-earning employees from the application of their respective employment protection statutes (in line with the applicable international standard), is a very strong indication that such an exclusion is reasonable and justifiable in an open and democratic society.

23. In light of the above, the proportionality analysis set out above leads to the conclusion that the exclusion of high-earning employees from protection against "ordinary" unfair dismissal as proposed in the LRA Amendment Bill is reasonable and justifiable in the context of the test for limitations set out in section 36 of the Constitution. For this reason, the proposed section 188B would withstand constitutional scrutiny.

24. Further, the Courts would, in the light of this, regard the choice of technique for achieving such a limitation to be a matter with the appropriate purview of Parliament.

PAUL BENJAMIN

CAPE TOWN, NOVEMBER 2012

COMPARATIVE TABLE ON THE LIMITATION OF HIGHLY PAID / SENIOR EMPLOYEES' LABOUR RIGHTS (PARTICULARLY RELATING TO UNFAIR DISMISSAL):[13]

Jurisdiction:	Nature of limitation:
Angola	Certain categories of employees, including those in managerial positions, are excluded from the scope of Angola's employment protection legislation, the General Labour Act.
Austria	'Managers and directors', amongst other categories of workers, are excluded from the Works Constitution Act, the statute containing the country's employment protection provisions.
Australia	Most senior executives are excluded, through the operation of a 'high-earnings threshold', from bringing unfair dismissal claims under the Fair Work Act 2009.
Bangladesh	"[A] person employed mainly in an administrative or managerial capacity" is excluded from the definition of "worker" in Bangladesh's Labour Act. As such, the country's employment protection provisions do not apply to managerial employees.
Canada	'Managers' are excluded from the hours of work and unjust dismissal protections available under the federal Canada Labour Code. 'Superintendents' and employees 'exercising management functions' (who, for the purposes of the Code, fall below 'managers' in an organisation's hierarchy) are excluded only from the hours of work protections. Whether or not an employee falls within one of these categories is

[13] In addition to the jurisdictions included in the table, at least the following countries also exclude executive or managerial employees from the scope of labour legislation to a greater or lesser extent: Chile; Estonia; Kyrgyzstan; Russia; Viet Nam; and Zambia. (See http://www.ilo.org/dyn/eplex/termdisplay.sourceScope).

	determined with consideration to various factors relating to that employee's functions, level of authority, and so on, and thus depends on the facts of each case.
Ethiopia	"Contracts relating to persons holding managerial positions" are excluded from the application of Ethiopia's Labour Proclamation Act.
Germany	Managers and executives are excluded from certain provisions (including the general dismissal protections) of Germany's Protection Against Dismissal Act.
Italy	Italy's employment protection legislation does not cover managers and directors.
Portugal	Portugal's Labour Code sets out specific rules applicable to the termination of senior managers' employment. Most notably, the Code allows for the conclusion of 'service commission contracts' with a relatively broadly defined category of managerial employees, in terms of which employment may be terminated on notice by either party without having to give reasons, provided that certain notice and severance pay requirements are observed.[14]
Singapore	Those employed in "managerial, executive or confidential" positions are not covered by the employment protections set out in Singapore's Employment Act (by virtue of being excluded from that Act's definition of "employee").
Slovenia	Under Slovenia's Employment Relationship Act, contracts of employment with managerial employees may derogate from the

[14] These requirements are as follows: employees must be given either 30 or 60 days notice, depending on their length of service; in either case payment may be given in lieu of notice; and in cases where employment is terminated without any fault on the part of the employee, the latter is also entitled to a month's severance pay for every year's service.

	provisions of that Act, including in relation to termination of employment.
Sweden	Managerial executives or employees occupying equivalent positions are excluded from the application of the Employment Protection Act, which contains the country's unfair dismissal protections. The provision is given a restrictive interpretation, so that, for example, employees who perform managerial functions but do not benefit from the high wages and other perks associated with such a position, will not fall within the exclusion.
Turkey	Managerial employees are excluded from the job security provisions (which require termination of employment to be justified by a valid reason) of Turkey's Labour Act.
United Kingdom	Although compensation awards in cases of unfair dismissal are generally determined with reference to a claimant's earnings, the Employment Rights Act limits the maximum amount of compensation payable in any case to a fixed sum, rather than to a multiple of the dismissed employee's wages (as in South Africa, where the upper limit for compensation in an unfair dismissal claim is set at 12 months' wages). This has little effect on the unfair dismissal claims of most employees – who would not usually expect compensation in the region of the limit in any case – but reduces employers' risks of facing crippling awards when dismissing high earning employees. It also means that high earning employees will in some cases be limited to lower awards in relation to their earnings than other employees. The compensation limit does not apply to discrimination claims.

United States	Managerial or executive employees are excluded from the application of the National Labor Relations Act.