RULE OF LAW PROJECT

a division of the

FREE MARKET FOUNDATION

16 March 2018

SUBMISSION TO THE

PORTFOLIO COMMITTEE ON LABOUR

ON THE

LABOUR RELATIONS AMENDMENT BILL, 2017

Johannesburg PO Box 4056 | Cramerview 2060 | **Tel** 011 884 0270 | **Email** martinvanstaden@fmfsa.org
NPO No 020-056-NPO | PBO & Section 18A(1)(a) No 930-017-343

Contents

1. Free Market Foundation and Rule of Law Project

The Free Market Foundation (FMF)[1] is an independent public benefit organisation founded in 1975 to promote and foster an open society, the Rule of Law, personal liberty, and economic and press freedom as fundamental components of its advocacy of human rights and democracy based on classical liberal principles. It is financed by membership subscriptions, donations, and sponsorships.

Most of the work of the FMF is devoted to promoting economic freedom as the empirically proven best policy for bringing about economic growth, wealth creation, employment, poverty reduction, and greater human welfare for all, especially the poor.

The FMF's Rule of Law Project is dedicated to promoting a climate of appreciation throughout South Africa, among the public and government, of what the Rule of Law really is, and why it is an essential precondition for peace, liberty and prosperity; continually improving the quality of South African law; identifying problematic provisions in existing and proposed laws, and, where feasible, advocating rectification.

2. Introduction

On 21 February 2018 Parliament's Portfolio Committee on Labour opened a call for comments on the Labour Relations Amendment Bill, 2017. The Bill, *inter alia*, proposes "to provide criteria for the Minister before the Minister is compelled to extend the collective agreement as contemplated in the Act" and "to provide for the renewal and extension of funding agreements".

This submission highlights the general principles of labour regulation that a government hoping to create employment and prosperity must bear in mind, and a comment on the proposed amendments to section 32 of the Labour Relations Act.

The proposed legislation is probably unconstitutional, for reasons given below.

3. General principles

3.1 No free lunch

The discourse on labour law and policy tends to focus on details at the expense of basic truths. Arguably, the only immutable "law" of economics that is that "there ain't no such thing as a free lunch" (TANSTAAFL). The implication of this law is of critical importance in South Africa since it is seldom acknowledged, especially in the context of labour. An inescapable fact is that all benefits have costs and – or all advantages have disadvantages – that the benefit of mandatory improvements in working

[1] www.freemarketfoundation.com

conditions, wages and job security are achieved by the imposing on others fewer jobs, less investment, lower growth, substitution of technology for labour, adverse conditions for the formally unemployed, and retarded prosperity for all. Economic theory predicts and the world's experience confirms that it is impossible to have the former without the latter, that coercive benefits for a privileged few harms everyone else.

Former President Zuma declared job creation as the leading national priority. Economic theory and the world's experience suggest that all the jobs he envisages can be created with relative ease and certainty. The challenge is not how to increase employment and prosperity for all, but whether the government has the political wisdom and will to do the right thing. If it does so, it will be politically popular and its citizens will be economically prosperous.

The measures necessary to increase employment are mercifully straightforward yet curiously difficult to articulate. Laws and policies that increase the cost, risk and difficulty of employing people, as the proposed measures do, necessarily have benefits for a few at the expense of transformation, the unemployed, SMMEs, and generalised prosperity.

Given the priority of job creation, our proposal is that the existing measures should not be considered for implementation in isolation, but that the government should undertake a comprehensive review of relevant laws and policies, and retain only those that reduce unemployment immediately without harming the working conditions, incomes and job security of the employed. The precondition for that to happen is the implementation of laws and policies that increase demand for labour rather than draconian legislation that reduces it.

Increased demand for labour, namely conditions that promote capital formation, skills, and the desire for hiring more employees, is the only sustainable means of achieving two otherwise irreconcilable objectives: more jobs and improved working conditions. In a static or low growth economy, one of these can be achieved only at the expense of the other. Both can be achieved only under conditions of economic prosperity.

It is therefore recommended that the envisaged measures not be proceeded with. Instead they should be included in a comprehensive response to the former President's call for "jobs, jobs, jobs". It is recommended that the government include in such a comprehensive policy review not only all existing and proposed labour law and policy, but all other measures that are of direct relevance. Such other measures include the proposal repeated by the former President in two State of the Nation addresses, by Minister Ebrahim Patel and others, that there should be a review of laws and policies impacting small business so that it is easier for small business to operate and prosper in general and so that small businesses create more jobs in particular. Comprehensive review of measures to increase

employment should consider all disincentives to savings and investment, both by local and foreign investors.

There are two broad categories of policy available to government if it wants to create jobs. The first is to discontinue measures that discourage and penalise employment, and the second is to implement new measures that encourage and reward employment, including self-employment.

3.2 High levels of job security have costly consequences

Labour laws that increase the job security of those already in employment cannot avoid interfering with the contractual rights of both the unemployed and potential employers. If that were not so, there would be nothing to prevent job-seekers from contracting freely with firms on mutually agreeable terms. Given unrestricted freedom of contract, no one should be unemployed other than those who are holding out for higher wages or better conditions.

Onerous termination requirements, minimum conditions of employment, compulsory minimum wages and other regulatory conditions imposed on employers, all serve to consign some people to the ranks of the permanently unemployed. This is because the sum total of their wages and the costs to the employer of complying with the labour regulations exceed the economic value of their expected production.

Compliance costs include the time required to understand the legislation and to implement and maintain the administrative processes needed to avoid contravening the laws, and the potential executive time, professional fees and other costs related to an inadvertent contravention.

3.3 Small firms and complex regulations

Many small firms are incapable of dealing with the complexities of regulations and respond by refraining from hiring staff. Compliance costs are similar for high-wage and low-wage employees, which means that they constitute a greater percentage of the total cost of employing low-wage workers. They are therefore a greater deterrent to the employment of unskilled than skilled workers.

Wealthy countries tend to adopt more demanding labour laws than others and the detrimental consequences become increasingly visible over time. Even highly developed European countries are finding that they can no longer afford onerous labour laws and comfortably provide social grants (the dole) to the resultant unemployed. Germany, well known for its ‘labour democracy’, has revised its labour laws in an attempt to reduce the cost and level of unemployment.

3.4 Inflexibility of labour laws

South Africa’s labour laws are as inflexible as those of Germany, France and Italy, and considerably more inflexible than those of the United States, United Kingdom, New Zealand and Chile. Hong Kong,

Singapore and Taiwan, by comparison, have greater freedom of contract in their labour markets. Comparisons of levels of inflexibility have to be viewed in context, in light of circumstances prevailing in the countries being measured, and taking into account that effects vary according to the strictness of enforcement. For instance, whereas South Korea's labour laws appear to provide job security at a similar level to that in South Africa, the consequences are very different because South Korea has weak labour unions and the laws are not strictly applied, while South Africa's unions are politically powerful.

According to the International Monetary Fund (IMF), South Africa's labour laws are not more inflexible than those of the Organisation for Economic Co-operation and Development (OECD) countries. However, that does not mean that they are appropriate for our circumstances. For one thing, South Africa has an appreciably higher number of unskilled and semi-skilled people than the OECD member states. Since the administration and labour law compliance costs of employing an unskilled worker can be equal to or higher than the costs of employing a skilled person, employers tend to hire skilled people in preference to the unskilled. In this way, regulation creates a serious bias against the employment of the unskilled.

Most importantly, all OECD countries have full or nearly full employment. South Africa, on the other hand, has one of the world's highest – probably the highest – level of sustained unemployment. The biggest victims are young black women. Two out of every three young black women are unemployed and have zero prospect under if the current proposals are enforced of ever being employed lawfully.

3.5 Regulatory bias against the employment of low-skilled workers

Countries such as South Africa that have many low-skilled job seekers usually also have large numbers of existing and potential low-skilled employers, who do not have the capacity to administer and comply with the requirements of complex labour laws. Inflexible labour laws then have a doubly retarding effect on the employment of labour: not only do they price unskilled people out of the labour market, they also prevent low-skilled people from becoming employers. Relief for both employees and employers at the lower end of the South African job market could consequently bring about both a significant reduction in unemployment and an increase in the number of labour-intensive firms.

4. The Rule of Law

Section 1(c) of the Constitution provides that South Africa is founded upon the supremacy of the Constitution and the Rule of Law. Section 2 provides that any law or conduct that does not accord with this reality is invalid. This co-equal supremacy between the text of the Constitution and the doctrine

of the Rule of Law remains underemphasised in South African jurisprudence, but it is important to note for the purposes of this submission.

One of the Constitutional Court's most comprehensive descriptions of what the Rule of Law means was in the case of *Van der Walt v Metcash Trading Ltd*.[2] In that case, Madala J said the following:

> "[65] The doctrine of the rule of law is a fundamental postulate of our constitutional structure. This is not only explicitly stated in section 1 of the Constitution but it permeates the entire Constitution. The rule of law has as some of its basic tenets:
>
> 1. the absence of arbitrary power – which encompasses the view that no person in authority enjoys wide unlimited discretionary or arbitrary powers;
> 2. equality before the law – which means that every person, whatever his/her station in life is subject to the ordinary law and jurisdiction of the ordinary courts.
> 3. the legal protection of certain basic human rights.
>
> [66] The concept of the rule of law has no fixed connotation but its broad sweep and emphasis is on the absence of arbitrary power. In the Indian context Justice Bhagwati stated that:
>
> 'the rule of law excludes arbitrariness and unreasonableness.'
>
> I would also add that it excludes unpredictability. In the present case that unpredictability shows clearly in the fact that different outcomes resulted from an equal application of the law."[3]

The Rule of Law thus:

- Permeates the entire Constitution.
- Prohibits unlimited arbitrary or discretionary powers.
- Requires equality before the law.
- Excludes arbitrariness and unreasonableness.
- Excludes unpredictability.

The Good Law Project's *Principles of Good Law* report largely echoed this, saying:

---

2 *Van der Walt v Metcash Trading Ltd* 2002 (4) SA 317 (CC).

3 At paras 65-66. Citations omitted.

> "The rule of law requires that laws should be certain, ascertainable in advance, predictable, unambiguous, not retrospective, not subject to constant change, and applied equally without unjustified differentiation."[4]

The report also identifies four threats to the Rule of Law,[5] the most relevant of which, for purposes of this submission, is the following:

> "[The Rule of Law is threatened] when laws are such that it is impossible to comply with them, and so are applied by **arbitrary discretion** […]"

Nobel Laureate, Friedrich August von Hayek, wrote:

> "The ultimate legislator can never limit his own powers by law, because he can always abrogate any law he has made. The rule of law is therefore not a rule of the law, but a rule concerning what the law ought to be, a meta-legal doctrine or a political ideal." [6]

What is profound in Von Hayek's quote is that he points out that *the* Rule of Law is not the same as *a* rule of *the* law. Indeed, any new Act of Parliament or municipal by-law creates and repeals multiple 'rules of law' on a regular basis. The Rule of Law is a doctrine, which, as the Constitutional Court implied in *Van der Walt*, permeates all law, including the Constitution itself.

Albert Venn Dicey, known for his *Introduction to the Study of the Law of the Constitution*,[7] and considered a father of the concept of the Rule of Law, wrote that the Rule of Law is "the absolute supremacy or predominance of regular law as opposed to the influence of arbitrary power, and excludes the existence of arbitrariness, of prerogative, or even wide discretionary authority on the part of the government".[8]

Dicey writes "the rule of law is contrasted with every system of government based on the exercise by persons in authority of wide, arbitrary, or discretionary powers of constraint".[9] He continues, saying the Rule of Law means "the absolute supremacy or predominance of regular law as opposed to the influence of arbitrary power, and excludes the existence of arbitrariness, of prerogative, or even of wide discretionary authority on the part of the government".[10]

The opposition to arbitrary power should not be construed as opposition to discretion in and of itself. Officials use discretion to determine which rules to apply to which situation, and thus some

---

4 Good Law Project. *Principles of Good Law.* (2015). 14.
5 Good Law Project (footnote 4 above) 29.
6 Von Hayek, FA. *The Constitution of Liberty.* (1960). 206.
7 Dicey, AV. *Introduction to the Study of the Law of the Constitution.* (1959, 10th edition).
8 202-203.
9 Dicey (footnote 7 above) 184.
10 Dicey (footnote 7 above) 198.

discretionary power is a natural consequence of any system of legal rules. However, the discretion must be exercised per criteria which accord with the principles of the Rule of Law, and the decision itself must also accord with those principles.

A common example of arbitrary discretion is when a statute or regulation empowers an official to make a decision "in the public interest". What is and what is not "in the public interest" is a topic of much debate, and empowering officials to apply the force of law in such a manner bestows upon them near-absolute room for arbitrariness. The "public interest", however, can be one criterion among other, more specific and unambiguous criteria.

The fact that some discretion should be allowed is a truism; however, the principle that officials may not make decisions of a substantive nature still applies. Any decision by an official must be of an enforcement nature, i.e. they must do what the legislation *substantively* requires. For instance, an official cannot impose a sectoral minimum wage. The determination of a minimum wage is properly a legislative responsibility because it is of a substantive nature rather than mere enforcement. Unfortunately, the Basic Conditions of Employment Act gives the Minister of Labour the authority to make "sectoral determinations" – which includes determining a minimum wage – which is a clear violation of the Rule of Law and the separation of powers.[11]

5. Problematic provisions in the Labour Relations Amendment Bill[12]

The insertion of a new section 32(2A) states that the Minister must publish a notice of extension within 90 days if the registrar has determined that the parties are sufficiently representative for purposes of section 32(5)(a). However, section 32(5) currently has additional criteria contained in sections 32(5)(b)-(d) which the Minister must satisfy herself of before she may decide to extend or not. It is unclear whether these criteria are still applicable from the wording of the proposed subsection (2A). The intention of the amendment apparently is to set time frames; however, the proposed wording is certain to cause confusion as it is seemingly contradicting the current section 32(5).

The insertion of the word "or" between subsections (b) and (c) has the effect that the Minister must in future extend agreements to non-parties in circumstances where only the employer parties or the labour parties to a bargaining council represent the majority of employees, either by way of employment or membership.

---

11 Section 51 of the Basic Conditions of Employment Act (75 of 1997).

12 This section is adapted from the December 2017 submission of the National Employers' Association of South Africa.

This amendment flies in the face of the majoritarianism principles which collective bargaining is based on. It is clearly aimed at benefiting large employers at the expense of SMMEs and to protect entrenched interests. The proposed amendment is in all probability as a result of the increasing discontent expressed by employers regarding the current collective bargaining model. However, instead of addressing the cause of the discontent and the underlying issues, the election was made by the Minister to simply paper over the cracks. This amendment will cause even more discontent and we believe will lead to further business closure and unemployment as SMMEs, which are subjected to completely different economic realities, cannot survive in an environment where they, in terms of wages and other conditions of employment, are dictated to by big business with the intention of eliminating SMMEs' competition. In this regard, we wish to state the following examples:

- the wage versus turnover ratio of a small business may be as high as 60%, whereas in the case of a big business, it may be as low as 5% and even lower;
- the operational realities of a SMME in a rural area cannot be compared to that of a big business situated within an economic hub;
- SMMEs do not enjoy the benefits of economies of scale; and
- in a certain sense big business can be regarded as 'price givers', with the ability to pass on wage increases, by means of the pricing of their products, to the downstream, which comprises mainly of SMMEs. SMMEs, in contrast, are limited in passing on any price increases to customers, resulting in SMMEs effectively paying for both their wage increases and those of big business.

Furthermore, we believe that a second reason for the amendment is the dwindling representativity figures of unions across all sectors. Seemingly the Minister has realised that the unions will not be able to regain the losses in membership they have experienced over the last number of years, which places collective bargaining under threat. This proposed amendment might in fact have the unintended consequence of causing further decline in union membership as the need for recruitment, in the context of collective bargaining, has now been removed. The bizarre situation may now arise where a union party representing 10% of employees in the industry can agree with a majority employer party and extend that agreement to 90% of employees the union does not represent. This will seriously compromise the legitimacy of collective bargaining. It is our submission that this proposal will not pass constitutional muster.

The deletion of section 32(6)(b) effectively allows the Minister to extend the period of operation of agreements (excluding fund agreements) without having to adhere to the provisions of sections 32(3) and 32(5). Therefore, the Minister may extend any agreement, which is not a fund agreement,

indefinitely without taking into account the levels of representativity of the parties or having to ask for submissions in terms of section 32(5)(c). This would allow parties with very low levels of representativity to keep agreements alive perpetually without having any legitimate right to do so. It will also impact on the legal right of non-parties to be heard and it will also not pass constitutional muster.

The insertion of section 32A proposes that the Minister may extend the period of operation of a funding agreement for a period of 12 months at the request of any of the parties to a bargaining council. It is obvious that this proposal infringes on a number of entrenched principles:

- It, without doubt, infringes on the constitutional and collective bargaining principles of majoritarianism.
- It also infringes on the voluntary nature of collective bargaining. The nature of collective bargaining is one of self-determination. It should therefore be up to the parties to decide if and how they wish to fund their council and which benefits they wish to provide. It is not for the legislature to interfere in this dynamic as this interference in itself may cause collective bargaining to become obsolete.
- The Minister may extend the period of operation of fund agreements "where the Minister is satisfied that the failure to renew the funding agreement may undermine collective bargaining at sectoral level …". This seems to be the only criteria of which the Minister must be satisfied. No cognisance is taken of the levels of representativity of parties, which again could create a situation where agreements are kept alive artificially by parties who have no right to do so.

6. Constitutionality

In addition to these fatal flaws in the Bill, it is clear from a seminal full bench judgement of the Gauteng High Court[13] that labour agreements and extensions amount to administrative action as defined n section 33 of the Constitution. Agreements may therefore be concluded or extended only in accordance with the Promotion of Administrative Justice Act, 2000 (Act 3 of 2000) (PAJA). The Bill envisaged non-compliant agreements and extensions.

What the judgment means in practice is that there must be public participation and the objective must be the promotion of public interest, as opposed to the interests of the parties. Legislation may not, as envisaged, negate, subvert or avoid the full implications of the Constitution, PAJA and the judgment.

13 *Free Market Foundation v Minister of Labour and Others* 2016 (4) SA 496 (GP).

If the Bill is adopted and implemented, it will probably be challenged and set aside.

7. Conclusion

Whenever the government interferes in the economy, it distorts prices. Instead of simply focussing on trading and trying to make a profit, firms must spend more on compliance costs and advisors to deal with legislation and regulations, which in turn means, to keep the prices of their goods and services within a range acceptable to the consumer, they end up with less money to spend on hiring more workers or increasing wages. At worst, it often means most firms need to increase their prices regardless of a market-induced desire to lower them in competition with rival firms.

South Africa's labour market competitiveness is lagging behind the developing world. The World Economic Forum ranks South Africa as the 7th-worst country out of 139 countries in the world in terms of its labour laws and regulations. This has created two significant problems for the country: the highest unemployment rate in the world (because labour laws and regulations do not promote job creation) and low rates of economic growth (because South Africa's labour force is unproductive in comparison with its peers, the rest of the developing world).

Two sets of laws are particularly problematic. Firstly, collective bargaining (i.e. the legal process by which business, trade unions and government agree on wage escalations, as opposed to market forces) has caused wage escalations to exceed labour productivity growth over the past 15 years. Secondly, dismissal protections (i.e. legal protections afforded to employees that protect them from dismissal despite performing poorly on the job) have caused labour productivity, on average, to be very low. In order to boost employment and raise economic growth rates, South Africa requires changes to labour laws and regulations that would promote high labour productivity and a concrete, market-based link between productivity and remuneration.

The labour market in South Africa is politically sensitive for many historical reasons. The system of apartheid started as a government policy to exclude blacks from the labour force, so apartheid was, in its essential form, a highly restrictive labour policy. Liberalising the labour market is viewed with great suspicion, especially by black trade unions, which fear that liberalising reforms will revive the apartheid labour system. But the apartheid labour system was not a free market system by any measure. In fact, South Africa has not had a relatively free labour market since the 1890s.

It is recommended that the government include in such a comprehensive policy review, not only all existing and proposed labour law and policy, but all other measures that are of direct relevance. Such other measures include the proposal repeated by the former President in his two State of the Nation addresses, by Minister Ebrahim Patel and others, that there should be a review of laws and policies

impacting small business so that it is easier for small business to operate and prosper in general and so that small businesses create more jobs in particular. Comprehensive review of measures to increase employment should consider all disincentives to savings and investment, both by local and foreign investors.

There are two broad categories of policy available to government if it wants to create jobs. The first is to discontinue measures that discourage and penalise employment, and the second is to implement new measures that encourage and reward employment, including self-employment.

Prepared by:

Leon Louw	Eustace Davie	Martin van Staden
Executive Director	Director	Legal Researcher
Free Market Foundation	Free Market Foundation	Free Market Foundation