edward nathan sonnenbergs

BUSINESSDAY

Business Law & Tax Review

www. problem solved .co.za

July 2008

A review of the Government Gazette and new developments in law

Conciliator's hands are tied

IN A ground-breaking decision, the Labour Appeal Court recently ruled that a conciliator did not have the authority to dismiss a matter at the stage of conciliation. The employee had referred an unfair dismissal to the bargaining council for hearing and had failed to attend the conciliation. The matter was dismissed. The court held that the matter should rather have been set down for arbitration.

In the case of *Premier of Gauteng and others versus Ramabulana NO* the court ruled that the Labour Relations Act does not empower a conciliator or bargaining council to dismiss a matter because of the employee's failure to attend the conciliation. Even though the Commission for Conciliation, Mediation and Arbitration (CCMA) rules provide for a dismissal of a dispute should the referring party not attend, the court held that the rules are ancillary to the act. In the event that they are in conflict or inconsistent with the provisions of the act, the rule will be *ultra vires* or beyond the legal power or authority of a corporation.

In the case in question, the employee was employed by the Gauteng provincial government in the social services and population development department. Following his dismissal a dispute, according to the council rules, was referred to the bargaining council within a 30-day period from the date of dismissal. However, the employee, as well as his union, failed to attend the conciliation set down by the bargaining council. The conciliator dismissed the matter. The union referred a dispute to the bargaining council for conciliation for a second time. That referral was outside the 30-day period from the date of dismissal and it was accompanied by an application for condonation (overlooking or pardoning the offence). The condonation application was opposed by the employer on the basis that the initial referral had been dismissed and therefore the bargaining council did not have jurisdiction to entertain the second referral, including the application. Despite this, a conciliator of the bargaining council granted the union's condonation application.

The matter was then taken on review to the Labour Court. The Labour Court decided the union's condonation application had to be treated as an application for the rescission of the first conciliator's decision in the light of the fact that the bargaining council rules did not make provision for rescission applications. It concluded that the conciliator was correct in granting the condonation application. The employer then appealed to the Labour Appeal Court.

There it was found that if a bargaining council or CCMA receives a referral from a dismissed employee within the 30-day period or, if after the 30-day period, receives a referral with an accompanying condonation application, the bargaining council has an obligation to attempt to conciliate the dispute. The court took the view that it is not necessary for parties to be physically present at the conciliation meeting and that their failure to attend cannot give rise to a dismissal of the matter on that basis.

It was held that the Labour Relations Act does not empower a conciliator or bargaining council to dismiss a matter because of the employee's failure to attend the conciliation. Even though the CCMA rules provide for a dismissal of a dispute should the referring party not attend, the court held that the CCMA rules are ancillary to the act and in the event that they are in conflict or inconsistent with the provisions of the act, the rule will be *ultra vires*. The reasoning behind this is that a conciliating commissioner has no power to deal with the merits of the dispute in deciding whether or not a dismissal is fair, and therefore the conciliator cannot simply dispose of the dispute by dismissing it due to the non-attendance of the employee at the meeting. The CCMA rule must be construed to

Continued on Page

bennett 1 gilwala 2 itzikowitz 3 gluckman 4 collins 5 faber 6 rees 7 de klerk 8
le grange 9 anderson 10 cross 11 rabe 12 tucker 13 wessels 14 blumenthal 15 brand 16 king 17 van der walt 18
loubser 19 wambugu 20 kirsch 21 fazel 22
africa's largest
banking and finance team
23 24 25 26 27 28 29 30 31 32
33 34 35 36 37

johannesburg +2711 269 7600
cape town +2721 410 2500
durban +2731 301 9340
info@problemsolved.co.za

law | tax | forensics

edward nathan sonnenbergs

problem solved

Matter set for arbitrator

Continued from Page 1

mean that the matter was dismissed for purposes of conciliation only and was capable of being referred again to the CCMA or bargaining council.

Section 191(4)of the Labour Relations Act provides that the council or commission must attempt to resolve the dispute through conciliation. Since this judgment, the interpretation of the meaning in matters at the CCMA has not been consistent but in many instances it has been that if one or none of the parties are at conciliation the conciliating commissioner now issues a certificate of outcome, certifying that the matter was unresolved and that it can be referred to arbitration or adjudication depending on the facts case without making attempts to conciliate the dispute.

IT COULD be argued that the rationale for the conciliation process has been undermined as dismissed employees could now refer a dispute to the CCMA alleging unfair dismissal, fail to attend the conciliation meeting and have the matter set down for arbitration. It could further be argued that if the arbitrating commissioner conciliates or attempts to conciliate the dispute prior to proceeding with the arbitration, section 191(4) has been complied with.

This judgment may present further difficulties at the CCMA in that if conciliating commissioners are not authorised to dismiss matters at conciliation stage then they may take the view that points in limine which if granted will dismiss the matter, for example jurisdictional points, cannot be entertained at the conciliation stage. Although this view may represent an erroneous interpretation of the judgment in practice, this may result in a certificate of outcome being issued conferring jurisdiction on the council or commission to arbitrate the matter or Labour Court to adjudicate the matter depending on the facts of the case. If the seminal judgment of the Labour Appeal Court in the *Fidelity Guards Holdings (Pty) Ltd v Epstein No & Others* matter is to be applied in a limited and literal sense jurisdictional points cannot be raised at the arbitration or adjudication stage if a valid certificate of outcome conferring jurisdiction on the council or commission or court to arbitrate or adjudicate the matter has been issued and reviewing and setting aside would therefore be pre-requisite for raising the point in limine.

It is suggested that one will have to monitor how the CCMA and bargaining councils deal with these situations in the light of the Ramabulana judgment.

Suemeya Hanif
Edward Nathan Sonnenbergs

Capital gains risk when winding up or liquidating

THE distribution of profits by a company being liquidated, wound up or deregistered is considered to consist of dividends to shareholders and a return of their investment in the company.

However, these distributions can have unforeseen capital gains tax consequences for the shareholder receiving the distribution.

Distributions to shareholders excluded from the definition of "dividend" in section 1 of the Income Tax Act (such as returns of share capital) are automatically characterised as "capital distributions" under the Eighth Schedule of the Income Tax Act. The receipt or accrual of a capital distribution gives rise to a deemed part-disposal by the shareholder for capital gains tax purposes. The shareholder must calculate a capital gain or loss on the part-disposal by apportioning the base cost of the share according to the ratio of the market values of both the capital distribution and the share, and treating the capital distribution as the proceeds on the part-disposal.

The method of calculation may have the anomalous effect of creating taxable capital gains upon the receipt of, for example, a liquidation distribution comprising retained earnings and a portion of the originally contributed capital.

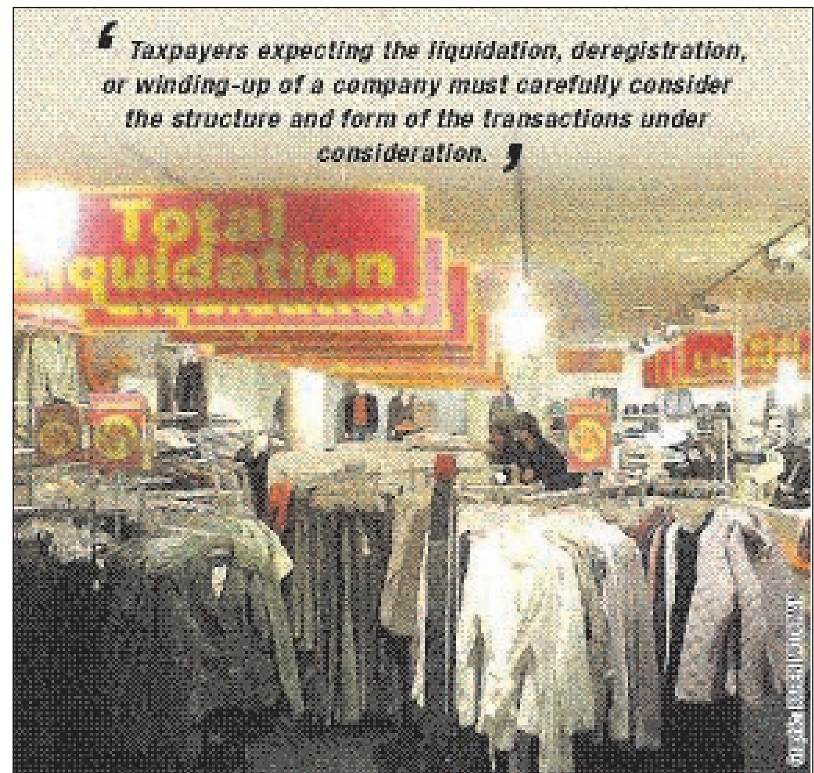
Consider the example of an individual shareholder who subscribed for the only share issued by a company for R10, represented by R1 of share capital and R9 of contributed share premium. The company has since accumulated R2 of retained income, giving the share a market value of R12, and is now being liquidated.

If the company pays out a distribution of R11 in anticipation of its liquidation (representing R9 of share premium and R2 of retained income — everything but the share capital), the following tax implications arise:

- The shareholder receives a tax-exempt dividend of R2 (giving rise to a liability for secondary tax on companies (STC), at a rate of 10%, in the hands of the company); and
- The shareholder receives a capital distribution of R9, giving rise to a deemed part-disposal under paragraph 76A of the Eighth Schedule.

The shareholder must now calculate the capital gain or loss in respect of the part-disposal; the first step is the apportionment of the capital gains tax base cost of the share.

The portion of the base cost attributable to the part-disposal is (R9/R12 x R10), or R7,50 — the capital distribution is R9, the market value of the share is R12 (the act provides that the market value prior to the deemed part-disposal must be used for the calculation), and the original base-cost of the share is R10. The capital gain on part-disposal is thus (R9-R7,50), or R1,50. At the maximum effective capital gains tax rate for individuals, the shareholder is liable for R0,15 of tax.



'Taxpayers expecting the liquidation, deregistration, or winding-up of a company must carefully consider the structure and form of the transactions under consideration.'

IN REALITY, the shareholder has received a dividend of R2 and a return of a portion of the original investment. The shareholder should expect the liquidation distribution to be entirely tax-free. However, the calculation mechanism of the part-disposal rules includes the R2 dividend in the predisposal market value of the share, resulting in "lost" base cost and a taxable capital gain where no capital gain has actually been made.

The above can be contrasted with the position where the company first distributes the R2 of retained income, and subsequently distributes the contributed share premium. In this case, the shareholder receives a tax-exempt dividend, and the market value of the share falls to R10. When the subsequent capital distribution is received, the apportioned amount of base cost attributable to the part-disposal is (R9/R10 x R10), or R9. The capital gain is thus (R9–R9), or nil. By separating the two transactions, the application of the legislation produces a result that is in line with the commercial realities of the transaction.

This article deals solely with the application of the part-disposal rules to liquidation distributions; the situation set out in the above example could also apply in a holding company and subsidiary relationship, where the latter was acquired with existing profits. The distribution of pre-acquisition profits can also result in a capital distribution (through an exclusion in the "dividend" definition), and could also result in capital gains tax upon return of the invested capital to the holding company.

It is clear that taxpayers expecting the liquidation, deregistration or winding-up of a company must carefully consider the structure and form of the transactions under consideration, to prevent the creation of unintended taxable capital gains.

Matthew Marcus
Edward Nathan Sonnenbergs