Agbiz presentation to the Portfolio Committee on Trade and Industry

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Public Hearings on the National Credit Amendment Bill

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agricultural business chamber
the way to prosperity

For Today

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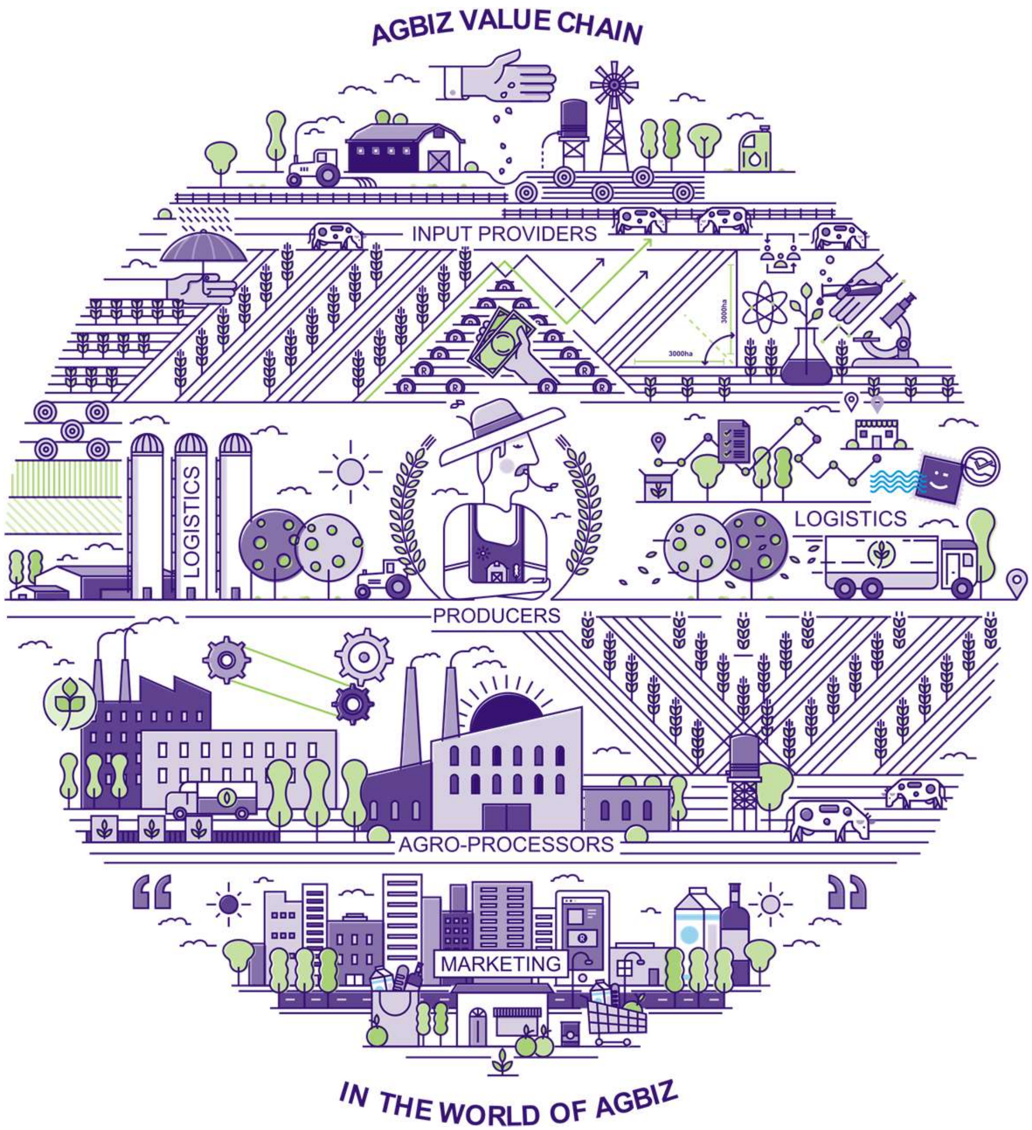
5. Debt intervention
6. Mandatory provision of credit life insurance
7. Enforcement mechanisms



1. Who we are:

- Agbiz represents the agricultural value chain;
- This includes;
  - Input providers such as seed, fertilizer and machinery manufacturers;
  - Financial institutions and insurance companies;
  - Logistics;
  - Off-takers, Agro-processors; and
  - Market linkages.

In essence, the farmer is the client and many of the agribusinesses we represent are registered credit providers.

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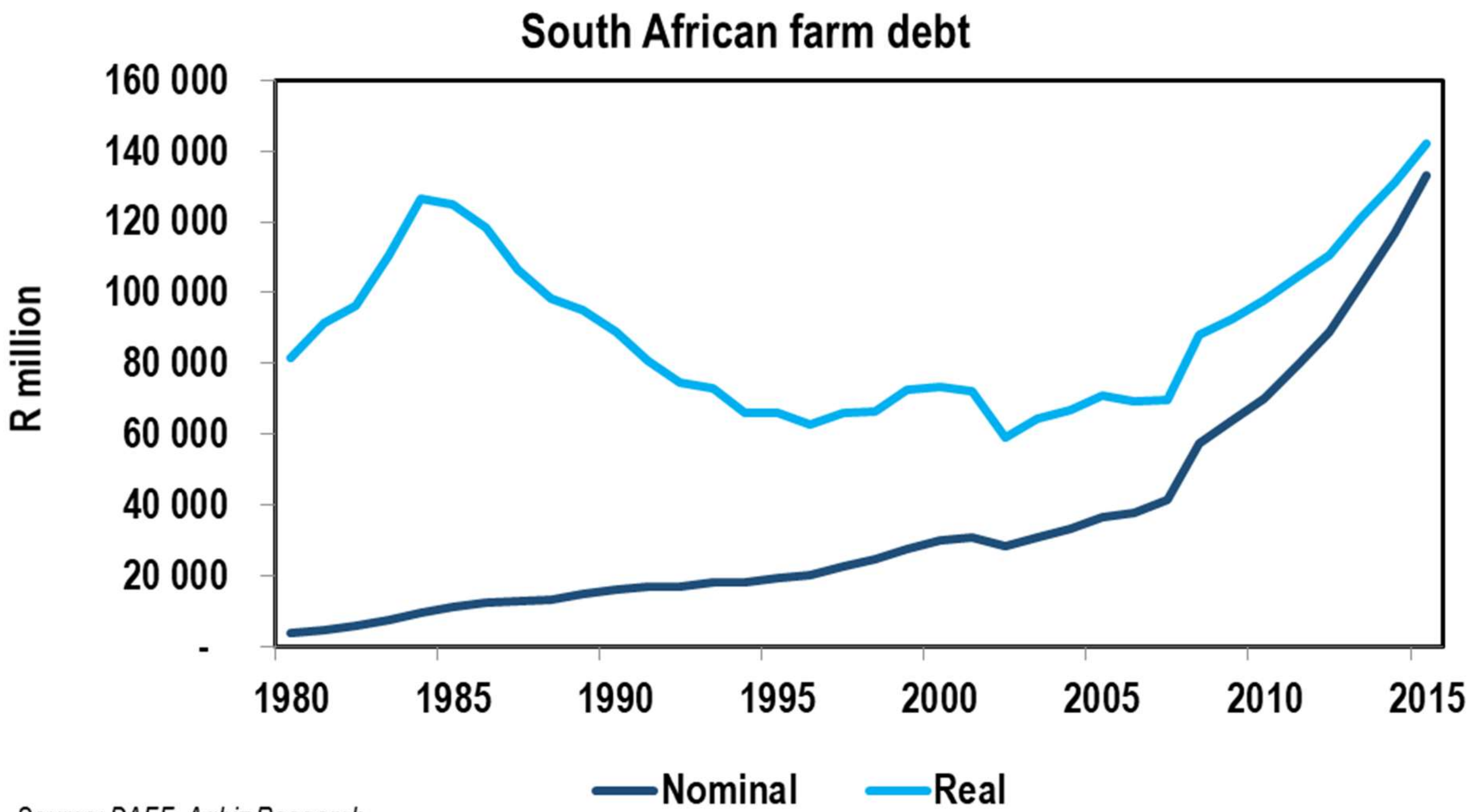
2. Agriculture reliant on credit financing

Agribusinesses finance the sector in several ways, including:

- Long-term bond financing to acquire land;
- Capital to acquire implements such as tractors and harvesters; and
- Production finance for inputs;
  - Seeds, fertilizer, diesel, pesticides etc.
  - Cooperatives/agribusinesses sell these products and provide clients with a credit facility to purchase them.

2. Agriculture reliant on credit financing



Source: DAFF, Agbiz Research

3. Unique nature of agricultural finance

1. Farmers do not have a fixed or even regular income;
   - Farmers rely on credit for their expensed throughout the year and pay off their debts ‘once-off’ after an annual harvest.
2. Many farmers carry on business in their personal capacity;
   - Some farming businesses are juristic persons but the average ‘family farm’ is not;
   - Large credit transactions may take place in the name of a natural person acting as a ‘sole proprietor’, hence they fall within the ambient of the Act;
   - A farmer will therefore have personal expenses as a consumer as well as business transactions.

3. Unique nature of agricultural finance

3. Risk assessment;
    - Agricultural economists are employed to assess the potential of a harvest based on soil type, location, expected commodity prices etc.
    - Prospective based on feasibility of harvest, not retrospective based on ‘earnings’;
    - Obliged to look at existing credit agreements by law but not really useful – clothing accounts, credit cards etc. are of a personal nature and have little bearing on risk assessment for production finance;
    - Multi-peril crop insurance sometimes required to reduce risk;
4. Farmers not always to blame for defaults;
    - Agriculture is subject to the whims of nature – droughts, floods, hail etc. can all affect a crop and are beyond the control of the farmer;
    - Defaults therefore not always predictable – farmer not at fault nor was credit reckless at the time.

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3. Unique nature of agricultural finance

5. Carry-over debt & debt restructuring

- In the event that a harvest is insufficient to satisfy the production finance, the debt is often 'carried-over' to the next production year.
- This means that the remainder of the debt can be satisfied the following year, but it does not preclude the farmer from obtaining credit again to plant in the next season;
- Failure to do so would place food security at risk;
- If the farmer is at fault, penalty interest can apply but in the event of a natural disaster, the repayment terms are simply restructured;

When a disaster occurs, farmers and agribusinesses are in it together. It is unlikely that an agribusiness will sacrifice a long-standing relationship with its clients for short-term gain.

4. Relevance – reckless credit assessments

Reckless credit

- The Bill seeks to:

1. Provide the NCR with the power to suspend reckless credit (Clause 82A);
2. Provide the Tribunal with the powers to declare credit reckless and extinguish the debt (clause 82A read with clause 130 (4) (e) (ii)); and
3. Place an obligation on debt counsellors and other credit providers to report suspected reckless credit agreements (Clause 82A).

In all of the scenarios outlined above, it is of vital importance that the criteria used to assess the risk is understood within the context of agricultural finance, and especially production finance.

4. Reckless credit

NCR's power to suspend a reckless credit agreement

- We believe that there is merit in providing the NCR with greater functions in relation to the investigation of reckless credit, but its ability to unilaterally suspend credit agreements are problematic;
- Such a decision will be administrative action and must comply with a fair procedure;
- The fact that the NCR can initiate, investigate and adjudicate on the matter allows the NCR to be a player and referee;
- The Constitutional Court found in the case of *De Lange v Smuts* that the lack of independence on the part of a decision maker can result in arbitrary decision making, which is contrary to the founding principle of rule of law in the Constitution De Lange v Smuts NO 1998 (3) SA 936 (CC);
- The credit provider should also be entitled to state its case, in line with the *audi alteram partem* principle.
- Proposal: NCR to investigate, Tribunal to decide on suspension;

4. Reckless credit

Tribunal's role in assessing reckless credit

- Both during the NCR's investigation and the Tribunal's decision, it is vital that the unique nature of agricultural finance and risk assessment is understood;

  "section 82 (2) (b) of the NCA:…whether there is a reasonable basis to conclude that any commercial purpose may prove to be successful, if the consumer has such a purpose for applying for that credit agreement."

- The law is sufficient, but Agbiz would welcome the opportunity to assist the NCR to develop a guideline on how to apply this criteria in the context of production finance.
- Secondly, section 80 (b) (ii) states that a credit provider must not have entered into a credit agreement if;

  "(ii) entering into that credit agreement would make the consumer over-indebted."

- In the event that the farmer becomes over-indebted due to circumstances such as drought, hail etc. it should not retrospectively be seen as reckless credit if it was not foreseeable at the time.

4. Reckless credit

Obligation on credit providers & Debt counsellors to report on reckless credit

- As mentioned before, agricultural production finance is not consumer credit in its true form;
- We are therefore very concerned about this obligation as it could be misinterpreted by other credit providers and debt counsellors;
- Credit providers outside the agricultural sector will not know how the risk was assessed when production finance was granted;
- As such, they will not be in a position to assess whether production finance was reckless and vice-versa, agribusinesses will not be able to assess whether their client's personal credit agreements were reckless or not.
- This could negatively affect a farmer in his personal capacity, and an agribusiness could be erroneously reported for reckless credit;

5. Debt intervention

'Once-off' Debt Intervention in terms of clause 88A

- Agribusinesses are typically not involved in micro lending and as such the threshold proposed for debt intervention would likely exclude the majority of credit transactions in the sector;
- Be that as it may, we would urge the Committee to be mindful of the need to balance the interests of the consumer and the credit provider;
- The intention is noble as it seeks to protect the most vulnerable in society; however
- If debt can be extinguished by operation of law, it could raise the risk of lending to these vulnerable members of society;
- Can result in more difficulty in accessing credit or higher interest rates to off-set the increased risk;
- Could have the unintended consequence of promoting credit exclusion.

5. Debt intervention

Debt Intervention to be prescribed

- Clause 88F makes provision for discretionary, ad-hoc debt intervention measures to be promulgated through regulation;
- Sub-clause (2) specifically makes provision for disaster situations:

  "(2) A debt intervention measure contemplated in subsection (1) must address economic circumstances that –

  …

  (b) were caused by a regional natural disaster or similar emergent and that is of grave public interest, which was identified by the Minister by notice in the Gazette as such…"

- Appear to be aimed at creating a special dispensation in the event that a natural disaster, such as the drought experienced in the 2015/2016 production year;
- Once again, the intention is noble however it may be unnecessary as agribusinesses already make arrangements with their clients in these instances.

5. Debt intervention

Debt Intervention to be prescribed

- Agribusinesses are inextricably linked to primary agriculture in a symbiotic relationship – the one cannot survive without the other;
- It will always be in the best interests of agribusinesses to assist producers affected by natural disasters such as drought by restructuring the repayment conditions;
- This is based on affordability and the circumstances of each client – a delicate balance must be reached between what the client can afford and the liquidity needs of the agribusiness;
- This is always done on an ad hoc basis, if a 'one-size-fits-all' intervention is prescribed, it could upset the balance and endanger the long-term survival of either the client or the agribusiness;
- A creditor may not have sufficient liquidity to simply extinguish debt on a grand scale. At the same time it will do all that is possible to prevent its client from becoming insolvent as this endangers food security and future business.

5. Debt intervention

Debt Intervention to be prescribed

- Agribusinesses’ relationship with their clients often span many decades and generations;
- An agribusiness will proverbially ‘shoot itself in the foot’ if it does not come to an arrangement with clients during times of natural disaster;
- When the worst drought in living memory was experienced in the 2015/2016 production year, the stellar recovery of the sector that followed was largely attributable to an ad-hoc process whereby the parties could strike an equitable balance based on the circumstances of each client;
- If an intervention is prescribed that cripples the agribusinesses, farmers may not be able to access the production inputs required to farm once conditions are favourable again;
- Such an outcome would be a tragedy for all involved, and endanger food security.

5. Debt intervention

Debt Intervention to be prescribed

- From a legal point of view; a debt, whether secured or unsecured, should qualify as ‘property’ within the context of section 25 of the Constitution;
- If a debt is ‘extinguished’ by operation of law, it will amount to a deprivation of property which may be challenged in terms of section 25 (1) of the Constitution;
- Could possibly amount to an expropriation without compensation, which is unconstitutional;
- We furthermore believe it is irrational to extinguish debts by operation of law when a natural disaster is per implication a temporary state of affairs which can be remedied by a rearrangement of repayment terms;

Recommendation: delete clause 88F (4) (c)

6. Mandatory provision of 'credit life insurance'

- The new section 106 (1A) places an obligation on a consumer and credit provider to obtain mandatory credit life insurance for debts not exceeding R50 000 over a term of more than 6 months;
- We strongly urge the Committee to reconsider this draft provision for the following reasons:
- The section is only workable if the credit provider can in fact also underwrite a credit life insurance scheme and regulate the costs thereof;
    - Unless the applicant can find an insurer willing to underwrite him/her at the costs prescribed by the Minister, the credit provider will not legally be able to extend credit as it will be in breach of the Act
- This will once again result in credit exclusion of the poor;
- From an agribusiness perspective, life insurance is not typically required as a condition for a credit facility as multi-peril crop insurance is far more relevant;
- A farmer is not a salary earner, as such credit is not extended on the basis of his personal earning potential but rather the earning potential of the anticipated crop, being the commercial purpose for which the credit was extended.

7. Enforcement mechanisms

- Section 157B (1) (d) seeks to criminalise prospective reckless credit agreements;
- There should be sanction, but criminalisation may not be suitable:
    - Burden of proof solely on the state;
    - Onus of proof much higher than in civil cases (proof beyond a reasonable doubt required);
    - Criminalisation would take the decision out of the hands of the NCR into the hands of the NPA;
    - Could result in a low conviction rate or low prosecution rate as it must compete for resources against cases where violent crimes were committed.

Recommendation: administrative fine more streamlined

Thank you

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