The Chairperson
Parliamentary Ad-Hoc Committee to Initiate and Introduce Legislation
Amending Section 25 of the Constitution
c/o Mr V Ramaano
3rd Floor, 90 Plein Street
Cape Town
8001

By Email: section25@parliament.gov.za

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Dear Sirs

JOINT SUBMISSION TO THE PARLIAMENTARY AD-HOC COMMITTTEE TO INITIATE AND INTRODUCE LEGISLATION AMENDING SECTION 25 OF THE CONSTITUTION BY SAPOA AND SAREIT.

1. The South African Real Estate Association ("SAREIT") represents all SA Listed REIT's on the JSE, together with the South African Property Owners Association ("SAPOA"), which is the representative body and official voice of commercial and industrial property in South Africa, hereby makes its formal submission.

2. South Africa's property industry, excluding agriculture, is currently estimated to be valued at R8 trillion. From the Property Sector Charter Council's Report, residential property accounts for three quarters of the value at R3.9 trillion. Commercial property carried a value of R1.3 trillion with R790 billion held by corporates, R300 billion held by Reit's, listed on the stock exchange, R130 billion by unlisted property funds and R50 billion by life and pension funds.

3. In a letter dated 14 June 2018, which is attached as Annexure A, SAPOA submitted representations to the Joint Constitutional Review Committee on the Review of Section 25 of the Constitution.

4. The conclusion of the submission was that:

   4.1 The call for Expropriation Without Compensation ("EWC") in the field of land reform has, from an economical and legal point of view, a strong probability of landing the Republic of South Africa in international controversy and disastrous consequences for the economy;

   4.2 It is unnecessary to amend the Constitution as Section 25(3) of the Constitution is flexible enough to provide in certain exceptional circumstances for minimal or no compensation being awarded where it is just and equitable to do so; and

   4.3 The amendment of the Expropriation Bill is possible without infringing upon international law and without successful challenge in terms of Section 31(1) of the Constitution, if the principles set out in the letter of 14 June 2018 are adhered to.

5. Whilst we are encouraged by the ANC's resolution that the Government will "*not undermine future investment in the economy, or damage agricultural production or food security (and that) …..interventions must not cause harm to other sectors of the economy*", we believe that the matter needs to be dealt with carefully or it could cause further damage to the economy.

6. The Economic consequences of EWC are well documented in an academic paper, written by University of Pretoria Gordon Institute of Business Science (Gibs) academic Roelof Botha and University of Johannesburg Professor Ilse Botha, predicts that land expropriation without compensation could have "drastic implications" for the South African economy.

7. The South African economy is currently under significant strain. With the possibility of a downgrade of the country's sovereign bonds to junk status, higher interest rates, a fairly sharp decline in taxation revenues and a deep recession, expropriation without compensation will result in a further contraction of the economy, leading to further job losses.

8. Countries that implemented a similar plan for land redistribution, such as Portugal, Spain, Romania, Vietnam, Venezuela, Ethiopia and Zimbabwe had a significant drop in GDP.

9. “The ratio of capital formation/GDP in these countries declined annually by an average 13.9% after the implementation of such policies and noted that the public debate about land expropriation without compensation in SA had already precipitated a decline in real terms of capital formation by more than 7% over the past eleven quarters.”

   As a result, funding requirements for health, security, infrastructure, education and the like will be reduced, causing further social instability.

10. IMPACT OF AMENDING PROPERTY RIGHTS

The ASISA submission on Amending the Constitution dated May 2018 captures the economic impact very well as follows:

“A market economy cannot operate without legally enforced property rights. Any action that erodes such rights will seriously concern investors locally and internationally and will have an economic cost. In the current debate on land redistribution it is important that these costs be understood. While the debate is focused on land, section 25(4) of the Constitution expressly states that property is not limited to land. The Constitutional Court has held that constitutional property is a broad construct encompassing real and personal rights, immovable, movable, corporeal and incorporeal property. Any amendment to section 25 would therefore be far reaching, even if the amendment were to be limited to land, the consequences of ill-conceived constitutional amendments could have far ranging unintended adverse effects on the economy as a whole.

Amending the Constitution has two separate effects on investor and business confidence.

1. *The first is the practical impact caused by the amendment (such as the amendment of property rights referred to in the recent motion). It has an effect immediately upon amendment as well as any future unintended impact not presently conceived when making the amendment. Amending property rights will impact on property offered as security for credit extended which will have the impact of pushing up the cost of capital.*

2. *The second, and more pernicious effect is psychological. This effect impacts the citizens and foreigners who may have built trust and confidence in the stability and dependability of our Constitutions. It also affects the perspective of politicians who may now be more disposed to make future amendments to*

suit their own political objectives. Amending the Constitution will cause a loss of confidence that will have the impact of pushing up the cost of capital.

Both of these effects will impact the value of property negatively. Where property is held as security for credit the value of the property will drop. Portfolios holding the property as investments will see their value decline (Pension funds, corporate balance sheets, REITS and other investment vehicles as well as private investors). This may have a secondary effect in terms of those granting the credit not having sufficient security for the funds loaned. This will in turn impact their balance sheets negatively thereby reducing their value. This is likely to impact negatively on the systemic risk of the financial services sector in SA dependent on the extent of the amendment to the Constitution. This increases the cost of the capital borrowed will also have a negative impact on the economy. Ultimately this will have the impact of pushing up prices of goods and reducing much-needed investment in the economy.

IMPACT ON THE LOCAL INVESTORS AND CREDIT PROVIDERS

Increased costs and lower savings Listed (and unlisted) South African companies hold large amounts of land and property as assets on their balance sheets. Land is a means of production for numerous companies including those outside the agriculture sector. Examples include companies in the listed property sector, agricultural processing businesses, specialist manufacturers including specialist chemicals manufacturers, mining companies and leisure companies.

Likely declines in property prices (collateral) will increase the cost of borrowing and constrain bank lending, while increasing systemic risk in the entire financial sector, including the risk of deposit withdrawals and pressure on commercial banks' balance sheets. If so, this would increase the risk of asset sales by banks, including bank holdings of government stock, which amounted to R311 billion at end December 2017.

Impact on investment portfolios - South Africa has a savings pool of about R8 trillion, most of which underpins pension obligations. Government pension funds account for about quarter of this asset. Any sustained attack on property rights will erode the value of this asset. Without a continuing inward flow of foreign investment not only will there be less economic growth but also the exchange rate will depreciate. This is an inflationary combination that is bad for savers. Real investment returns will be eroded.

Increased inflation has a pernicious impact throughout the economy. It requires correspondingly higher interest rates that divert government spending away from socially desirable activities to funding the cost of debt. For investors there is inverse relationship between interest rates and asset prices. Asset prices decline as rates increase.

Commercial property *- The commercial property sector is a significant contributor to GDP. We believe that an amendment to this section of the constitution and other property rights' related clauses, poses a risk of destroying value to the R1.2trn commercial property market (property market value estimates from Property sector council charter, 2014/15), of which mortgage debt advanced to the sector is estimated at ca. R380bn (BA900 data).*

Exposure to the sector is through financial institutions who act as custodians of retail and pension fund assets. It is our view that equity and debt investors' real ownership and limited real rights (respectively) will be significantly affected by this amendment. The implications could be negative for the already challenged South African savings culture and for pension funds. This impact should also be viewed within a framework of the country's external accounts (notably the savings gap, including the government's savings gap), the currency, domestic interest rates and inflation.

President Ramaphosa aims to increase South Africa 's fixed investment ratio to 30% of GDP. Even though, arguably, the accompanying increase in income growth may boost savings, it is not reasonable to expect South Africa's savings ratio, which was just 15.8% of GDP in 2017, to increase sufficiently to close the gap. Foreign savings (investment) will be needed to do that.

Mortgage based lending *- A successful market economy is based upon the efficient deployment of scarce capital. South Africa has a well-developed banking system that on 31 December 2017 had made domestic loans amounting to R3 184 billion rand. Of this R1 348 billion or 42 per cent was mortgage lending that is loans secured by land and buildings. The credit markets have always regarded property as superior collateral for loans. Would be homeowners and farmers can borrow say 80 per cent or on occasion even 100 per cent of the cost of a property. Home ownership and farming are totally dependent on a well-functioning mortgage market. This in turn requires a legal certainty that the collateral can be accessed and sold by the lender should the borrower default. Any constitutional amendment which gives the government the right to seize a property without fair and reasonable compensation immediately will put the entire system of mortgage lending at risk. Lenders will not*

accept statements from government that it will not use these powers against them. They would quite reasonably argue that such changes to the constitution would not have been made if there were not the intention to use them. While lending may well continue lenders would require higher interest rates to compensate for higher risks.

Also, the criteria for granting loans would become more onerous with the consequence that less affluent borrowers may no longer be able to fund property purchases. As stated above the amounts involved are large. A one per cent increase in mortgage costs would amount to R13.5 billion per year. Borrowers who have to bear the increased cost will then have less money to spend on other goods and services.

Overall, therefore, the value of assets held by local insurers, pension funds and collective investment schemes (property portfolios, government bonds, private sector equity and corporate bonds) on behalf of pensioners and savers will fall.

IMPACT ON THE FOREIGN INVESTORS *- Reduced foreign investment*

South Africa has a low savings rate and its economy is dependent on continuing foreign investment inflows. President Ramaphosa has correctly identified boosting foreign investment as a key component of any strategy aimed at accelerating growth. Any action that threatens property rights will undermine this strategy. Foreign investors can choose where they wish to place their money among many competing jurisdictions. The memory of Zimbabwe' s disastrous land expropriation is too recent not to heavily and adversely influence the attitudes of these investors. At all costs we must avoid the narrative that South Africa is set on the same path as Zimbabwe.

Business confidence within South Africa is also very fragile. There has been a surge in confidence since the leadership changes within the ANC, but it is noteworthy that since the land issue has become a focus of political debate this enthusiasm has waned. The world has evolved into a global market. South African companies have choices as to where they should invest. If property rights are under attack at home, they will inevitably look elsewhere. Even draconian legislation cannot force business to invest locally. People with skills can always move if they feel unwelcome.

A successful economy requires business confidence. Anything that erodes this confidence will reduce domestic investment and have a price in form of slower economic growth." (ASISA May 2018).

11. IMPACT ON LOCAL AUTHORITIES

The impact of EWC on South Africa's local authorities cannot be underestimated. The likelihood of a higher proportion of urban land being expropriated is possible due to its proximity to working and living opportunities. Local government has a profound impact on the lives of ordinary South Africans in expanding the provision of services to its citizens.

Local authorities are however collectively owed almost R170 billion for rates and services, and their inability to collect it from residents who are unable or unwilling to pay, is a cause for concern. The threat of EWC will further deter investors from investing in these jurisdictions, thereby compounding the dire financial situation many of our local authorities find themselves in.

Less investors mean less property developments. For existing investors, a bulk of who are SAPOA and SAREIT members, the pain is even greater as lower growth translates to a smaller pool of rates to be collected, thereby restricting the ability of local authorities to provide the much-needed services and infrastructure to its citizens.

More than 90% of the investments in the Special Economic Zones came from foreign countries. These are largely situated in the jurisdiction of local authorities. One could argue that the investments in Coega, in East London, Saldanha, took place on state-owned land. However, these investors want security of tenure, and would be hesitant to invest if the threat of expropriation without compensation is at their doorstep.

12. We understand from the preamble to the Amendment Bill that Section 25 of the Constitution is to be amended to make explicit that which is implicit therein so that an amount of nil compensation is explicitly stated as a legitimate option for land reform.

13. A legal opinion on the amendment Bill prepared by Adv. G.L Grobler S.C, an expert on the law of expropriation, is attached as Annexure B.

14. The legal opinion re-iterates that international law does not countenance expropriation without compensation. In international law, this concept is not regarded as expropriation but rather the confiscation of property.

15. As was pointed out in our letter of 14 June 2018, Annexure A, there is a small window afforded by Article 16, paragraph 1 of the Charter of Economic Rights & Duties of States, whereby all States have the right and duty to eliminate colonialism, apartheid, racial discrimination and economic and social consequences thereof as a pre-requisite for development.

16. As set out in Annexures A and B, Section 25(3) of the Constitution may be unpacked to provide for specific relevant circumstance when minimal or no compensation will be payable, but then the circumstances have to be closely and very clearly circumscribed and be subject to the provision that the equivalence principle remains applicable.

17. The equivalence principle is to the effect that where one or more individuals has to bear a sacrifice in the form of a loss property for the common good, the individual and excessive burdens should be compensated by the community. The equivalence principle does not allow nominal compensation nor, as a rule, does it justify less than market value.

18. Section 25(3) of the Constitution which states that the amount of compensation must be just and equitable encompasses or includes the equivalence principle which may not be transgressed in instances where no compensation is paid.

19. As set out in Annexure B, it is very difficult, if not impossible, to correctly circumscribe the circumstances where it would be just and equitable to pay nil compensation, because the practical circumstances of each owner whose property is expropriated cannot be foreseen by a legislature. If instances are crystalised or contained in national legislation, this, in all probability, would amount to confiscation.

20. If these instances are identified, then they should always be subject to the qualification of justice and equity and to put the burden of proof of justice and equity in each instance on the expropriating authority.

21. SAPOA and SAREIT queries why the Constitution should be amended, whilst the amendments will have no practical effect, being already in existence. The perception, which is bound to arise with investors, particularly international investors, is that what South Africa is after, is to legitimise confiscation on the basis

of it being just and equitable to do so. That will put at risk the R8 trillion investment in the non-agricultural property sector.

22. In Section 3 of Annexure B, we set out the changes to the Bill which we believe are necessary. These include:

    22.1 The anomaly between expropriation for land reform and expropriation in the public interest as set out in the Expropriation Bill;

    22.2 The amendments to the Expropriation Bill required so as to ensure that it is not unconstitutional.

    22.3 the need to provide that the power of the courts should not be circumscribed by the national legislation. Accordingly, the proviso to sub-section 2 (b) needs to be amended; and

    22.4 the addition of a proviso to sub-section (3A) to the effect that where the State expropriates at nil compensation, the State should obtain an order of court that it is just and equitable to pay nil compensation in the specific case.

23. In the addendum to Annexure B, Adv. G.L Grobler S.C has dealt with the statement of the ANC NEC following an NEC Lekgotla of 19/20 January 2020. The statement was to the effect that "The Lekgotla endorsed the recommendations that the power to determine issues relating to expropriation of land without compensation should reside in the executive".

24. If this is the intention, then the amendment would be contrary to the rule of law and affect the foundational values of the Constitution. It would also require a 75% majority of the National Assembly and a supporting vote of at least 6 provinces in the National Council of Provinces.

25. Any attempt to undermine the rule of law is strongly opposed and would have dire consequences to South Africa's economy.

26. We would welcome the opportunity of engaging with you further so as to clarify or elaborate on the points which we have raised both in this letter and Annexures A and B hereto.

Yours faithfully

NEIL GOPAL
Chief Executive Officer
SAPOA

ESTIENNE DE KLERK
Chairperson
SA REIT Association