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SACTA – THE END POINT ROYALTY

Introduction

Industry role players have for some time acknowledged that there is a need for a sustainable Industry Research Funding Strategy for self-pollinated crops. End Point Royalty (EPR) systems have been implemented in numerous agricultural economies as a solution towards funding research and obtaining ag related intellectual property. Examples include Australia, France, Germany, Uruguay and the USA.

In South Africa, the Minister of Agriculture has established End Point Royalties for Wheat, Barley, Oats and Soy Bean in the form of statutory levies applied in terms of sections 13 and 15 of the Marketing of Agricultural Products Act, 1996 (Act No 47 of 1996) and the published in the Government Gazette.

These End Point Royalties are statutory measures which impose legal obligations to comply. They are administered by the SA Cultivar and Technology Agency NPC (SACTA) and are the product of an industry wide initiative including the South African National Seed Organisation (SANSOR representing plant breeders); Grain SA (representing wheat and barley growers), the Department of Agriculture Forestry and Fisheries (DAFF), Agricultural Research Council (ARC), AGBIZ Grain and various other industry role players.

This document provides insight into the need for such a statutory measure, its aim and purpose, as well as information pertaining to the levy's scope of application and affected parties. It also attempts to present and explains some questions and uncertainties.

Purpose and Aim of the SACTA levy

The Government Gazette presents that the "purpose and aim of the statutory measures are to compensate breeders of wheat, barley, oats and soya varieties for their contribution towards obtaining and utilising improved international agriculture related intellectual property to the benefit of their respective industries in the Republic of South Africa". It further states that "The agricultural sector is expected to ensure food security, strengthen the economy and create job opportunities. This can be reconciled with the provisions of Section 2(3) of the Act. In order to achieve these aims and to further the competitive position of these industries in the Republic of South Africa, cultivation of high yielding crops from seed varieties that are most suited for particular regions, is essential".

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Contribution of breeding programs to commercial farming is significant.

A recent US study indicated that for the period 1996 - 2016, the value flowing to the South African wheat Industry from just the Sensako wheat breeding programs was US$ 2 billion. A 2018 BFAP report prepared for SACTA further indicated that the implementation of the EPR could translate to yields that would represent revenue increases of R 1 Billion in soya and R 1.5 billion per annum in wheat & Barley respectively by 2027.

To better understand the value of breeding programs, consider the impact of cultivar improvement on commercial yields. A 1% average annual yield improvement over a ten-year period would imply that yields will have increased by 10%. Said differently, on a constant area of production, farmers can produce 10% more than 10 years before. For wheat in South Africa, this would equate to approximately 160 000 tons of added annual production with an approximate value of (wheat price of R 4 500 per ton x 160 000 tons) R 720 million per year.

Impact of Farmer Exception/Privilege on breeding programs

The Farmer Exception clause in South African Seed Law allows farmers to retain grain for planting as "Farm Saved" seed in subsequent seasons. For self-pollinated crops, this creates a situation where farmers can make a once off purchase of a small amount of seed and then lawfully use it to produce seed for planting in the next, and subsequent planting seasons. The result is that profits from commercial seed sales that fund breeding programs are diminished because;

- Sales volumes tend to be low (it is cheaper to retain grain for seed) and
- Profit margins tend to be low (higher commercial seed prices trigger increases in the use of farm saved seed).

The consequence is that seed revenues in self-pollinated crops are generally insufficient to warrant sustainable research and access to international IP.

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Why is the SACTA levy necessary?

Without support from industry and an appropriate funding mechanism:

- South African self-pollinated crop breeding programs, such as wheat, barley, oats and soya are not financially viable; and
- South Africa is being excluded from beneficial technologies as it is an unattractive destination for Ag related Intellectual Property associated with self-pollinated crops. This is important since most Ag related Intellectual Property is either owned by, or under foreign control.

Therefore, without an appropriate funding mechanism,

- The sustainability of domestic breeding programs is questionable, and
- South African producers will continue to be excluded from having access to and utilising internationally held nurseries, markers, techniques and technologies which are available to, and being utilised by their international counterparts.

What is the SACTA levy?

The SACTA levy for wheat, barley and oats is to a large extent a replacement of the breeding component of the Winter Cereal Trust (WCT) levy, but with a fairer means of remunerating breeders based on the contributions that their cultivars make to the market (market share). For soya, the SACTA levy is new. The levies are imposed on the all wheat, barley, oat and soya that is;

a) Sold by or on behalf of the producer thereof. In this case - the levy is payable by the buyer and may be recovered from the grain producer.
b) Processed or converted or caused to be processed or converted into a wheaten or barley product, by or on behalf of the producer thereof, if the wheaten or barley product is intended to be disposed of. In this case - the levy is payable by the processor/convertor of the grain and may be recovered from the grain producer.
c) Where a silo receipt has been issued, if the levy in respect of such winter cereal has not already been paid in terms of paragraph (a) or (b), the levy is payable by the person issuing the silo receipt and may be recovered from the person to whom such silo receipt is issued.

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Is the SACTA levy aligned with international End Point Royalty (EPR) systems?

Yes. The SACTA levy is based on the Australian EPR. Information presented in the SACTA levy application included that "*the proposed implementation of a breeding and technology levy, based on the* ***Australian end-point*** *royalty system".* The Australian EPR is aligned with the SACTA levy in that Intellectual Property (IP) owners either market commercial seed directly to farmers, or license to seed distributors who also supply commercial seed to farmers. In Australia, where IP owners license to Seed distributors, the seed distributors pay royalties/licence fees to the IP owners on commercial seed that they have sold. The Australian endpoint Royalty is also levied on harvested material produced and sold by farmers.

The SACTA levy and market share

Revenue flowing to IP owners from the SACTA levy is based on market share. Should an IP owner be able to grow its market share, either by reducing prices or supplying the market with a superior product, it will receive a greater proportion of the levy revenues. Were this to be the case, then other IP owners may be forced to follow suit by either reducing seed prices and or royalties or investing in research to improve their portfolio of products. Market forces would therefore be functioning normally.

Is seed subject to the SACTA levy?

No. Both commercial seed, and farmer retained seed, are not subject to the SACTA levy as they are not sold by the producer, processed on behalf of the producer for sale, and are not in respect of a silo certificate issued where the Levy has not already been paid.

Commercial License Agreements (between Seed Distributors and IP owners). Are they necessary?

Without license agreements, many technologies and germplasm would not be available to farmers. Examples may include foreign entities, and research focused companies that do not have their own seed distribution networks in South Africa. In these situations, IP owners conclude license

agreements with Seed Companies and Seed Distributors that give them the right to trade, utilise, multiply, market, use trademarks and to sell seed.

Commercial seed prices

Seed companies that supply seed directly to the market will recoup research costs as a component in their seed price.

Similarly, license fees (or royalties) payable by Seed Distributors to IP owners are for the benefit of the Seed distributor for the services/technology and rights provided to them. As such, these fees would also represent a component of their commercial seed price.

Should royalties be waived?

It has been argued in some circles that all royalties should have been waived with the implementation of the SACTA levy. This view is, however, flawed and impractical since:

- There are no royalties applicable where a PBR owner sells seed directly into the market. In such cases research costs are recouped as a component of the seed price. As such waiving royalties would not affect these commercial seed prices.
- Domestic research companies that license to seed distributors and charge royalties would be placed at an unfair disadvantage compared to seed companies that sell direct to producers.
- IP owners would be incentivised to change their route to market and sell direct to farmers so that royalties/license fees are not applicable. This might not be in the best interest of seed merchants and producers.
- Seed merchants are at liberty to determine and set their own seed prices. As such – there is no guarantee that the removal of royalties would be passed on to growers.
- The intention of the SACTA levy is to attract and compensate owners of Ag-related intellectual property for revenues that are lost when farmers use farm saved seed. Its aim not to eliminate royalties and technology fees, but to create an additional and sustainable income flow. Any measure to limit royalties would probably have the unintended consequence that IP owners would withdraw current or withhold future genetics and technology. The effect would be the opposite of the aims of the SACTA levy

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- Eliminating royalties on commercial seed sales could render the rights afforded Intellectual Property owners unenforceable since, in the event of a breach of IP rights, a civil claim for damages would have to be instituted. Where there is no loss of income (resultant from zero royalties), it is difficult to prove damage. Being unable to show damage would essentially render the IP rights unenforceable. As such, Ag-related IP would be open to abuse by unscrupulous parties with the added unintended consequence of providing a disincentive to invest in South Africa.
- It is questionable whether the statutory imposition of prescriptive licensing terms could be enforced against foreign PBR holders, particularly those prescribing that foreign law shall apply to the licence agreements.
- Most Ag- related IP is owned by, or under foreign control. It is common international practice for Seed companies and Seed merchants to enter royalty bearing licence agreements with PBR and technology owners. The whole international seed business is based on this premise of seed licensing and compensation (royalties/license fees) for use of intellectual property. If IP owners could not receive royalties/license fees, it is unlikely that international owners of Ag-related IP will make their genetics and technology available to the South African market
- The only way a Statutory Measure could eliminate the effect of royalties/license fees on commercial seed sales would be to regulate commercial seed prices. This would represent a breakdown of the free market system.
- License agreements are private agreement between PBR owners and Seed Distributors. The Agricultural Marketing Standards Act does not provide the Minister with powers to affect or interfere with licence agreements.

Can a distinction be made between South African and international owners of intellectual property (IP) in respect to the payment of royalties?

No. The South African constitution does not allow for discriminatory practices.

What is double dipping?

The term “double dipping” means “**Receiving two incomes from the same source "**.

The SACTA levy is levied on grain or "harvested material" produced and sold by farmers. The **Source** of levy is therefore the grain produced and sold by farmers. If grain has not been produced and sold by a farmer – it is not subject to the levy. This would include grain retained by producers for seed in terms of the Famers Exemption (Section 23(6)f of the Plant Breeders Rights Act).

Since the grain/harvested material produced by farmers is subject to the SACTA levy, any additional royalty payable on the use of this farmer produced grain/harvested material (for farm saved seed) would be from the same source as the SACTA levy and therefore constitute "double dipping". For this reason, and to prevent "double dipping", Sensako agreed that upon imposition of the SACTA levy, Sensako would not sell or license seed to farmers under a contract that a) prevents the use of, or b) requires payment of a fee, when farmers use their grain/harvested material as farm saved seed. Sensako adhered to this in that since the imposition of the SACTA levy, all royalties applicable to farmer produced grain/harvested material, for farm saved seed, were waived. This does not, however extend to third parties that conduct a business of cleaning or treating of seed (processing for purposes of propagation).

Farmers Exemption and the Processing of seed

Section 23(1)b requires that any person wishing to “Processing for purposes of propagation” must obtain a license from the holder of the Plant Breeders Right (PBR).

The “Farmers Exemption” clause 23(6)f of the PBR Act is limited to a farmer who on land occupied by him or her, uses harvested material obtained on such land from that propagating material for purposes of propagation and, provided that harvested material obtained from the replanted propagating material shall not be used for purposes of propagation by any other person other than that farmer.

This means that:

- Any person that makes a business or provides a service of cleaning or treating seed is required to obtain a license from the PBR holders.
- Farmers may clean their own seed that they produced on their own farms. As soon as they provide a service for another farmer without a license – they will be contravening the PBR Act.