

DIRECTORATE-GENERAL FOR INTERNAL POLICIES

POLICY DEPARTMENT B
STRUCTURAL AND COHESION POLICIES



Agriculture and Rural Development

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**THE CAP TOWARDS 2020:
WORKING PAPER ON THE EC
COMMUNICATION OF 18
NOVEMBER 2010**

NOTE



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**The CAP towards 2020:
Working Paper on the EC Communication
of 18 November 2010**

NOTE

This document was requested by the European Parliament's Committee on Agriculture and Rural Development.

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POLICY DEPARTMENT B: STRUCTURAL AND COHESION POLICIES

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The CAP towards 2020: Working Paper on the EC Communication of 18 November 2010

NOTE

Abstract:

This paper is written by Policy Department B for the Working Group on Common Agricultural Policy Reform, as agreed by the COMAGRI Coordinators on 27 October 2010. The purpose of this document is to facilitate the legislative work of the MEPs relating to the next reform of the CAP. It analyses the Commission's Communication of 18 November 2010 on the basis of the European Parliament (EP) Resolution of 8 July 2010 and offers some suggested questions in order to help the EP with its response to the Commission's proposals.

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FOREWORD

The "*Health Check*" adopted by the Council on 20 November 2008 and implemented from January 2009 was the latest stage in the Common Agricultural Policy (CAP) reform process. In essence, it was an exercise in evaluating and adjusting the mechanisms adopted in 2003 in a rapidly changing international context (particularly as a result of the financial and economic crisis and the increased volatility of agricultural prices and costs). Once the work on the "*Health Check*" implementation had been completed, there was a new challenge ahead: establishing a new CAP for the post-2013 period, after the end of the current financial perspectives.

Agricultural interests are particularly at risk, given that in 2013 several **new institutional factors** will come into play: the implementation of the "*Europe 2020*" strategy for intelligent, sustainable and inclusive growth; the end of the transitional period of the CAP for the newest Member States; possible future accessions; a possible new agricultural agreement resulting from the WTO Doha Round; a new protocol on climate change to replace the Kyoto Protocol; and, especially, the end of the 2002 agreement to fix the CAP Pillar 1 budget and the decision on the new multiannual framework for the post-2013 period.

The Conclusions of the European Council of 17 June 2010, adopting the "**EU 2020 Strategy**" ⁽¹⁾ suggests that all EU policies, including the CAP, will need to support this strategy ⁽²⁾. In particular, the European Council recognises that "*a sustainable productive and competitive agricultural sector will make an important contribution to the new strategy, considering the growth and employment potential of rural areas while ensuring fair competition*".

The result of the debate in the Informal meeting of Agriculture Ministers concluded that agriculture could play a central role in achieving the goals of the Europe 2020 strategy through its current multifunctional role and by producing greater economic, environmental and social competitiveness.

In this context, the **economic crisis** and the measures adopted for economic recovery bring public spending to the centre of political debate, creating pressure on the traditional lines of the European budget. However, the effects of the global financial and economic crisis also reverberate within the agriculture sector, with farmers facing a decrease in their incomes, as shown by the most recent Eurostat figures. This situation is exacerbated by increased exposure to the phenomenon of price volatility, with recent experience suggesting this may become an ongoing and systematic factor.

Against this background, a reflection process was launched by the **Agriculture Council** on the new CAP. Even before adoption of the Health Check, the French Presidency devoted the Informal meeting of Ministers of Agriculture in Annecy (November 2008) to a debate on the future of the CAP after 2013 ⁽³⁾. Subsequently, under the Czech, Swedish, Spanish and Belgian Presidencies, Council meetings have been devoted to specific aspects of the future

¹ "*Europe 2020: A strategy for smart, sustainable and inclusive growth*" (COM(2010) 2020, 3.3.2010).

² Conclusions of European Council, 17 June 2010 (in particular, point 5).
(http://www.consilium.europa.eu/ueDocs/cms_Data/docs/pressData/en/ec/115346.pdf).

³ Informal meeting of Agriculture Ministers (Annecy, France): *Future of the CAP after 2013*, Council Conclusions, 27 November 2008 (doc. 16287/2/08 REV. 2).

of the CAP: direct aid schemes ⁽⁴⁾, rural development ⁽⁵⁾, market and crisis management instruments ⁽⁶⁾, and the budgetary balance between the two pillars ⁽⁷⁾.

A public debate on the future of the CAP was also launched by the **European Commission** in April 2010. With the aim of bringing together the various contributions submitted during the debate and continuing the thinking on the objectives and principles of the new policy, a conference on the CAP post-2013 took place on 19-20 July 2010 in Brussels. On the basis of the conference, the Commission has presented the Communication "*The CAP towards 2020: meeting the food, natural resource and territorial challenges of the future*" (COM (2010) 672, 18 November 2010).

The debates on the future of the CAP post-2013 began in the **European Parliament** even before the Commission had presented its Communication. On the basis of an own-initiative report, the European Parliament adopted a Resolution in July 2010 ⁽⁸⁾.

The original purpose of the Commission's Communication is to suggest some changes, explore avenues on the CAP after 2013 highlighted in the public debate and conduct a proper consultation before the preparation of legal proposals (to be presented in summer 2011). The extended nature of this initiative reflects the level of importance of the debate and the significance of the reform process that will address a complex legal and administrative structure facing, for the first time, the new legislative procedure enforced by the Lisbon Treaty.

The scope of the Commission Communication is, however, very general and the budgetary concerns on the new CAP remain almost entirely absent. In the figurative sense, we have now some pieces of the puzzle, but we do not know the final design or its size. In fact, most of its elements, announced by the Communication were already developed by the EP Resolution of 8 July 2010 on the future of the Common Agricultural Policy after 2013. Indeed, sometimes the EP Resolution is more ambitious and concrete than the Commission has been in its Communication.

In this Resolution ⁽⁹⁾, the EP called for "*appropriate measures to be taken to explain what the CAP consists of, not only to farmers but to all Europe's citizens, while providing transparently clear information about the objectives being pursued, the means available and the anticipated beneficial effects of implementing the CAP*". Unfortunately, the Communication does not satisfy these requirements. It lacks detail and it is devoid of analysis.

Furthermore, the preparations of the future CAP should be seen in the broader context of the Budget Review. On 19 October 2010, the Commission presented a Communication on this subject (COM (2010) 700). As with the Commission's CAP options paper, the text of this Budget Review Communication was also very vague, leaving the impact on the new CAP uncertain.

⁴ Informal meeting of Agriculture Ministers (Brno, Czech Republic), May - June 2009 (doc. 10713/09).

⁵ Agriculture Council of December 2009, Brussels: *Rural Development in the post-2013 CAP* (doc. 17488/09).

⁶ Agriculture Council of 15 February 2010, Brussels: *Market management measures post 2013*, Presidency Paper and Questionnaire (doc. 6063/10); Council Conclusions (doc. 7451/1/10 REV 1). Informal meeting of Agriculture Ministers (Mérida, Spain): *Agriculture and reform of the CAP in the perspective of the EU 2020 Strategy*, Presidency Paper, 1st June 2010 (doc. 8728/10).

⁷ Informal meeting of the Ministers of Agriculture, La Hulpe, Belgium, 19-21 September 2010: *Choosing today for a stronger CAP tomorrow* (doc. 13452/10).

⁸ European Parliament resolution of 8 July 2010 on the future of the Common Agricultural Policy after 2013 (2009/2236(INI) - T7-0286/2010, 8.7.2010). See bibliographical references - point 2.

⁹ See Paragraph 57.

In this briefing, written by the Policy Department B, the Members of the EP will find an overview and **analysis of the content** of the Commission's Communications on the future of the CAP and the budget review. It also discusses the **key issues of interest** that will be tackled during the CAP reform process on the basis of the EP resolution of 8 July 2010. Finally, it provides a **questionnaire** on the new CAP Communication and some **suggestions** in order to facilitate the legislative work on the reform dossier.

Brussels, 23 November 2010

I. GENERAL TOPICS

1. LEGITIMISING THE CAP: NEW CHALLENGES AND NEW OBJECTIVES

1.1. Proposals (Sections 3 and 5)

The Communication of 18 November sets out **three key challenges** for agriculture (Section 3):

- To preserve Europe's capacity to deliver **food security**. In a world characterised by increasing globalisation with rising price volatility, the CAP has to improve the competitiveness of the agricultural sector, enhance its value share in the food chain, ensure a diverse and high quality supply of food and address low incomes in the light of the economic crisis.
- To help farming adapt and make a positive contribution to address **climate change** (through carbon sequestration, biomass production and reducing GHG emissions) and **environmental challenges** (such as depletion of soil, water and air quality, and biodiversity).
- To mitigate the **territorial imbalances**, improving the vitality and economic potential of rural areas, in particular in "*predominantly rural regions*" ⁽¹⁰⁾.

From these three challenges are derived **three objectives**, each unpacked into other sub-objectives (Section 5):

- **Viable food production**. This objective is broken down into three policy sub-objectives: to contribute to farm incomes and limit volatility; to improve competitiveness of the agricultural sector and its bargaining power in the food value chain; and to maintain the spatial distribution of agricultural production, including in areas with natural constraints where there is a risk of land abandonment.
- **Sustainable management of natural resources and climate action**. This objective is made up of three elements: securing the provision of environmental public goods by agriculture and forestry; fostering green growth through innovation; and pursuing climate change mitigation and adaptation actions.
- **Balanced territorial development**. This objective is in turn distributed across three rural development sub-objectives: support for rural employment; promotion of rural economic diversification; and encouragement of structural diversity in farming systems through improving conditions for small farms and local markets.

1.2. EP Resolution 8 July 2010

The EP Resolution devotes a chapter to the **challenges** to which the CAP post-2013 must respond (Paragraphs 10 to 20). The Resolution draws a distinction between "*first generation*" public goods (food security and food safety) and "*second generation*" public goods (such as environment, land management and animal welfare) (Paragraph 6), and

¹⁰ The OECD identifies the "*predominantly rural regions*" (PRR) if more than 50% of the population of the region (NUTS 3) is living in rural communes (with less than 150 inhabitants / km²). In the EU-27, PRR represent 54.4% of the territory and 19.2% of the population in 2006. The primary sector represents around 16% of the employment and 5% of the value added in PPR of EU-27.

highlights the importance of climate change (Paragraphs 13 and 14) and the economic crisis (Paragraph 17).

The EP Resolution also defines the new CAP **priorities** for the 21st century inside the new EU 2020 Strategy (Paragraph 37). It believes that agriculture is well placed to make a major contribution to tackling climate change, creating new jobs through green growth and supplying renewable energy, whilst at the same time continuing to provide food security for European consumers by producing safe and quality food products ⁽¹¹⁾.

Additionally, the EP Resolution remarks that the CAP priorities should be embedded in a multifunctional food and agricultural policy (Paragraphs AE and 20).

1.3. Observations

The Communication retains **three dimensions** of the CAP: economic, environmental and socio-territorial. This multidimensional approach implies the recognition of the **European Agricultural Model** and the **multi-functional role of farmers** ⁽¹²⁾.

Looking further into the details of the proposals, the **food security** objective is cast in terms of the need to preserve the food production potential throughout the EU ⁽¹³⁾. Indirectly, food security becomes the most tangible reason for maintaining farm income support, taking into account the severe impact of the economic crisis on agriculture ⁽¹⁴⁾. While the emphasis on competitiveness and innovation is laudable, it remains unclear how these references will be translated into the specific and transformational reforms required to release the EU's latent productivity potential, in a sustainable manner.

The **environmental policy challenge** is in principle focused on the provision of environmental public goods not remunerated by the market (also described as "*collective services to society*" in the Commission's paper). The Communication seems to focus almost exclusively on this category of public goods, while public goods from agriculture are generally classified into two main categories: environmental goods and non-environmental goods (or social goods) ⁽¹⁵⁾. In the first category are placed those public goods closely related to environmental externalities such as farmland biodiversity, water availability and quality, resilience to flooding and fire, climate stability (mainly carbon storage and reducing greenhouse gas emission) and agricultural landscapes. The second category contains those public goods related more to social externalities, including rural vitality, farm animal welfare and health, and food security. The latter two, in particular, seem to receive little attention in the Commission's paper, with the Communication failing to show a direct link between them and the tools of the future.

¹¹ See also the Paragraphs AE, 21, 50 and 60 concerning the EU 2020 Strategy.

¹² See paragraphs AE, 7 and 20 of the EP Resolution of 8 July 2010.

¹³ The EP Resolution also recalls that potential events can be detrimental to production capacity (Paragraph 21). It is also interesting that the Commission chooses to cite the Scenar 2020 study in this context, since its updated analysis (see list of references) shows a negligible impact on food production under the scenario reflecting a 30% cut in direct payments. Indeed, the Communication's reference to "*withdrawing support*" is probably deliberately ambiguous, as it could be argued that the problems cited—deterioration of habitats and EU's productive capacity—could be most appropriately addressed with properly targeted Pillar 2 payments, rather than universal income support.

¹⁴ Agricultural income fell by 11.6% in the EU in 2009, mainly caused by a drop in output prices (Eurostat - Statistics in focus, 18/2010). This overall decrease is adding to an already fragile situation of an agricultural income significantly lower (by an estimated 40% per working unit) than that in the rest of the economy, despite the agricultural labour in the EU decreasing by 24.9% since 2000 (which, in terms of AWU (annual work unit) represented a drop of 3.7 million from 14.9 million AWU in 2000 to 11.2 million AWU in EU-27 in 2009).

¹⁵ IEEP - Cooper *et al.* (2009): "*Provision of public goods through agriculture in the European Union*" (see references).

Concerning the **balanced territorial development** objective, the Communication does not mention that relevant measures related to quality of life in rural areas or to territorial cohesion lie outside the scope of the CAP. Furthermore, the Commission chooses not to raise the coordination framework between the European Agricultural Fund for Rural Development (EAFRD) and the rest of the Structural Funds (Section 6.1).

The main question is how the new CAP will achieve the objectives proposed. The links between the new objectives, both the pillars and the new mechanisms remain unclear. It is also difficult to define what objectives will be prioritised in financial terms. In this context, the process of better targeting appears only partial, especially inside the first pillar (dividing the current Single Payment Scheme into a basic income payment, a "*greening component*" based on supplementary costs, additional income support in areas with specific natural constraints, and coupled support to particular types of farming) (see §12). Finally, the type of instruments relating to each objective (through support, compensation, regulation or the use of incentives) remain unspecified.

In any case, one must recall that the new CAP objectives proposed by the Communication will just concern the derived legal acts, since the agricultural chapter of the Treaty remains unchanged (Article 39 of the Treaty on the Functioning of the EU - TFEU) ⁽¹⁶⁾. In fact, it could be argued that the Treaty chapter on agriculture ⁽¹⁷⁾ has become less relevant in light of developments in the CAP.

1. QUESTIONS ON CAP OBJECTIVES

- *How will the multiple objectives proposed by the Communication be prioritised in financial terms?*
- *How will the new objectives relate to both CAP Pillars and the mechanisms within them? In particular, how does this relate to the process of better targeting?*
- *Is it intended that this round of reform will set a path for the future CAP, moving it away from its traditional agricultural and economic focus and more towards environmental, territorial or even social objectives?*
- *What would failing to move the CAP beyond its status quo position represent in terms of the missed opportunity to improve its policy effectiveness and legitimise its budget?*

¹⁶ Confirmed by the Communication (Section 2): "*The main objectives of the CAP set out in the Treaty of Rome have remained the same over the years. However, the reform path of the CAP since the early 1990s has led to a completely new policy structure*".

¹⁷ Title III of Part Three of the TFEU.

2. CAP ARCHITECTURE

2.1. Proposals (Section 6.1)

The Communication retains both pillars: annual direct payments and markets measures in the first pillar; multiannual rural development measures in the second pillar.

2.2. EP Resolution 8 July 2010

The EP Resolution considered that the two-pillar structure should be maintained, but that it should avoid duplication of policy objectives and instruments, as well as reflecting the content of the building blocks proposed by the EP (Paragraph 67). The EP also called for "*simple multiannual contracts*" (Paragraphs 56 and 71) to achieve real environmental gains. ⁽¹⁸⁾

2.3. Observations

The Communication proposes to preserve the current (two-pillar) structure in relation to the type of instruments (annual direct payments and markets measures in the first pillar; multiannual and contractual programmes inside the second pillar). It seems that the previous **'financial' distinction** between the pillars still remains. Currently, the first pillar is funded entirely by the EAGF and the second pillar is financed by a joint funding system through the EAFRD ⁽¹⁹⁾. The speculation around this financial distinction suggests that further clarification is required regarding the evolution of the Commission's thinking over whether or not to include co-financing in the new model of support in the first Pillar. Furthermore, the Communication seems to eliminate the current budgetary transfers and mechanisms such as modulation or Art. 68 of Regulation (EC) N° 73/2009 ⁽²⁰⁾.

In principle, the aim of the Communication is to avoid overlaps between the current pillars and introduce more targeting of the new CAP instruments (Section 6.1). However, the role of each pillar is not clearly defined and the targeting of support remains confused. One could argue that, by taking part of agri-environment into Pillar 1 and by increasing the environmental conditionality of direct payments, the Commission is proposing an overlap between the two pillars. Similarly, the scope of the second pillar is reduced through the transfer of part of the LFA support to the first pillar (as direct payments). It is not clear if the transfer of these competences will be accompanied by the respective budgetary reallocation (see §19 and §20).

Finally, the new CAP instruments will be based on new basic legal acts concerning direct aids ⁽²¹⁾, single CMO measures ⁽²²⁾ and multiannual rural development payments ⁽²³⁾. All

¹⁸ The EP studies "*The Single Payment Scheme after 2013*" (Eurocare) and "*Elements of the post 2013 CAP*" (Buckwell) also advocated contractually based payments for the provision of public goods or services (see references).

¹⁹ EAGF is the European Agricultural Guarantee Fund and EAFRD is the European Agricultural Fund for Rural Development.

²⁰ However, the new voluntary coupled support component in the first pillar could be analogous to the current Art. 68 (see footnote of Annex in Communication). See also below the comments on the direct payments scheme (§11).

²¹ Replacing current Council Regulation (EC) N° 73/2009 establishing common rules for direct support schemes for European farmers (OJ L 30, 31.1.2009 and OJ L 43, 18.2.2010).

²² Replacing current Council Regulation (EC) N° 1234/2007 establishing a common organisation of agricultural markets (OJ L 299, 16.11.2007).

²³ Replacing current Council Regulation (EC) Nos 1698/2005 (OJ L 277, 21.10.2005) and 473/2009 (OJ L 144, 9.6.2009) on support for rural development by the European Agricultural Fund for Rural Development - EAFRD.

these legal acts would be adopted by the codecision procedure ⁽²⁴⁾. In this context, a possible option could be the creation of a third pillar for the single CMO measures, currently sitting alongside direct payments inside the first pillar. One advantage of this development would be that the separation between the three pillars should bring about clarity of objectives, with each pillar being complementary to the other, without overlaps, helping improve the efficiency of the policy ⁽²⁵⁾. Since the costs of market measures under such a new pillar would vary depending on the state of the market, it would be necessary to ensure the overall CAP budget still respected financial disciplines.

2. QUESTIONS ON CAP ARCHITECTURE

- ***Is it correct to assume that 'co-financing' will be confined solely to the second pillar?***
- ***If the basis on which the pillars are to be defined is their objectives, would it not be logical to create a third pillar for markets measures?***

²⁴ Furthermore, the current regulation on the financing of the CAP will be also modified (Council Regulation (EC) N° 1290/2005, OJ L 209, 11.8.2005).

²⁵ As called by the EP Resolution of 8 July 2010 (Paragraph 57).

3. SCENARIOS FOR THE CAP REFORM

3.1. Proposals (Section 6.2)

Three broad policy options are presented as potential paths whose impact will be analysed before final decisions are made:

- **Option 1** - *Continuity* (Current CAP with gradual adjustments): This option would be restricted to resolving some current discrepancies, such as distributing direct payments more equitably between Member States and farmers. Even here, this redistribution would be limited, thereby ensuring continuity and stability within the current CAP.
- **Option 2** - *Evolution* (Balanced CAP reform): Another alternative would be to make major overhauls of the CAP in order to ensure that it becomes more sustainable, and reshapes the balance between different policy objectives, farmers and Member States, in particular by introducing a more targeted approach to priorities. This option would imply greater spending efficiency and greater focus on the EU value added (see §20).
- **Option 3** - *Break up* (Rural and agri-environmental policy): This more far reaching reform would go further, moving away from income support and most of the market measures, and giving priority to environmental and climate change objectives, rather than the economic and social dimensions of the CAP.

3.2. EP Resolution 8 July 2010

The EP Resolution did not include an analysis by scenario.

3.3. Observations

The Communication retains both pillars and proposes a progressive evolution so the policy can face the food, environmental and territorial challenges with a different balance between pillars in relation to the three broad policy options. The Budget Review Communication ⁽²⁶⁾ repeats these same broad policy options (Section 3.2, pages 11-12).

According to the Commission Communication, reform of the CAP could therefore be pursued with different degrees of intensity. It seems that the Commission is steering a course between the status quo and those saying the CAP should only be about the environment and the provision of public goods.

In principle, the Commission introduces itself as being neutral towards the three options proposed. However, given the extent of the development of the respective proposals (see Annex in Communication), it is clear that the Commission sees the **second option** as the best route, establishing a better balance of support between the economic, environmental, territorial and social dimensions ⁽²⁷⁾. However, even this option lacks detail on the instruments to be used and is devoid of policy priorities in financial terms.

²⁶ COM (2010) 700. 19.10.2010. See references - point 6-d.

²⁷ The pragmatic and political approach of Option 2 could be supported by some members of the Council. In this context, the Franco-German letter could be interpreted as being close to Option 2, although the financial basis seems more conservative and closer to the Option 1 (see references - point 7). Paradoxically, only a few studies and papers would support this second option.

It seems apparent that **Option 1** will be favoured by the traditional farm unions. Obviously, the uncertainties of the Commission proposals and the fears of their final impact on farming serve to reinforce the preference of the *status quo* among most of the farming stakeholders. It is questionable, however, whether this option represents sufficient change to enable the CAP to address wider economic and social challenges and avoid being seen as an invitation to downsize its budget in favour of other spending priorities perceived as having higher EU added value.

Option 3 is close to several proposals presented by academics, economic think-tanks and environmental and development NGOs ⁽²⁸⁾, with it implying a fundamental CAP reform abolishing market measures and income support and focusing exclusively on environmental public goods and climate change. In effect, it turns a common agricultural policy into a rural policy. This option is consistent with a targeting approach, allowing specific and clear goals of the policy, and increasing the visibility by the citizens. However, it ignores the current income crisis of many sectors, the price volatility experienced in recent years, and more general, traditional failures of agricultural markets ⁽²⁹⁾. It also does not recognise the tight links between income stability support, sustainable farming activity, provision of public goods and balanced territorial development. In the absence of some basic income support, many EU producers would opt for the intensification of production, while others would simply abandon production. The result would be more concentrated production in the most competitive regions, which would lead to less public goods overall and more challenges to meet climate change targets ⁽³⁰⁾.

The three scenarios analysed are not in fact clearly differentiated. Option 2 would be close to Option 1 if the basic income support in the first pillar is allocated a large share of the national envelopes. Conversely, Option 2 could be converted to Option 3 if the greening component represented a significant share of the first pillar budget.

In any case, the Commission seems to suggest that the Impact Assessment accompanying the legislative proposals of summer 2011 will evaluate all three options ⁽³¹⁾.

3. QUESTIONS ON THE SCENARIOS

- *Is the second option the best route in the opinion of the Commission?*
- *To what extent is it possible to regard the main distinguishing feature of the three options as being the relative weight of each component within the new model of Pillar 1 direct payments? Under this hypothesis, to what extent will the final decision between the options be down to the Member States?*
- *Will the Impact Assessment accompanying the legislative proposals evaluate all three options separately or could hybrids, combining certain aspects of the different options, be included?*

²⁸ See references in bibliography (Point 8) to both Declarations by a Group of Leading Agricultural Economists (2009 and 2010). See also the studies from EuroCare, BirdLife International, IEEP and WWF International

²⁹ See Paragraphs 26 and 44 of EP Resolution of 8 July 2010.

³⁰ See Point 31 of EP Resolution of 8 July 2010.

³¹ The Communication notes that the options presented have "*clear, but different advantages and drawbacks in fulfilling the objectives of the new CAP as presented in this Communication*". They will need **to be evaluated on the basis of their economic, environmental and social impacts**" (Section 6.2). With these parameters of evaluation, Option 2 seems most capable of ensuring the synergies between the economic, environmental and social dimensions of the CAP.

4. TRANSITIONAL PERIOD

4.1. Proposals (Section 6.1)

The Communication does not contain any references to a transitional period in order to implement the new CAP. However, it does mention the Commission's intention to avoid "*major disruptive changes*" inside the **first pillar**. It proposes "*a system that limits the gains and losses of Member States by guaranteeing that farmers in all MS receive on average a minimum share of the EU-wide average level of direct payments*".

In regard to the distribution of rural development support (**second pillar**) among Member States, the Communication propose the use of objective criteria, "*while limiting significant disruption from the current system*".

4.2. EP Resolution 8 July 2010

The EP (Paragraphs 65 and 66) called for a sufficient transition period (in connection to a move to an area basis) allowing farmers and agricultural structures that are still using the historical payments system the flexibility to adapt to the changes, and to avoid too radical a redistribution of support.

4.3. Observations

The Communication lacks any discussion of the transitional period (either phasing in changes or phasing out certain elements). Neither does it analyse the transaction costs of the new CAP implementation, nor the possible accompanying measures (for example, the advisory services necessary to guide farmers in their attempts to implement innovation measures ⁽³²⁾ or to deliver public goods ⁽³³⁾).

In directional terms, it only makes clear that the Single Payment Scheme should be replaced by four new direct payments (see §7, §8, §9, §10 and §11) addressing: basic income support, a greening component of direct payments, additional income support in areas with specific natural constraints, and coupled support to particular types of farming.

4. QUESTIONS ON THE TRANSITIONAL PERIOD

- *What will be the period for 'phasing in' the new mechanisms?*
- *Which mechanisms will be affected by any possible transitional arrangements?*
- *Will Member States be able to decide the pace of any transition concerning the direct aids scheme inside the first pillar?*

³² See Paragraphs 49 and 50 of the EP Resolution of 8 July 2010. Paragraph 78 also recalls the crucial role of the training and the advice to farmers in applying new techniques. Concerning the current *Farm Advisory System*, see the report: http://ec.europa.eu/agriculture/farm-advisory-system/com2010-665_en.pdf (in references - point 6).

³³ See Paragraphs 51 and 92 of the EP Resolution of 8 July 2010.

5. COMPATIBILITY WITH SIMPLIFICATION AGENDA

5.1. Proposal (Section 1, 6.1 and Annex)

The main, specific references to simplification in the Communication appear in relation to cross compliance, market measures and rural development. The first proposes providing farmers and administrations with a simpler and more comprehensive set of rules, without watering down the concept of cross compliance itself. The second cites the need for "*streamlining and simplifying*" the market measure instruments currently in place. The third suggests a simplified set of indicators in the Common Monitoring and Evaluation Framework. Continuation of the work on simplification is also cited as an essential element in ensuring controllability of the measures proposed.

5.2. EP Resolution 8 July 2010

In a dedicated section headed "*A common and simple policy*" (Paragraphs 55 to 59), the EP Resolution called for a "*simplified support system*", which must be "*easy to administer, transparent, and reduce red tape and administrative burdens on farmers, particularly for smaller producers*" (³⁴). The simplification of the CAP was also the subject of a separate EP Resolution of 18 May 2010, which stressed the need for the CAP to be "*simpler, more transparent and more equitable*" (Paragraph 11) (³⁵).

5.3. Observations

Given the nature of the Commission's proposals, it is perhaps not surprising that few references are made to 'simplification'. There is a clear tension between simplifying a policy, by reducing the administrative burdens and conditions attached to payments, and simultaneously attempting to improve the targeting and legitimacy of payments and their efficiency in delivering public goods. As income support payments complete the move to an area basis, however, the retention of a system of "*transferable entitlements that need to be activated by matching them with eligible land*" could be seen as being rather anachronistic.

5. QUESTIONS ON COMPATIBILITY WITH SIMPLIFICATION AGENDA

- *To what extent are proposals for a multi-tiered Pillar 1 (with compulsory and voluntary elements), capping with labour adjustment and extra payments for small farmers consistent with the 'simplification' agenda?*
- *Similarly, to what extent does the proposal to target support exclusively to 'active farmers' fit with a drive for further CAP simplification, given the potential difficulties in finding a robust definition and then implementing its conditions?*
- *Under a generalised, area-based payment system, why would it be necessary to retain the complexity of entitlements?*

³⁴ Paragraph 87 also noted the EP's belief that "*the design and implementation of the new CAP should have simplicity, proportionality and the reduction of bureaucracy and of administrative costs at its heart*".

³⁵ *European Parliament resolution of 18 May 2010 on simplification of the CAP (2009/2155/INI - T7-0172/2010)* - see references.

6. TOWARDS A CAP FOR PUBLIC GOODS

6.1. Proposal (Sections 1, 2, 3, 4, 5, 6 and Annex)

One of the strategic aims of the proposal is to support farming communities that provide European citizens with quality and diversity of food produced sustainably, in line with Europe's environmental, water and animal welfare ambitions.

The Communication has as its basis the idea that the future system of remunerating collective services that *'active farmers'* provide to society would increase the effectiveness and efficiency of support and further legitimise the CAP. To achieve this, it is proposed that the future CAP should contain a greener and more equitably distributed first pillar and a second pillar focusing more on competitiveness and innovation, climate change and the environment.

6.2. EP Resolution 8 July 2010

The EP resolution devoted much attention to the issue of public goods. In particular, it recalls that agriculture has always been a producer of first generation public goods (food security and food safety) and that this purpose "*should continue to constitute the primary raison d'être for the CAP*" (Paragraph 6). The EP resolution also included in the objectives of the future CAP what is described as 'second-generation' public goods - such as the environment, land management or animal welfare - regarding these as being complementary to the first generation goods, rather than replacing them.

A specific chapter (Paragraphs 30 - 36) is devoted to the role of the future CAP in delivering public goods. In this chapter, the EP stresses that food is the most important public goods produced by agriculture and highlights how the failure of the market to recognise the value of public goods is the basis of the need to compensate farmers for their production, particularly in the less favoured areas.

Regarding the issue of environmental public goods, the EP believes that incentives should be provided to optimise the delivery of eco-system services and further improve the sound environmental resource management of EU farmland. In pursuing these objectives and, in particular, the mitigation of climate change, the EP considers that an important role is played by advances in knowledge, by better use of innovations stemming from research and development and improving the efficiency of agricultural production (Paragraph 53).

6.3. Observations

The Communication seems to focus attention on **supporting the production of environmental public goods**. Even if the focus of the changes included in the Communication is on how to integrate public goods into the first pillar, it is clear that rural development will continue to play a central role in their delivery.

Despite the Communication's references to various public goods (such as animal welfare and health, food security, environment, climate change, social and territorial balance), the proposals focus their attention narrowly on a greener and more equitably distributed first pillar. In the section on future CAP instruments, no reference is made to public goods related to social externalities (in particular animal welfare and food security).

If we agree that **animal welfare** is a public good, it would be more consistent with the proposed configuration of the single payment to put this in the requirements **under the green component**. This would support the agricultural sectors most exposed to the farm income crisis. Moreover, the costs incurred to comply with the requirements of the legislation on animal welfare are high and are not compensated by the market (an essential feature of a public good) and are far removed from the other laws outside the EU. The support provided for the adaptation of existing legislation in the rural development regulation, although very important, is a structural and non-direct investment to offset the extra costs of managing animal welfare.

In general, while the direction of travel of the Communication appears to be towards a 'greener' Pillar 1, with top-up payments, **the overall architecture of the future CAP is still unclear in both the definition of the environmental target and the related instruments**.

6. QUESTIONS ON PUBLIC GOODS

- *Why is animal welfare not included in the requirements under the greening component?*
- *How will it be possible to evaluate the efficiency of delivery of public goods between the mechanisms across the two respective pillars?*

II. FUTURE INSTRUMENTS: DIRECT PAYMENTS

7. GENERAL APPROACH AND DISTRIBUTION OF DIRECT PAYMENTS

7.1. Proposal (Sections 1, 2 and 6.1)

The Communication makes explicit the need for a **greener and more equitably distributed first pillar** (Section 1). In this sense, the Commission is proposing adjustments to the current configuration of decoupled payments, already regarded, in principle, as being capable of providing basic income support and delivering the basic public goods desired by European society (Section 2). The future first pillar should be based on a model of support, paid on an annual basis to all active farmers, adapted on the basis of **two fundamental objectives**:

- to reach a more equitable **distribution** of the direct payment support;
- to **redesign and better target** support to make it more consistent with its economic (basic income support), environmental (provision of environmental public goods) and territorial functions.

In relation to the distribution objective, the Communication proposes a system that limits the gains and losses of national envelopes "*by guaranteeing that farmers in all Member States receive on average a minimum share of the EU-wide average level of direct payments*".

As regards the second objective, the new direct payments appears to be composed of **four main components**: basic income component, green component, additional income payments in "*areas with specific natural constraints*" and a limited voluntary coupled support (see Annex).

A simple and **specific support scheme for small farmers** is proposed to enhance the competitiveness and the contribution to the vitality of rural areas and to cut red tape.

Finally, the Communication includes a specific objective of **simplifying cross-compliance rules**, which is consistent with the overarching aim of CAP simplification, more generally.

7.2. EP Resolution 8 July 2010

The EP calls for a equitable distribution of CAP payments that should be fair to farmers in both new and old Member States (Paragraph 45) ⁽³⁶⁾ and for a **simplified support system** (Paragraph 56) in which the direct support (paid to provide public goods and to stabilise farmers' incomes (Paragraph 64)) **should move to an area basis in all Member States within the next financial programming period**. The EP underlines the need for a **sufficient transition period** allowing farmers and agricultural structures that are still using the historical payments system the flexibility to adapt to the changes and avoid too radical a redistribution of support (Paragraph 65).

³⁶ See also the EP Resolution of 29 March 2007 on the integration of the new member States into the CAP (P6_TA (2007) 0101). See references - point 2.

In order to reflect the wide diversity characterising European agriculture, the EP believes that **the hectare basis alone will not be sufficient**, and therefore **calls for additional objective criteria** to be evaluated in terms of their potential impact, taking into account the complexity of the agricultural sector and the differences between Member States, in order to achieve a more balanced distribution (Paragraph 64).

7.3. Observations

The Communication alludes to a proposal that has found much attention in the public debate on the future of the CAP post 2013, that of a universal **flat rate payment**. The preferred model, however, moves away from this, with the Commission actually proposing to **combine the use of a single flat rate direct payment with the need to take into account the diversity of economic and physical conditions** affecting European agriculture, as well as the need to limit economic losses and gains of Member States (see §4).

The paper does not define the national budgetary envelopes and no reference is made to the basis on which such allocations could be made. It is also not clear how the Commission intends to establish a system to limit the *"gains and losses of Member States by guaranteeing that farmers in all Member States receive on average a minimum share of the EU-wide average level of direct payments"*.

Regarding the **beneficiaries of direct payments**, the paper states that payments would be confined to **"active farmers"**, which raises interesting questions about how these would be defined (see §12).

In general, the scheme proposed in the Communication is rather vague. In particular, there are several outstanding issues that need to be resolved in order to define more clearly the approach taken by the Commission:

- The new structure of direct payments includes some actions that were previously part of the second pillar (see § 9 and § 10). It is not clear how this transfer will take place or whether this transfer will be accompanied by a reallocation of resources from the second to the first pillar. If this transfer is not to be accompanied by such a reallocation, then the resources devoted to basic income support will be squeezed.
- The above question is closely linked to the issue of the balance of expenditure between the components of the proposed scheme and more generally to the balance between the first and second pillar. The uncertainty on this point prevents a full understanding of which of the three broad policy options (see §3) would be best to pursue.

The proposal seems to allow **greater flexibility for Member States** in the application of direct payments. This increased flexibility is also accompanied by a structural change to the system of direct payments, which will have implications for the way the resources represented by the different components of the new support are distributed.

7. QUESTIONS ON GENERAL APPROACH AND DISTRIBUTION OF DIRECT PAYMENTS

- *On which objective criteria (e.g. agricultural output, area or employment) will the budget for direct payments be allocated between Member States?*
- *How will the proposed system to limit the "gains and losses of Member States by guaranteeing that farmers in all Member States receive on average a minimum share of the EU-wide average level of direct payments" work in practice?*
- *What will be the balance of expenditure between the four components of the new model of direct support?*
- *What degree of flexibility will be granted to Member States in implementing the different components of direct support?*

8. BASIC COMPONENT OF DIRECT PAYMENTS

8.1. Proposals (Section 6.1)

Basic income support will be granted through a basic decoupled direct payment, providing a **uniform level of obligatory support to all farmers in a Member State (or in a region)** based on transferable entitlements that need to be activated by matching them with eligible agricultural land, plus the fulfilment of cross-compliance requirements.

8.2. EP Resolution 8 July 2010

The EP believes that there should be a basic EU-funded direct area payment to all EU farmers in order to ensure the social and economic sustainability of the European agricultural production model. This should provide basic food security for European consumers, allow farmers to produce high-quality food competitively and ensure that farming activity and jobs in rural areas are encouraged across the EU, while also providing baseline public goods through adherence to the cross-compliance requirements (Paragraph 69).

8.3. Observations

The Communication proposes to maintain a specific support to farm incomes, taking into account the severe impact of the economic crisis on agriculture (§1 - footnote 14) ⁽³⁷⁾.

Payments would be awarded on a **decoupled, per-hectare basis**. It would be a uniform area payment to all farmers in a Member State (or a region), implying **the end of the historic basis for payments as practiced in some Member States**.

The **cross-compliance requirements**, to which the Communication refers, are presumably similar to those which currently exist, with the added inclusion of the Water Framework Directive. In this respect, further legitimacy for the CAP could be achieved through the possible inclusion of requirements relating to **social legislation**.

In order to understand the implications of the changes proposed, it would be desirable to have a clearer understanding about the assumptions regarding the classification of **eligibility of land**.

Finally, as highlighted by the EP (Paragraph 65), the move away from the historical basis may create particular challenges for Member States or regions with a relatively large amount of "*naked land*" (unclaimed eligible land).

8. QUESTIONS ON BASIC COMPONENT OF DIRECT PAYMENTS

- *What assumptions have been made regarding the eligibility of land for this component?*
- *What is the weight of this component in the proposed model?*

³⁷ The impact of abolishing specific income support has been analysed by LEI - Wageningen UR (2010): "*Farm viability in the European Union. Assessment of the impact of changes in farm payments* (see references - point 8).

9. GREENING COMPONENT OF DIRECT PAYMENTS

9.1. Proposals (Section 6.1 and Annex)

The Communication indicates that a major feature of the Commission's proposed reforms will be the "*enhancement of environmental performance of the CAP through a **mandatory 'greening' component** of direct payments by supporting environmental measures applicable across the whole of the EU territory*".

Such a 'greening' component "*could take the form of simple, generalised, non-contractual and annual agri-environmental actions that go beyond cross compliance*" (Section 6.1), based on the supplementary costs for carrying out these actions (Annex). The Communication also includes the possibility of including the requirements of current Natura 2000 areas and enhancing certain elements of the GAEC standards.

9.2. EP Resolution 8 July 2010

The EP Resolution proposed the introduction of an **EU-funded top-up payment for farmers through simple multiannual contracts** rewarding them for reducing their carbon emissions per unit of production and/or increasing their sequestration of carbon in the soil through sustainable production methods and through the production of biomass (Paragraph 71) and called for "*clear and measurable criteria and targets to be defined appropriately to allow these payments to be implemented as soon as possible in every Member State*".

The EP Resolution also called for "*the vast bulk of agricultural land to be covered by agri-environmental schemes to reward farmers for the delivery of additional eco-system services*" (Paragraph 77), but linked this recommendation to an increased rural development budget, rather than the alternative explored by the Commission of "*greening*" Pillar 1.

9.3. Observations

In introducing the new greening aids, it is noted they will be a compulsory component of the system of direct payments. However, ambiguity surrounds the **forms of implementation** of the different sorts of environmental actions (requirements concerning Natura 2000 areas, GAEC standards) and the **cross-compliance baselines**.

There is a passing reference to **high nature value** (HNV) areas ⁽³⁸⁾ in the section on rural development, but it is similarly unclear why HNV farming is excluded from the greening component in comparison to the Natura 2000 areas.

The agri-environmental actions cited in the text are part of current activities covered by agri-environmental measures in the second axis of the rural development pillar. It is not clear if this transfer of function is also to be accompanied by a **transfer of resources from the second to the first pillar**. Which activities remain within the second pillar and which are transferred across into the greening component remains uncertain. There is also no recognition given to the need for a managed transition

³⁸ See Beaufoy, G. - Marsdem, K. (2010): "*CAP Reform 2013. Last chance to stop the decline of Europe's High Nature Value farming?*", EFNCP - BirdLife International - Butterfly Conservation Europe - WWF, September 2010 (References - point 8).

for farmers with existing agri-environment contracts, extending beyond 2013, whose land management obligations will be at least partly subsumed into the new Pillar 1 greening component.

Even if this greening component is compulsory, it seems likely that Member States will retain flexibility powers in order to tailor the implementation of the 'greening' component to the specific national and regional circumstances. It might be useful, and consistent with the objective of better targeting of support, to provide a broad set of agri-environmental actions from which Member States can "build" their own green component, in line with their specific environmental needs.

9. QUESTIONS ON THE GREENING COMPONENT OF DIRECT PAYMENTS

- *How will the Natura 2000 requirements and enhanced GAEC standards included in the greening component be implemented?*
- *What will be the differences between the cross compliance in the basic income component, the environmental requirements in the greening component and the baseline of the more targeted agri-environmental measures in the second pillar?*
- *What evidence does the Commission have to conclude that the proposed new "greening" component in Pillar 1 will deliver environmental public goods more efficiently than redeploying the same resources towards properly targeted schemes in Pillar 2?*

10. PAYMENTS FOR 'AREAS WITH SPECIFIC NATURAL CONSTRAINTS'

10.1. Proposals (Section 6.1 and Annex)

The third component of the proposed new system of direct payments envisages an additional income support to all farmers in **areas with specific natural constraints**, in the form of an area-based payment. This payment would be complementary to the support given under the second pillar.

10.2. EP Resolution 8 July 2010

The general EP approach calls for "*the continuation of specific measures to compensate farmers producing in disadvantaged areas*" and underlines that any reform, in particular regarding how LFAs are designated and classified, should be granted an adequate phasing-out period to the farmers which may be excluded under any new rules (Paragraph 74).

With the Resolution of 5 May 2010 on "*agriculture in areas with natural handicaps: a special health check*", the EP underlined that support for Less Favoured Areas is an essential component of the second pillar of the Common Agricultural Policy (Paragraph H) and stressed the importance of an appropriate compensatory payment for Less Favoured Areas as an indispensable tool to secure the provision of high-value public goods (Paragraph 1)

10.3. Observations

The Communication **does not make clear whether the transfer of functions will be matched by the transfer of the respective resources**. Moreover, it is not clear how the future support to farmers in LFA areas will be managed across the two pillars.

In any case, for the purpose of giving an assessment of these options it is necessary to know the **classification of LFA areas**, whose approval is expected next year.

10. QUESTIONS ON PAYMENTS FOR 'AREAS WITH SPECIFIC NATURAL CONSTRAINTS'

- *Will the new classification of Less Favoured Areas be ready before the legislative proposals on the future of the CAP?*
- *Which elements of the LFA farming support will remain in the second pillar?*

11. RESIDUAL VOLUNTARY COUPLED ELEMENT

11.1. Proposal (Section 6.1 and Annex)

A fourth tier would be a limited voluntary coupled support that may continue to be granted *“in order to take account of specific problems in certain regions where particular types of farming are considered particularly important for economic and/or social reasons”*.

11.2. EP Resolution 8 July 2010

The EP highlights that an adequate margin for flexibility should be left to Member States to enable them to respond to the specific needs of their territory and proposes that this flexibility would take the form of capped coupled payments (Paragraph 66).

11.3. Observations

This component seems **similar to the partial coupling remaining within the Single Payment Scheme and to the current Article 68 measure** for particular regions or types of farming, but no references are made to specific measures available and their mode of application. Furthermore the Communication propose to transfer the current risk management measures, now in the Art. 68 and 69, to the second pillar.

In comparison with the current Article 68, however, the proposal appears to have more limited objectives, as it refers solely to measures to address disadvantages for farmers in certain sectors and regions. No specific references are made about measures focused on enhancing and protecting the environment and on improving the quality of the agricultural products, nor are there references to risk management measures.

Although there is no specific reference to the livestock sector, the elements on which the support is based would likely include the farmers acting in the livestock sector with no eligible hectares (special aids define by Art. 60 Council Regulation (EC) No 73/2009).

11. QUESTIONS ON THE VOLUNTARY COUPLED ELEMENT

- *Which elements of the current Art. 68 will be support by the new coupled voluntary aid?*
- *Would this component provide support to livestock producers with no eligible hectares in continuity with the current situation?*

12. DIRECT PAYMENTS BENEFICIARIES

12.1. Proposal (Sections 4 and 6.1)

The Communication proposes targeting support to "*active farmers*", responding to the criticism of the European Courts of Auditors - ECA (³⁹).

12.2. EP Resolution 8 July 2010

The EP Resolution has no references concerning this topic.

12.3. Observations

Currently, a "*farmer*" is defined as a natural or legal person who exercises an "*agricultural activity*" (Article 2(a) of Regulation (EC) N° 73/2009) (⁴⁰). An "*agricultural activity*" is defined to mean the production, rearing or growing of agricultural products including harvesting, milking, breeding animals and keeping animals for farming purposes, or maintaining the land in good agricultural and environmental condition (GAEC) (Article 2(c) of Regulation (EC) N° 73/2009). The Commission has addressed the issue of the "*farmer definition*", referred to by the Court of Auditors in the framework of the Health Check. It has proposed that Member States should exclude natural or legal persons from the direct payments schemes whose business objectives **do not consist** of agricultural activities or whose agricultural activities are insignificant. However, the Council made this provision **optional** for Member States (Article 28(2) of Regulation (EC) N° 73/2009).

The Commission seems now to be proposing the **deletion of the optional basis** of Article 28(2) of Regulation (EC) N° 73/2009 in the context of the new CAP. Additionally, a European statute of "*farmer*" will not be proposed and the legal status of farmers will continue to be defined by national law. In this context, the Communication has not taken up the opportunity to define the (voluntary) European framework of the "*priorities holdings*" or "*priorities beneficiaries*" which apply to the CAP aids (within the first and second pillars) (⁴¹).

³⁹ See References (Point 5): *Annual Report concerning Financial Year 2008*, Sections 5.5, 5.17, 5.47 and 5.49.

⁴⁰ OJ L 30, 31.1.2009

(<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2009:030:0016:0099:EN:PDF>).

⁴¹ In order to encourage for example the farmers' participation in the organisation of the sector (cooperatives, local action groups, inter-branch agreements, etc), the delivery of public goods, the entrepreneurship in young farmers, the contractual negotiations, the gender mainstreaming (community property), etc.

12. QUESTIONS ON THE DIRECT PAYMENTS BENEFICIARIES

- *How does the Commission intend to improve the definition and targeting of support to "active farmers"?*
- *Given the increased focus on the delivery of public goods, to what extent is a more inclusive definition required, encompassing all those responsible for actively managing the land?*
- *Why has the Commission not proposed a voluntary EU framework defining a European statute of "farmers" and/or the "priorities beneficiaries" for the CAP aids?*
- *What sort of existing beneficiaries do the Commission want to disqualify through this initiative: landlord claimants, charities or trusts that have land kept in GAEC, or diversified enterprises whose income comes mainly from off-farm activities?*

13. DIRECT PAYMENTS TO SMALL FARMERS

13.1. Proposals (Sections 3.3, 5 - Objective 3, and 6.1)

Under the sections on territorial balance (Sections 3.3 and 5 - Objective 3), the Communication underlines the importance of rural employment as the basis of the social fabric of rural areas, and the structural diversity in farming systems. In this context, small farms play a specific role in contributing to the attractiveness and identity of rural regions (Section 5). The Communication aims to improve the conditions for small farmers and develop local markets. It also proposes a new scheme (inside the first pillar) specifically to support small farmers in order to enhance their competitiveness and the contribution to the vitality of rural areas, as well as cutting red tape (Section 6.1).

13.2. EP Resolution 8 July 2010

The EP Resolution included some references to structural diversity and equity issues: Paragraphs 16, 18, 19, 23, 25, 29, 40, 45, 47, and 64. Specifically, the EP believes that in order to reduce the disparities in the distribution of direct support funds between Member States and to reflect the wide diversity characterising European agriculture, the hectare basis alone would not be sufficient, and therefore calls on the Commission to propose additional objective criteria and to evaluate their potential impact (Paragraph 64).

1.7.3. Observations

The Communication does not provide any definition of "*small farmer*", neither does it explain whether this notion is synonymous with (or restricted to) subsistence farms (SFs) and/or semi-subsistence farms (SSFs).

In fact, the definition of "*small farmer*" is controversial, with three main criteria currently being used **at a European level** ⁽⁴²⁾:

- **Physical measure** (e.g. UAA). In this case a small farm would have less than 5 ha, despite the variety in land fertility or specialisation.
- **Economic size** (below a certain ESU threshold). In 2007 there were 11.1 million small farms **below 8 ESU** within the EU-27. Of these, 6.4 million were **below 1 ESU**, therefore considered SFs and the remaining 4.7 million were SSFs ⁽⁴³⁾.
- **Market participation** (the share of output sold). In this case, farms that sell less than 50% of their agricultural production are considered SSFs ⁽⁴⁴⁾.

Additionally, some **Member States** use "*standard labour requirements*" (SLR) which allows them to differentiate between hobby farms.

In this context, the Commission ought to explain better the scope of the notion of "*small farmer*" and, specifically, if the legislative proposals would include the total exclusion of

⁴² See the Sofia Davidova background paper presented in the seminar on semi-subsistence farming in Sibiu (Romania) on 13th - 15th October 2010 (*Semi-subsistence farming in Europe: Concepts and key issues* - see bibliographical references: point 6-e).

⁴³ The total number of holdings in 2007 in the EU-27 was 13,7 million, so the share of SFs and SSFs was equal to 46,6% and 34,5% of the total number.

⁴⁴ Council Regulation (EC) N° 1698/2005 defines SSFs as "*agricultural holdings which produce primarily for their own consumption and also market a proportion of their output*" (Article 34.1, page 18 OJ L 277, 21.10.2005).

holdings from the direct payments schemes whose business objectives do not consist of agricultural activities or whose agricultural activities are insignificant (see above, §12).

Furthermore, the Communication seems ready to introduce a **simple and specific support scheme to small farmers** inside the first pillar (Section 6.1). However, the Communication lacks detail concerning the nature of these direct aids (possibly to be calculated in the form of a minimum share of the basic income support).

13. QUESTIONS ON SMALL FARMERS

- *What is the detailed definition of "small farmer"?*
- *Is the notion of "small farmer" here synonymous with subsistence farms and/or semi-subsistence farms?*
- *Will the support to small farmers inside the first pillar be calculated on the basis of a share of the basic income support?*

14. CAPPING OF DIRECT PAYMENTS

14.1. Proposal (Section 6.1 and Annex)

The Communication proposes the adoption of an **upper ceiling for direct payments** received by large individual farms, although exemptions may be possible for large farms with high employment numbers, as **salaried labour intensity** will be taken into account.

14.2. EP Resolution 8 July 2010

The only reference to capping in the EP resolution is in regard to the consideration that an adequate margin for flexibility should be left to Member States, to enable them to respond to the specific needs of their territory and to prevent production from stopping completely or the diversity of farming from being reduced (Paragraph 66). The EP believes that this margin for manoeuvre would take the form of capped coupled payments for vulnerable agriculture sectors and territories and environmentally sensitive areas.

14.3. Observations

The proposal for an **upper ceiling** for direct payments received by large individual farms (capping) is not well defined. It is not clear what the **threshold** should be for the upper ceiling applied to the basic income support payments and it is also unclear how the exemption based on "**salaried labour intensity**" could be applied. Moreover, the reference to this issue is made in the description of the "*basic income component*".

14. QUESTIONS ON CAPPING OF DIRECT PAYMENTS

- *Why is the capping restricted solely to the basic component?*
- *What should be the threshold for the upper ceiling applied to the basic income support payments?*
- *How could the exemption based on 'salaried labour intensity' be applied in practice?*
- *Given the historic resistance previous 'capping' proposals have faced from those Member States with the highest distribution of large farms, how will the Commission ensure this idea navigates its way through to the final reform agreement?*

III. FUTURE INSTRUMENTS: MARKETS

15. MARKETS INSTRUMENTS

15.1. Proposals (Section 6.1)

The Communication outlines three policy fields concerning markets measures:

- Potential **adaptations of the single CMO** including the extension of the intervention period, the use of disturbance clauses and private storage to new products. Such market measures, and in particular the public intervention, should only be used as a safety net in case of price crises and potential market disruption.
- Additionally, the "**quality package**" to be presented by the end of 2010 ⁽⁴⁵⁾ would improve possibilities for farmers to better communicate the qualities, characteristics and attributes of agricultural products to consumers.
- Acknowledging that improving the functioning of the **food supply chain** is necessary, it lists key issues of interest such as the imbalance of bargaining power, contractual relations, the need for restructuring and consolidation of the farm sector, transparency, and the functioning of the agricultural commodity derivatives markets. The milk package to be presented before the end of 2010 will have to specify these measures.

15.2. EP Resolution 8 July 2010

The EP Resolution devotes many paragraphs to market policy: 3, 4, 10, 15, 26, 27, 41, 43, 44, 79 and 80. It calls for a safety net in view of the agricultural market failures (Paragraph 26), specific features of agricultural production (Paragraph 27) and the increasing volatility of prices (Paragraph 12).

The EP Resolution also calls for measures to improve the functioning of the food supply-chain (Paragraphs 42 and 82).

15.3. Observations

The systemic instability of agricultural markets has always been a key factor in agricultural policies. The economic stability of rural areas can be jeopardised by crises caused by different types of *natural disasters*, from climatic events to livestock or plant diseases. The biological nature of agricultural production processes and their strong dependency on natural and climatic conditions induce a high degree of uncertainty surrounding the economic performance of farm enterprises, in comparison to what happens in other sectors of the economy.

A broad consensus across the analyses performed points to an increasing volatility of agricultural markets in the future ⁽⁴⁶⁾. Price and supply crises will be likely to be more frequent and more severe with negative impacts on the incomes of producers and, of course, on food availability, particularly for the poorest population groups (see §16).

⁴⁵ See bibliographical references - Point 6 - c.

⁴⁶ Depending on different elements: e.g. rise in global food demand; situation of world food stocks; reinforcement of interdependence between the prices of agricultural products and energy prices (e.g. biofuels); trends in financial markets and currency fluctuations; etc.

Price variation is desirable in terms of providing price signals that reflect changing market conditions which lead to resource reallocations. Nevertheless, the extreme price volatility in several agricultural commodity markets in recent years is creating mostly negative consequences for processors, farmers and other food supply chain participants. Thus, the need for tools with which to manage price volatility and the associated risk becomes a central issue for the new CAP.

The factors contributing to the 2007/2008 agricultural price spikes and the subsequent volatility have been analysed extensively in the literature⁽⁴⁷⁾. Some recent studies conjecture that the excess liquidity, speculation by index fund activity, strong links between agricultural and energy prices and, finally, the increasing demand for crops for the production of biofuels all played key roles during the 2008 price boom⁽⁴⁸⁾. These conclusions provide insights into the determinants of the future path of food commodity prices. In consequence, it may be appropriate to establish specific mechanisms to address any deep crisis of the market.

Unfortunately, the Communication does not provide much detail on the development of market management instruments and the products concerned are not even defined.

Furthermore, the references to the "*quality package*" and the "*milk package*" could be interpreted as implying they are precursors to the CAP reform, because they should be approved before the adoption of the legislative proposals⁽⁴⁹⁾. However, it is not yet apparent how, or indeed whether, the new mechanisms to improve the functioning of the food supply chain proposed for the milk sector will be implemented in others sectors.

The evaluation of the proposed packages will not be speedy since the new mechanisms identified (regarding contractual relations, restructuring, bargaining power along the chain, consolidation of commodity derivatives markets) will need a long period of implementation. The Communication does not develop the modalities and timing of the implementation.

Under the circumstances, the following instruments serve, as suggestions only, as examples of the measures that could be used to build a new CAP regulatory framework and to update the **Single CMO**:

- **Private storage** (is already mentioned by the Communication but the products concerned are not specified).
- **Public intervention** (safety nets).
- **Risk management tools** (e.g. income insurance schemes, mutual funds, futures markets). In this context, if commodity derivatives markets are

⁴⁷ See for example: FAO (2009) or HM Government (2010). See references - point 8.

⁴⁸ Baffes & Hanriotis (2010). See references - point 8.

⁴⁹ The '*Dairy legislative package*' has to be presented by the European Commission before the end of 2010 after the publication of the Conclusions by the High Level Group on Dairy of May 2009 concerning mid-term and long-term arrangements for this sector, given the expiry of quotas on April 1, 2015. The High Level Group on Dairy invited the Commission to consider facilitating the use of "*future markets*", via targeted training programmes, and to explore new WTO *Green Box* compatible (safety net) instruments (§ 22) in the framework of the CAP post-2013 in order to reduce income volatility. Other suggestions outlined in the Conclusions included an examination of whether any of the current provisions for inter-professional organisations in the fruit and vegetable sector could also be applicable in the dairy sector (see bibliographical references - point 6 - b).

considered as market measures, it is not clear why the proposed risk management toolkit is located in the second pillar ⁽⁵⁰⁾.

- **Contractual mechanisms** inside the food chain in order to strengthen the bargaining power of farmers and to ensure greater market stability, including the possible extension of current competition rules.
- **Inter-professional organisations** and their regulatory role, including possible extension of the current provisions for producers' organisations in the fruit and vegetable sector to other production areas.
- **Internal food aid** (see §16) ⁽⁵¹⁾.
- **Security food stocks** (emergency reserves) in coordination with the *United Nations World Food Program* and the *International Fund for Agricultural Development (IFAD)*.
- **Budgetary Reserve** for severe crises of agricultural markets. It may be appropriate to create budgetary reserves to be used to address emergencies. This could also include the interventions carried out by member countries in the event that market disruptions distort competition within the EU ⁽⁵²⁾.
- **Internal and external promotion** ⁽⁵³⁾.

Obviously, the new market measures must take account of the EU's financing constraints, as well as its multilateral commitments (as negotiated in the WTO Doha Round).

15. QUESTIONS ON MARKET INSTRUMENTS

- *Will it be possible to replace the safety nets and others markets measures by the risk management toolkit and commodity derivatives markets?*
- *Will the new mechanisms to improve the functioning of the food supply chain, proposed for the milk sector, be extended to others sectors?*
- *Will the future framework of derivatives markets, mentioned in the market measures section, be included within the Single CMO?*
- *Why is the risk management toolkit not incorporated within the Single CMO?*

⁵⁰ Given the high diversity of risks and of socioeconomic backgrounds in the EU-27, it does not seem advisable to settle on a homogeneous common insurance system. Nevertheless, it could be worth establishing a common regulatory framework for the national risk management tools in the Single CMO. The possible turnover of premiums under a hypothetical EU support is approximately quantified in several scenarios by the JCE Study (2009) "*Risk Management and Agricultural Insurance Schemes in Europe*" (see references, point 8).

⁵¹ http://ec.europa.eu/agriculture/markets/freefood/index_en.htm

⁵² See EP Resolution of 8 July 2010: Paragraphs Z, 43, 58, 79, 80 and 90. In particular paragraph 79, contains a proposal to establish a special reserve budget line that should be made available in the EU budget which could be activated rapidly to respond to crises which arise.

⁵³ See in references (point 5): Special report 10/2009 from the Court of Auditors (<http://eca.europa.eu/portal/pls/portal/docs/1/3220313.PDF>).

16. FOOD AND AID FOR DEPRIVED PERSONS

16.1. Proposals (Section 4)

The Communication just mentions in a footnote that the CAP will provide contributions to the EU flagship initiative on "*An European Platform against poverty*" inside the *EU 2020 Strategy - Inclusive growth*.

16.2. EP Resolution of 8 July 2010

The EP (Paragraph 86) took the view that the CAP must enable a healthier diet to be made to all consumers, particularly the poorest among them. The EP proposed to continue aid programs for the poorest in society, in order to combat poverty and improve health.

16.3. Observations

The internal food aid is an important mechanism in others agricultural policies (⁵⁴). The current recession came after the peak of prices, breeding further uncertainty for people with lower incomes, in particular in the countries of Eastern Europe, where the proportion of spending on food consumption is still comparatively high. In this perspective, the sole CAP instrument to address this issue is the intervention aimed at distributing free *food to the most deprived persons* in the EU (⁵⁵). The programme is supported by a direct financial contribution and the allocation of resources between Member States is based on population data and statistics on poverty provided by EUROSTAT (⁵⁶).

The new CAP could look to incorporate this food aid scheme for needy people. Furthermore, it could justify an increased budget on the basis of rising food prices and extend the range of products which could be provided. This approach does, however, run counter to the position of some Member States, who view this more as a Member State social policy issue.

16. QUESTIONS ON FOOD AND AID FOR DEPRIVED PERSONS

- *To what extent is there scope, within the proposals for the future CAP, to include measures to enable a healthier diet to be made available to particularly the poorest consumers in the EU?*
- *Will the new CAP include the current food aid scheme for needy people?*
- *Would it be appropriate to introduce this programme within the Single CMO?*

⁵⁴ See references (point 8): "*The US Farm Bill 2008 and comparison with the EU CAP after Health Check*". EuroCare GmbH. IP/B/AGRI/FWC/2006-146-Lot4-C01-SC1, February 2009.

⁵⁵ Regulation (EC) N° 807/2010 (OJ L 242, 15.9.2010) and Regulation (CE) 945/2010 (OJ L 278, 22.10.2010). (<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2010:242:0009:0020:EN:PDF>) (<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2010:278:0001:0008:EN:PDF>).

⁵⁶ The "*risk of poverty rate*" represents the share of people with an income below 60% of the national average income.

17. WELL FUNCTIONING TRANSMISSION OF MARKET SIGNALS

17.1. Proposals (Section 5 and 6.1).

The Communication includes, as part of Objective 1 ("*Viable food production*") the need to enhance the value of agriculture's share in the food chain in order to redress the balance of power, since agriculture is dispersed compared to other sectors along the chain.

In reference to the 2009 crisis in the dairy market, the Communication shows the need to introduce new policy elements with respect to the functioning of the food chain.

17.2. EP Resolution 8 July 2010 (Paragraphs 26, 42, 80, 82)

The EP believes that there is an urgent need to strengthen the position of primary producers within the food-supply chain through a range of actions to address transparency, contractual relationships and unfair commercial practices (Paragraph 82). In this regard, the EP Resolution calls for measures to be taken to strengthen primary producers' and producer organisations' management capacity and encourages the formation of organisations that strengthen the links between the various stakeholders within branches.

Within the Resolution of 7 September 2010 on "*Fair revenues for farmers: A better functioning food supply chain in Europe*", the EP calls to improve the European food price monitoring tools (Paragraph 5). The EP also warns that contract farming imposed by buyers, vertical integration and futures, which are playing an increasingly important role, could weaken competition and farmers' bargaining positions (Paragraph 35). The EP calls for the promotion of fair contracting between all the actors of the food supply chain, based on terms negotiated with farmers' and producers' organisations, including sectoral and interbranch organisations, so as to enhance sustainable farming practices and ensure best product quality, to reduce purchase prices for inputs and to guarantee fair prices, and to provide for an easily accessible system to guard against breach of contract by buyers (Paragraph 36).

17.3. Observations

The need to balance power along the supply chain is not reflected in the part devoted to the tools of the future CAP. The reference to the transparency of the sector and the need to strengthen the role of contractual relations will probably find its place in the legislation on the milk package. This theme will, however, be important for all farm sectors.

17. QUESTIONS ON WELL FUNCTIONING TRANSMISSION OF MARKET SIGNALS

- ***Can the "milk package" be considered as a precursor to the regulations that will then be extended to the other sectors?***

18. DERIVATIVES MARKETS

18.1. Proposals (Section 6.1)

The Communication lists, in the section on market measures, the functioning of the agricultural commodities derivatives markets as one of the key issues to be pursued.

18.2. EP Resolution 8 July 2010

The EP calls for "*measures to help reduce volatility and provide stable conditions for agricultural business and planning*" (Paragraph 80). In this context, the EP takes the view that new innovative economic and financial tools such as across-the-board harvest risk insurance policies, futures markets and mutualisation funds should also be considered as a way of dealing with extreme market or climate conditions, without disturbing any private schemes that are being developed.

18.3. Observations

On this point, the content of the Communication is very vague. The market for derivatives is still very under-developed across Europe and only a relatively few farmers use these instruments to hedge against market risks. It is not clear what the specific proposals will be to encourage the use of these tools.

Regarding the functioning of the agricultural commodities derivatives markets, it would be useful to know how this intention relates to the Commission proposal on OTC derivatives, central counterparties and trade repositories and in the more comprehensive and ambitious reform of the raw materials markets plan that the Commission is pursuing.

18. QUESTIONS ON DERIVATIVES MARKETS

- *Will the development of derivatives markets that the Communication proposes, under the heading of market measures, be introduced in the Single CMO?*
- *How does the proposal to improve the functioning of the agricultural commodities derivatives market relate to the Commission proposal on OTC derivatives?*
- *How will the proposal seek to encourage farmers to access these tools?*

IV. FUTURE INSTRUMENTS: RURAL DEVELOPMENT POLICY (2nd PILLAR)

19. RURAL DEVELOPMENT INSTRUMENTS

19.1. Proposals (Section 6.1 and Annex)

As part of the proposals for rural development policy, the list of themes is expanded, with a notable new emphasis on innovation, and so too is the number of measures, with a **risk management toolkit** added to the menu. Such a 'toolkit' would be aimed at dealing with income uncertainties and market volatility, with these mechanisms being made available to Member States to address both production and income risks, ranging from a WTO green box compatible income stabilisation tool, to strengthened support for insurance and mutual funds.

The Communication also proposes new **effective delivery mechanisms**, suggesting that the current measures in the four axes would be targeted in a different way by setting quantified EU-level and programme-level targets, tied to incentives, to achieve a more outcome-based result. The potential benefits of a more locally-led approach are cited before the Communication stresses the importance of **strengthened coherence** between rural development policy and other EU policies, with a **common strategic framework** for EU funds being envisaged. It is also proposed that the set of indicators in the Common Monitoring and Evaluation Framework should be both simplified and improved for this purpose ⁽⁵⁷⁾.

Consideration of using **objective criteria** for the future distribution of rural development funding is proposed, although the Commission feels it would have to limit any resulting "*significant disruption*" from the current system.

19.2. EP Resolution 8 July 2010 (Paragraph 5, 16, 43, 64, 77 to 80)

The EP Resolution notes that "*rural development is now an integral part of the CAP architecture, and should remain an important element of the future CAP through a well-equipped rural development strategy with its focus on rural communities, improving the environment, modernising and restructuring agriculture, strengthening cohesion in EU rural areas, revitalising disadvantaged areas and areas at risk of abandonment, improving product marketing and competitiveness and maintaining employment and creating new jobs in rural areas, as well as on the new challenges addressed in the Health Check, namely climate change, renewable energies, water management and biodiversity*" (Paragraph 5). The EP also highlights the need for a new rural development strategy to create new green jobs through investment in "*modernisation and innovation, as well as new research and development techniques for adaptation to, and mitigation of, climate change*" (Paragraph 78). The EP also calls for an "*increased budget*" for rural development, if it was necessary, and for "*fair and objective criteria*" to be used as the basis on which future allocations would be made (Paragraphs 77 and 64).

The EP resolution includes proposals for a risk management system to mitigate the effects of extreme market price volatility and to provide a greater degree of stability (Paragraphs

⁵⁷ See RuDI (2010): "*Beyond indicators: Evaluating the process of EU Rural Development Policies*", RuDI -Rural Development Impacts, June 2010 - (references Point 8).

43, 79 to 80). The EP does not, however, specify that such a system should fit within a reconfigured Pillar 2.

19.3. Observations

There are very few concrete proposals to change Pillar 2 included in the Communication and it is not certain whether the Commission intends rural development to become a larger, more vital component of the CAP. The new emphasis on innovation and the inclusion of a risk management toolkit leaves the role of Pillar 2 in providing environmental public goods considerably watered down. Significantly here, not one mention is included of the more targeted agri-environment actions that presumably will be required to complement the generalised approach adopted in the 'greening' component of Pillar 1.

The Commission's decision to retain support for LFAs within Pillar 2, while simultaneously introducing Pillar 1 income support to all farmers in areas with specific natural constraints, brings into question the Communication's rhetoric around a clear "*separation between the two pillars*", without overlaps. Similarly, environmental measures to address Natura 2000 are referred to in the description of rural development policy and again in proposals for enhancing the GAEC standards attached to receipt of Pillar 1 payments.

The reference in the Communication to "*strengthened coherence*" between rural development policy and other EU policies, and the associated "*common strategic framework*" for EU funds, refers to the proposals contained in a letter sent by four Commissioners, including Dacian Cioloş (Agriculture), to the Commission President José Manuel Barroso, calling for key EU funds to be brought under the same umbrella from 2014, in order to cut out overlap and ensure better strategic spending (⁵⁸).

⁵⁸ The letter, sent in September 2010, was signed jointly by László Andor (Employment and Social Affairs), Maria Damanaki (Fisheries), Johannes Hahn (Regional Policy) and Dacian Cioloş (Agriculture)

19. QUESTIONS ON RURAL DEVELOPMENT POLICY

- *Since the Communication makes no reference to the rural development axes, does this imply that they will be replaced by a set of priorities or measures? If this is the case, what priorities will be set and what will be the measures?*
- *Will the transfer of part of the agri-environment measures into Pillar 1 be accompanied by a shift of resources?*
- *How does the Commission intend to set EU and programme level quantitative targets for the evaluation of rural development initiatives? Will the targets be linked to the overall priorities or to the different measures available?*
- *How will the monitoring system, based on indicators, be implemented on the specific measures?*
- *How will the proposed system of incentives, linked to the evaluation, work in practice? How might the proposed performance reserve be implemented and would resources be expected to move between different Member States as part of its operation?*
- *How will the Commission maintain separation and avoid overlaps between the LFA payments retained in rural development policy and the new supports for 'areas with specific natural constraints' proposed for Pillar 1?*
- *Which objective criteria should be used to provide the basis for future Pillar 2 allocations?*
- *How long would it be necessary to impose the limitations to the "significant disruption" caused by the redistribution of funds following a change to the allocation key?*
- *Why is the risk management toolkit included in the second pillar rather than the first?*
- *Based on the initial impact assessment analysis, how much resources will be diverted away from the existing rural development objectives to address the new innovation theme?*

V. SOME MISSED TOPICS FOR THE 2013 SCENARIO

20. BUDGETARY CONCERNS

20.1. Proposals (Sections 1, 3.3, 5, 6.1)

The Communication does not mention the budgetary concerns of the new CAP but does make the case for an EU-level expenditure on agriculture (Section 5). It mentions the Budget Review Communication in general terms (Section 1) and the CAP Communication also recalls the "*added value*" principle of EU spending (Sections 6.1 and 6.2) ⁽⁵⁹⁾. It also advocates an "*equitable distribution*" of first and second pillar aids between Member States and farmers (Sections 1, 3.3 and 6.1).

20.2. EP Resolution of 8 July 2010

The EP Resolution includes some references to the budget in Paragraphs 8, 20, 59, 61, 63, 68, 88, 89, 90, 91 and 92. The EP identified the need for key building blocks (Paragraph 67). Significantly, it notes that the budget must be "*adequate*" and funding for each of the priorities of the CAP must be agreed from the start of the reform (Paragraph 68), before calling for "*the amounts allocated to the CAP in the 2013 budget to be at least maintained during the next financial period*" (Paragraph 61).

20.3. Observations

At a cost of about €57 billions in 2010, the CAP is currently the EU's single largest item of expenditure. However, the Communication remains silent on the scale of the agricultural budget after 2013. It notes that public support for the agricultural sector and rural areas must be maintained in order to achieve the objectives proposed (Section 5). It also argues that an agricultural policy designed at an EU-level would provide for a more efficient use of budget resources than national policies. A common set of objectives, principles and rules can offer economies of scale to farmers in the single market and allow the effective targeting of EU policy priorities in a globalised environment (e.g. food security, social and territorial cohesion, cross-border environmental problems, climate change, water management, biodiversity, animal health and welfare, food and feed safety, plant health and public health as well as consumer interests) (Section 5). The Communication points out the constraints of limited budgetary resources and takes into account the severe impact of the economic crisis on agriculture.

The European Commission Communication on the budget review published on 19 October 2010 ⁽⁶⁰⁾ only partially compensates for the absence of explicit budgetary references in the CAP Communication of 18 November. This Budget Review Communication confirms that agriculture will represent a major public investment and one which will fall on the EU's shoulders, rather than on national budgets ⁽⁶¹⁾. However, it does not define either the EU spending priorities, the size of the budget, nor the share each policy will receive ⁽⁶²⁾. Presumably, all the budgetary elements will be put on the table before summer 2011 in the legislative proposal for a Regulation on the next Multiannual Financial Framework. The level

⁵⁹ The Communication mentions that Option 2 (§3) "*would imply greater spending efficiency and greater focus on the EU value added*" (Section 6.2).

⁶⁰ COM (2010) 700. 19.10.2010. See references - point 6-d. .

⁶¹ See Section 3.2 of the Communication - The Common Agriculture Policy (page 11).

⁶² The funding of agricultural policy currently amounts to about 40% of the EU budget.

of spending should reflect the EU's core policy priorities, as spelt out in the Lisbon Treaty and in the Europe 2020 Strategy ⁽⁶³⁾. This means that the budget should, above all, be designed to help deliver smart, sustainable and inclusive growth. It also means directing it towards collective challenges like energy or climate changes.

Given the strategic nature of the Communication presented by the Commission, it is hard to predict the budgetary concerns of the new CAP. Several issues, including the following, remain undetermined:

- The Communication remains silent about the **size of the overall agricultural budget**, to be agreed as part of the Financial Perspective negotiations.
- The Communication states that the CAP needs to evolve, especially concerning the historic basis of SPS and advocates an "*equitable and balanced support*" between Member States and farmers. However, it explicitly rules out a single EU flat rate (Section 3.3), which leaves the nature of the future **aid distribution** unclear.
- The Communication gives no clues as to how the First Pillar budget will be allocated across Member States. As the future **national envelopes** will finance different aid components (§12), some of which would be voluntary ⁽⁶⁴⁾, the **criteria to be used** for the internal distribution of new aids scheme remains unclear, as does the flexibility afforded to Member States in terms of defining the allocations.
- The crucial question of the **priorities** inside the first pillar (including the weight or the specific amounts allocated to every aid component) also remains uncertain. In relation to the share of direct payments going to support incomes or environmental public goods, the final model for the new CAP could vary substantially. In fact, this choice would affect the Options or Scenarios outlined by the Commission (§3). If a large share of the national envelopes is allocated to the basic income support in the first pillar, Option 2 would become close to Option 1. Conversely, Option 2 could be converted to Option 3 if the share of resources devoted to the greening component increases.
- The Communication does not analyse in detail the **rural development expenditures**. Specifically, it does not mention the final list of tools to be included in the rural development strategic framework. It does not explain either which rural measures will be determined at an EU level, which will be left to the Member States, or, even, whether any will be integrated into broader cohesion programmes in the future.
- The **cofinancing** principle is confirmed within the second pillar. However, we do not know if cofinancing will be included inside the first pillar and, consequently, whether the cofinancing requirement will remain a distinguishing feature between the first and second pillars.
- Finally, the Communication lacks detail on the future of the **EAGF** and the **EAFRD**.

⁶³ COM(2010) 2020, 3.3.2010. See references - point 6-i.

⁶⁴ The Communication defines the coupled support component as voluntary (see Annex).

20. QUESTIONS ON THE BUDGETARY CONCERNS

- *How will the budget for the first pillar be allocated between Member States?*
- *To what extent would adjusting payment levels to take into account the diverging national cost structures act in contradiction to the principles of cohesion policy?*
- *How will the national envelopes of the first pillar be allocated between the different aid components proposed?*
- *How will the different Pillar 1 objectives of income support and delivery of public goods be prioritised, in financial terms?*
- *How has the Commission's thinking evolved with respect to the question of whether or not to cofinance the new Pillar 1 support for areas with specific natural constraints?*
- *Which current rural expenditures are justified at EU level and which others could be left to the Member States?*
- *Is it adequate to introduce rural cohesion programmes into the Regional Policy to complement the EAFRD measures?*

21. WTO CONCERNS

21.1. Proposals (Sections 3.1 and 6.1)

The Communication recognises that EU agriculture finds itself in a competitive environment as the world economy is increasingly integrated and the trading system is becoming more liberalised (Section 3.1). This trend is expected to continue in the coming years, in view of the possible conclusion of the Doha Round negotiations and of the bilateral and regional agreements currently under negotiation (Section 3.1). However, the Communication does not comment on the WTO framework within which the new CAP will reside and merely mentions the issue indirectly in relation to the optional risk management toolkit in the second pillar and the adaption of "*disturbance clauses*" on markets policy (Section 6.1).

21.2. EP Resolution of 8 July 2010

The EP Resolution mentions the WTO in passing in Paragraphs 3, 39 and 66. More specifically, it confirms that exports refunds should continue to be phased out in the EU, in parallel with similar measures being taken by WTO partners (Paragraph 83).

21.3. Observations

One of the main features of the new CAP will be to ensure the compatibility with the rules of the new WTO Agreement on Agriculture, to be adopted by the Doha Round. The decoupling of aid and the transfer of funding to rural development through modulation had the objective of allowing the vast majority of European agricultural domestic support to be classified as being WTO "*Green Box*" compatible.

Despite the failure of the 2008 negotiations of the Doha Development Agenda, technical discussions continue, based on the last package tabled concerning the modalities for the future commitments⁽⁶⁵⁾. This document concerns the following matters:

- The **Green Box** would be tightened (see below).
- The **Amber Box** (or AMS) would be reduced by 70% overall for the EU. Prices and support for individual products would be capped at the average Amber Box support recorded for the 1995/2000 period⁽⁶⁶⁾.
- The **Blue Box** would be expanded, but would be restricted to 2.5% of production for developed countries, with caps set for each product.
- The **de minimis clause** would remain capped at 2.5% of production for developed countries. The EU currently notifies low levels of *de minimis* (mostly some 600 million Euros of insurance subsidies). The new voluntary coupled support proposed for the first pillar could be accommodated within the new *de minimis provision*.

⁶⁵ See references: *Stocktake of the WTO Agricultural Negotiations after the failure of the 2008 talks*, Gide, Loyrette, Nouel. EP Study IP/B/AGRI/IC/2008-131, June 2009.

⁶⁶ It should be mentioned that price support, which constitutes the bulk of the new *Amber Box*, may be constrained to a certain level in future. The safety-net intervention model was adopted on the basis of a positive economic perspective, and could be kept at low levels if the current situation persists. However, the recent volatility of prices and/or significant crisis could require an increased use of intervention. The *Amber Box* that would result from the Doha Round would still allow for a reasonable level of intervention (private or public), but less than previous levels.

- **Trade-distorting domestic support** (Amber Box + Blue Box + *de minimis* provision) would be reduced by 75-85% for the EU over a period of five years. An immediate reduction of 33% would be applied in the case of the EU.
- **Tariffs** would be cut according to a formula prescribing steeper cuts on higher tariffs. For developed countries, the cuts would range from 50% for tariffs under 20% to 66-73% for tariffs higher than 75%, meaning an average minimum cut of 54%. The latest EU proposals on the modalities for commitments agree to an average tariff reduction of 60% to improve market access, which is undoubtedly the most sensitive area for EU agriculture.
- **Sensitive products** would be subject to smaller cuts, however, these reductions could be offset by preferential tariff quotas.
- The **Special Safeguard Clause** (SSC) would gradually be abolished, although the EU would prefer it to remain.
- **Exports subsidies** would be abolished by the end of 2013. EU proposals are strictly conditional on further clarification from other developed countries on the elimination of their forms of export support. US commitments on food aid and export credits are not yet sufficient. The EP Resolution of 8 July 2010 confirmed this approach (Point 83).

Unfortunately, the Communication does not analyse the impact of the proposed changes to current CAP instruments in relation to the WTO and their compatibility with the Doha Round framework, especially in relation to domestic support. It just mentions that the optional risk management toolkit, to be included in the second pillar, would be designed as a new WTO Green Box compatible income stabilisation tool (Section 6.1). Cautiously, it also includes the use of "*disturbance clauses*" (possibly analogous to safeguard clauses) as potential examples of adaptations to current markets policy (Section 6.1). Even when the Communication argues in favour of an agricultural policy designed at an EU-level (Section 5), it forgets to cite the WTO as a crucial factor requiring negotiation and implementation on a multilateral basis.

The Impact Assessment accompanying the draft legislative proposals ought to explain the multilateral framework relating to the new CAP, with particular attention given to domestic support, including how the proposals are interpreted within the context of **Annex 2 of the WTO Agreement on Agriculture** ⁽⁶⁷⁾, in order to be reassured that the classification of the majority of the new direct payments in the first pillar will be safely within the *Green Box* ⁽⁶⁸⁾.

In this context, it is interesting to note that the last **WTO draft on modalities** states the following concerning the *Green Box*:

- Transfers of decoupled payments between farmers or landowners are not forbidden. This would provide an express basis for the transfer of entitlements of the new direct payments;
- Payments shall be made on a "*fixed and unchanging historical base period*", but an exceptional update is not precluded, at certain conditions, provided in particular that

⁶⁷ 94/800/CE, Council Decision concerning the conclusion on behalf of the European Community, as regards matters within its competence, of the agreements reached in the Uruguay Round multilateral negotiations (1986-1994) (OJ L 336, 23.12.1994). See the Agreement on Agriculture in pages 22 to 39 of OJ 336.

⁶⁸ The Annex 2 of the Agreement on Agriculture defines the basis for exemption from the reduction commitments (compatible aid provisions or *Green Box*). See pages 31 to 35 of OJ 336.

"production decisions are unaffected" (⁶⁹). The possibility for modification could provide a legal basis for the EU and Member States to move to flatter rates, to change their decoupling model, or to use the funds from further decoupling to increase the value of existing payment entitlements. However, Member States would be constrained in making only "exceptional" updates and to make only one change of decoupling payments within a period of five years, as part of the new Agreement. As for Member States currently under the SAPS, the situation would be different since the SAPS has been notified in a different category to the current SPS.

In the past, most of the EU notifications to the WTO concerning **Green Box measures** (Annex 2 of Agreement on Agriculture) are based on the decoupled income support (Point 6 of Annex 2). Significantly, the **current Green Box** includes some further interesting possibilities for the new CAP (⁷⁰):

- Public stocks for food security purposes (Point 3 of Annex 2), domestic food aid (Point 4), financial participation in income insurance and income safety-net programmes (Point 7), structural adjustment assistance provided through investment aids (Point 11), environmental payments (point 12) (⁷¹) and regional payments (Point 13) are all explicitly classified as Green Box measures;
- Financial contributions to crops, animals and plants insurance schemes (already introduced by the "Health Check") are designed to comply with the criteria of the payments for relief from natural disasters (Point 8 of Annex 2). In particular, insurance schemes should be applicable only for losses of more than 30% of the average production in the preceding three years, and Member States should only grant a financial contribution up to 65% of the insurance premium, should not compensate for more than the producer's total loss, and should not include conditions relating to the type or quantity of future production.
- By contrast, it should be underlined that the second risk management instrument included by the Communication inside the risk management toolkit (Section 6.1), the contributions to mutual funds for animal and plant diseases and environmental incidents, is not expressly designed (⁷²) to be classified in the *Green Box*.

⁶⁹ A footnote specifies that "where a Member has, at the time of entry into force of this Agreement, more than one type of direct payments within the same system of decoupled income support, it shall be possible to decide, within a period of no more than **five years from the date of entry into force of this Agreement**, to move from one to another type of direct payments for all or part of the territory of that Member, including the use of a changed base period. The decision shall be taken once and for all for each part of the territory of the Member concerned" (See Footnote 1 in the decoupled payments Category).

⁷⁰ See pages 31 to 35 of OJ 336.

⁷¹ The WTO Green Box requires agri-environment payments to be based on income forgone or additional costs, which necessitates some administrative complexity (in calculating the appropriate rate) and limits their attractiveness to farmers in the absence of true incentives. The way the Commission intends designing the compulsory Pillar 1 greening component (which is described in the Annex of the Communication as being based on supplementary costs) is particularly relevant in this regard.

⁷² However, should these risk management schemes pertain to the new trade-distorting boxes, they could be accommodated within existing budgetary ceilings (see above).

21. QUESTIONS ON THE WTO CONCERNS

- *Will the Impact Assessment accompanying the legislative proposals explain the multilateral framework relating to the new CAP, in particular to the possible WTO compatibility of the new arrangements for domestic support?*
- *On what basis will the new direct payments of the first pillar be justified as being compatible with the WTO Green Box?*
- *Could environmental payments, as well as regional payments, included in the current Green Box, become the new basis for the new aids proposed for the first pillar?*

22. FOOD SAFETY CONCERNS

22.1. Proposals (Section 2, 3 and 5)

The proposal points out that the issue of food security is one of the greatest challenges that have characterised the overall process of reform of the CAP. The Communication stresses that this issue remains one of the main objectives of the future CAP.

22.2. EP Resolution 8 July 2010

The EP resolution included food safety in the set of public goods provided by the agricultural sector and underlines that it should continue to constitute the primary *raison d'être* for the CAP, corresponding to its essence and representing the first concern of Europe's citizens (Paragraph 6). In this context, the EP believes that agricultural policy must enable a healthier diet to be made available to all consumers, particularly the poorest among them, on the basis of a more varied, accessibly priced range of products and calls for an extension of the programmes to boost consumption of fruit and vegetables in schools (Paragraph 86).

22.3. Observations

The Communication refers to the concept of food safety as being central to the objectives of the future CAP. Compared with that aim, the proposal does not provide much detail of how this objective will be pursued. In particular, there is no reference to the current European School Fruit and Milk Schemes.

22. QUESTIONS ON FOOD SAFETY CONCERNS

- ***How in the future CAP will the food safety concerns be implemented?***
- ***Will the current European School Fruit and Milk Schemes be continued?***

23. DECISION -MAKING PROCESS FOR THE CAP REFORM

23.1. Proposals

The Communication remains silent concerning the decisional making process.

23.2. EP Resolution of 8 July 2010

The EP Resolution recalls the new parliamentary powers concerning CAP and the budget with the entry into force of the Lisbon Treaty (Recitals AA and AB).

23.3. Observations

The TFEU introduced the **ordinary legislative procedure in CAP** (co-decision) at two levels: a) *specific rules of competition* applicable to the production of and trade in agricultural products (first paragraph of Article 42 TFEU); and b) the *establishment of the common organisation of markets and the other provisions necessary for the pursuit of the objectives of the CAP* (Article 43(2) TFEU) ⁽⁷³⁾.

The ordinary legislative procedure therefore became the common law procedure in agricultural matters. However, there were two significant exceptions: a) within the special rules on competition, only the Council may authorise the granting of aid for the protection of enterprises handicapped by structural or natural conditions and within the framework of economic development programmes (second paragraph of Article 42 TFEU); b) only the Council can adopt measures on *fixing* prices, levies, aid and quantitative limitations (Article 43(3) TFEU).

The Court of Justice has always considered that exceptions to a rule or general principle should be interpreted strictly. This is the case here, as the ordinary legislative procedure becomes the common law procedure in the agricultural area. This interpretation is supported by the general reference to the "*objectives of the common agricultural policy*" (first paragraph of Article 42 TFEU), with the Court of Justice having always advocated a broad interpretation of the objectives in Article 39 TFEU (ex Article 33 TEC). Furthermore, the exceptions stipulated in Articles 42 and 43 TFEU do not make any reference to a special legislative procedure. It should therefore be concluded that acts adopted on these bases are no longer legislative, but executive.

On this basis, Parliament calls for a *strict interpretation* of the second paragraph of Article 42 and of Article 43(3) TFEU.

In this context, the different timings of the Multiannual Financial Framework and the CAP reform negotiations are likely to have some impacts on the decision-making process.

⁷³ See the Policy Department B Study: "*Structural and Cohesion Policies following the Treaty of Lisbon*", IP/B/COMM/NT/2010-01, PE 431.591, 15.2.2010 (especially chapter 3.2, page 22) (See references, point 8).

23. QUESTIONS ON THE DECISION-MAKING PROCESS ON THE CAP REFORM

- ***Will the legislative proposals to be presented by the Commission in summer 2011 fix the amounts of aids and prices?***

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