

TOWARDS A MORE INTEGRATED RURAL POLICY FOR EUROPE: THE NEXT REFORMS OF THE CAP

EXECUTIVE SUMMARY

The Role of Land Managers

1. The European Landowners Organisation (ELO) represents the interests of the private owners and managers of rural land in fourteen EU member states and maintains regular contacts with associations in Central and Eastern Europe. The role of land managers is critical for the viability of the rural economy and rural communities, in the stewardship of rural resources of soil, water and air and of the rich biodiversity and huge variety of landscapes found in rural Europe. The economic, social and environmental health of Europe's rural areas is affected by a wide range of national governmental measures. However, the single largest EU policy, the Common Agricultural Policy (CAP) also has a very important impact on the wellbeing of the rural world. This paper is the ELO's contribution to the debate launched by the European Commission leading up to the mid-term review of the Agenda 2000 reforms of the CAP which will be underway in 2002.

Internal EU pressures for CAP reform

2. It is clear to the ELO that the CAP is not well adapted to the demands of the 21st Century. The policy has not sufficiently adjusted from its mid-20th Century focus on productivity and security of supplies to reflect current concerns with food quality and environment. Whilst food production is, and will always be, the prime task of agriculture, European society demands a great deal more from its rural areas. This is encompassed by the concept of "multifunctional land management". This reflects that land managers contribute to society not only by producing food and fibre, but also by supplying environmental and cultural landscape services. Their social role is also of great importance.
3. ***The ELO therefore wishes to steer the CAP towards a more integrated rural policy which acknowledges and supports the food, forestry, energy, recreational, social, environmental and cultural landscape roles of land management in a more balanced way. This can be characterised as a switch in emphasis from producers to land managers. Such a switch is even more necessary following the damaging effects of the recent breakdowns in farm animal health. It is now a vital task for land managers and governments together to work to restore public confidence.***
4. These issues constitute the internal pressures for reform of the CAP. Alone they create a formidable task. Yet the challenge faced is considerably more complicated by two further considerations - Eastern Enlargement and multi-lateral trade negotiations under the WTO.

Eastern Enlargement

5. The ELO welcomes the Eastern Enlargement of the EU. Landowners see this political development as a further cementing of the fundamental principles of market democracies. In particular it represents an affirmation that the most effective way for society to deliver food and raw material, as well as to manage the countryside to deliver rural environmental services, is through a decentralised market-based process based on the private ownership and operation of land. Furthermore, the ELO expects that, after suitable transitional arrangements, the new member states will wish to enjoy, the same agricultural and rural policy as applies in the EU-15. To the extent that this entails additional budgetary cost, this must be borne fairly by all of European society and not disproportionately by any one sector alone. ***The political and economic benefits of enlargement, the freedom, peace, democracy and development will be enjoyed by all, so the costs of achieving it must be borne by all.***

The WTO

6. The ELO broadly supports the EU approach to the next round of multilateral trade negotiations under the WTO. We are particularly concerned with three issues.
 - First, **non-trade concerns**, it is vital that a satisfactory resolution is found to the threat that EU standards on health, safety, animal welfare and environment are undermined by imported produce not respecting these standards. There is no single resolution to this problem, an internationally acceptable combination of approaches based on harmonising standards, import controls, consumer information, and compensation must be developed.
 - Second, on **domestic supports**, a combination of appropriate re-definitions of the Blue and Green boxes, and changes to the basis of supporting EU land managers through targeted, transparent, minimally trade-distorting, payments for the creation and maintenance of environmental and cultural landscape services must be established as an enduring part of internationally acceptable rural policy. Also, trade liberalisation must not undermine animal welfare. To provide the necessary time to achieve these goals it will be necessary to renew the Peace Clause.
 - Third, and not yet established in the WTO agenda, it is necessary to find a more rational and predictable framework for provision of **safety nets** for agriculture. Farming is more exposed than most sectors to the uncontrollable forces of nature, especially disease, markets and climate. The latter is expected to involve a greater frequency of extreme events. The provision of such safety net mechanisms is overtly a major part of US farm policy and is implicitly part of the justification for EU Blue Box payments. It would be helpful if this issue is dealt with more overtly as part of any new round.

The broad directions of CAP reform

7. Given these domestic, enlargement and WTO pressures for reform and taking note of the general debates of the past six years, future reforms will involve the following elements.
 - i **Decoupling** of the main agricultural supports from current production.
 - ii Redirecting support towards paying for public environmental services, by **degressivity or cross compliance** or a combination.
 - iii **Redistribution** of income support by modulating by farm size.
 - iv **Simplification of the CAP**
 - v **Reductions in export subsidies.**
 - vi **Increasing import access**
 - vii **Stimulating rural development**
 - viii **Developing more secure safety net mechanisms.**

Action on all of these elements except the third, modulation, is accepted by the ELO. Furthermore, we believe that supply management will continue to have a declining role in the new integrated rural policy.

The ELO's preferred options for CAP reform.

8. To effect the necessary rebalancing of CAP objectives and instruments, the ELO advises first that, given the fragmented structure of agriculture and that land and nature management requires a sensitive approach, rapid, unannounced, changes in policy are undesirable. Second, if society has encouraged investment and particular business structures by one policy, then a change in policy justifies that those affected are compensated to help them adjust to the new system. Third, in the context of the European single market, a common approach and framework for rural policy is essential to restrict the possibility of unfair competition arising from national rural support measures.
9. Domestic and international legitimacy for the CAP requires further **decoupling of supports from agricultural production** at the same time that there is a **recoupling of supports to the provision of environmental and cultural landscape services**. The ELO considers that a very large part of existing support through the CAP can be justified as the necessary price society is willing to pay to land managers who sign up to maintain the countryside and provide the biodiversity, habitat protection and enhancement and cultural landscapes that our urbanised society demands.
10. This switch in the basis of payments could, in principle, be achieved by fund switching from Pillar 1, direct commodity payments to Pillar 2 schemes under the Rural Development Regulation (RDR) through degressivity or modulation, or by applying environmental conditions to the receipt of remaining direct payments (Cross Compliance (CC)). These approaches are not mutually exclusive.
11. However, the ELO believes that certain principles must be observed in applying these changes. First, the fund switching must be done on an agreed uniform basis across the EU. Second, the ELO prefers the approach in which society contracts land managers to supply environmental services through purpose-built schemes. The cross compliance route must be seen as a second-best, transitional arrangement, and then only to achieve compliance with basic resource protection.
12. The aim of these approaches is two-fold. The first is to persuade citizens - especially taxpayers - of the integrated nature of farming and nature and landscape management and that without support along these lines treasured landscape and habitats will be lost. The second is to engage the interest of the maximum number of land managers in the idea that enduring receipts from the public purse must, in future be justified by the delivery of desired public benefits.
13. **Redistribution of support** will, inevitably, be an outcome of the changes in emphasis brought about by the measures summarised above. This is accepted. However, it is reasonable that those whose income suffers from the withdrawal of payments are given a transition or adjustment period during which payments are gradually reduced. This enables them to adapt their business to the new policy. ***The ELO insists on the principle of competitive neutrality, it does not support explicit schemes to modulate or differentiate either the receipt of payments or the reduction of existing payments based on crude measures like farm size or receipts of particular payments.***
14. **Simplification** of the CAP is indeed highly desirable. The successive building of layer upon layer of complexity in the common market organisations and other aspects of the CAP since 1968 has imposed its own cost. Thus steps to simplify CAP regulations are generally to be welcomed. The divorce of the payments from current production is also a welcome and necessary step towards decoupled payments. However, simplification can never be a prime objective of legislation. It's place is as a secondary consideration concerning the cost effective and

proportionate administration of regulations justified in their own right to achieve given, stated, purposes. There are dangers when simplification is welded to superficially attractive ideas, like helping the 'small' farmer, that the result is indeed simple but difficult to justify.

15. Given that European agriculture has an important role in international markets, the ELO supports the EU participation in international negotiations to **reduce export subsidisation and increase import access**. Such support is, of course, subject to the qualifications that they are part of a balanced multilateral trade liberalisation, and provided that the non-trade concerns are adequately addressed.
16. **Stimulating rural development** is an extremely important part of the new rural policy. It is a vital element to underpin the economic viability of rural communities. Rural development actions, of course, include those to stimulate *agricultural* development particularly by promoting greater value-added by raising quality and by assisting primary producers to get a larger share of consumer food expenditure by more effective marketing. Rural development outside agriculture is also vitally important for the viability of the land-based rural economy. In the long run, it does not help farmers to insist that the Common Agricultural Policy - which really should be renamed a Common Agricultural and Rural Policy - is restricted only to agricultural measures.
17. **Developing more secure safety net mechanisms**. The CAP reforms since 1992 have exposed EU agriculture to greater market price volatility. Simultaneously, there has been an increased frequency of incidents of other uncontrolled events - principally animal disease, and global climate change is bringing more frequent extreme weather events (notably floods). Whilst the first responsibility to deal with risk management lies with individual land managers themselves, there are grounds which justify a significant role for the collective action. A stabilisation function has been an acknowledged part of the CAP since its inception, and this role is also a dominant feature of current US farm policy. The ELO urges the Commission to give more explicit attention to this issue in discussions of further reforms of the CAP.

In summary

18. ***The ELO sees the current debate on the future for the European food system and the principal policy which drives it as a tremendous opportunity for land managers. European citizens want and are prepared to pay for high quality food produced in a high quality rural environment which sustains a vibrant rural economy. The CAP is in danger of becoming an instrument impeding the delivery of this vision. Yet with appropriate rebalancing of the priority given to the objectives of the CAP and a corresponding rebalancing the resources devoted to the available instruments, a better integrated European rural policy could make a major contribution to delivering this vision.***

TOWARDS A MORE INTEGRATED RURAL POLICY FOR EUROPE: THE NEXT REFORMS OF THE CAP

The Role of Land Managers

1. The European Landowners Organisation (ELO) represents the interests of the private owners and managers of rural land in fourteen EU member states. Since the collapse of the centrally planned economic systems in Central and Eastern Europe the ELO is actively developing contacts with and encouraging landowners' organisations in that region. The very concept of secure, private property rights in land is a foundation of our market economy. It is important that there are active organisations representing the interests of land managers and rural businesses throughout the enlarged Union.
2. The role of land managers is critical for the viability of the rural economy and rural communities, in the stewardship of rural resources of soil, water and air and of the rich biodiversity and huge variety of landscapes found in rural Europe. A wide range of national governmental measures affects the economic, social and environmental health of Europe's rural areas. However, the single largest EU policy, the Common Agricultural Policy (CAP) also has a very important impact on the wellbeing of the rural world. This paper is the ELO's contribution to the debate launched by the European Commission leading up to the mid-term review of the Agenda 2000 reforms of the CAP which will be underway in 2002.
3. The CAP is notoriously complex, and the language, jargon and acronyms surrounding it can be an obstacle to understanding. The endnotes to this paper provide non-technical definitions of some of the most common and confusing of these terms.

Internal EU pressures for CAP reform

4. It is clear to the ELO that the CAP is not well adapted to the demands of the 21st Century. The policy has not sufficiently adjusted from its mid-20th Century focus on productivity and security of supplies to reflect current concerns with food quality and environment. Whilst food production is, and will always be, the prime task of agriculture, European society demands a great deal more from its rural areas. This is encompassed by the concept of "multifunctional land management". This reflects that land managers contribute to society not only by producing food and fibre, but also by supplying environmental and cultural landscape services. Their social role is also of great importance.
5. Despite the Agenda 2000 reforms, Europe still has, in the CAP, an agricultural policy and not a rural policy. The CAP, as currently operated, still encourages farmers to produce commodity products in quantities unrelated to market conditions. For some commodities, it still pays insufficient attention to quality and consumer demands. In doing so the policy is thought to encourage over-intensification and to pay insufficient regard to food safety. It pays far too little attention to the non-market

services offered by land managers. It devotes too little of its resources towards creating the infrastructure to enable greater value-added from farm produce. It has not yet addressed the contribution land managers can make to mitigating global climate change through carbon sequestration in soil and forests, although it is now assisting the development of bio-energy crops. It does not extend its reach far enough into the wider rural economy recognising that the majority of European families engaged in farming must be pluriactive to survive.

6. ***The ELO therefore wishes to steer the CAP towards a more integrated rural policy which acknowledges and supports the food, forestry, energy, recreational, social, environmental and cultural landscape roles of land management in a more balanced way. This can be characterised as a switch in emphasis from producers to land managers.***
7. A classic illustration of the scale of the inter-dependency between agriculture and the massively important rural tourism and recreation industries has been shown by the 2001 Foot and Mouth Disease outbreak in the United Kingdom¹. There can be little doubt that this was an important factor in the change in the structure of the UK government department². Another animal disease, BSE, and food scares such as the Belgian dioxin incident have been responsible for raising CAP reform in the list of EU priorities. As soon as it became clear in autumn 2000 that BSE was a problem for the whole of European agriculture, this triggered an intense EU-wide debate about food safety, food production systems, and the main policy which influences it, the CAP. The pressures for a new look at agriculture and agricultural policy have been most intense in Britain and in Germany. In the latter they were manifest in a change in German Agriculture Minister and the Ministry under her charge³. The public costs of dealing with the BSE and FMD crises have added further pressure to review and revise the CAP.
8. These crises of livestock disease have widened an already existing gulf of misunderstanding between town and country, between, on the one hand, food consumers, citizens and taxpayers, and on the other, farmers and other land-based businesses. ***It is now a vital task for land managers and governments together to work to restore public confidence.*** To help achieve this task and resolve the conflicts between urban and rural interests it is important to understand how European society has reached the state of affairs when a larger number of people are better fed than at any time in human history, and yet there is a deep unease about our food.

¹ The interdependency between farming and the rural economy has been graphically illustrated by the case of Foot and Mouth Disease in the UK. Whilst affected UK livestock farmers have had their businesses destroyed by the disease and the measures necessary to control it, the damage has spread far and wide beyond farms. Livestock markets, auctioneers, rural haulage businesses, small abattoirs, specialist independent local butchers, feed and other input suppliers, farm advisers, accountants, secretaries and vets have all seen their revenues disappear. But the impacts extend much further than this. In order to control the spread of the disease, the Government advised local authorities to close all public rights of way in livestock areas. The effect on the rural tourism industry has been dramatic. Everything from restaurants, hotels, pubs, bed and breakfasts, holiday cottages and cafés to rural sport venues, fishing lakes and historic houses found a dramatic drop in their business. A large part of the pleasure of being in the countryside is being able to walk amongst the farms – particularly the livestock farms. No clearer demonstration of the multi-functionality of agriculture could be devised. Rural tourism needs farming – it supplies the landscape, the greenery, the quiet walks and the farm animals. But, because one of the most common ways to diversify a farm in a livestock area is to open a bed and breakfast or holiday cottage, agriculture needs tourism

² From Ministry of Agriculture Fisheries and Food (MAFF), to Department for Environment, Food and Rural Affairs (DEFRA).

³ From the Ministry of Agriculture and Forestry to the Ministry of Consumer Protection, Food and Agriculture.

9. This paradox has emerged from the following sequence of events. Economic development is the very process of people moving out of low productivity farming into higher productivity manufacturing and then services. This process starts from efficiency improvements in farming itself allowing some people to move off the land and yet enabling the non-farm work force to be fed. Later, successive waves of technical progress enabled much higher productivity to be achieved. This occurred through the application of the mechanical, chemical, managerial and now biotechnological developments, each of which releases yet more rural labour. The sequence of capital substituting for labour and land has gone furthest in Europe, N America and Japan where less than three percent of the work force provide the majority of the nation's food – and in many countries significant exports too. The whole food production system becomes more capital intensive and more integrated with the upstream and downstream sectors. This takes it further and further from the traditional practices of the past. The bulk of the population become divorced from food production. In the early stages of this development process people are glad to earn enough to feed their families. With economic progress people achieve higher real incomes and reduced working hours. These better-fed citizens eventually find that they have the time, mobility, information and inclination to enquire about how their food is produced. They are then surprised to find how much has changed.
10. The appliance of modern science, technology and management has truly revolutionised food production. For most food products there is a long and sophisticated chain from the supply of the seeds, feeds, crop protection and animal health products, machinery, informatics, financial and managerial inputs, through the restructured farming industry itself, to the multi-stage processing, packaging and distribution sectors. When this system works, as it does the vast majority of the time, it confers enormous benefits in the dependability, range and quality of food. The overwhelmingly non-farm population enjoys much higher material standards of living and are far happier with their urban lifestyle than with the drudgery of their peasant farming forebears. But, all is not well for at least two reasons.

Environment

11. First, and unavoidably, this path of economic development has a massive impact on the environment. The very creation of an urbanised and suburbanised society with extensive road, rail, cable and air communications swallows up farmland and natural habitats on a huge scale. At the same time, without the appropriate correctives and incentives, in some parts of Europe changes in the structure and technology of farming itself causes landscape change, losses of habitat and biodiversity, and pollution. As economic development has occurred these environmental impacts grow in magnitude. The population has the time and information to become aware of them. Society decides to give them greater priority and develops the institutions (governmental and non-governmental) to deal with them. Thus in the last two decades attention has increasingly turned away from the sheer need to produce food, towards ways of producing it with least harmful effects on the environment and delivering the kind of countryside society wishes as well. These environmental concerns manifest themselves and create pressure for action at local, national and international level. By the end of the 20th Century it was generally acknowledged that economic development was having a detectable, harmful effect on global climate. Whilst the majority of this impact arises from non-agricultural activity, feeding the expanded population contributes to greenhouse gases particularly from livestock and paddy rice production. ***Equally it is recognised that appropriate land management, especially forestry, has potentially - given the right signals and incentives – a very important role in mitigating climate change.***

Food safety

12. Second, inevitably, in the modern, complex food chain there are errors, misjudgements and even, occasionally, malpractice. The consequence of such faults is that some food item is sub-standard, causing illness and even death. The result is, not unnaturally, an extremely anxious public. People realise they have become out of touch with how their food is produced and what is in it. When the system goes wrong and people's trust in their food is dented, it is a basic human instinct to become alarmed. The development of instantaneous, 24-hour news media feeds on, and exaggerates such fears. The public then looks to *their* authorities and politicians to guarantee food safety. They then discover that their government has signed up to international agreements with what appear to be remote bodies like the European Commission, Codex Alimentarius, FAO, the WHO and the WTO. Governments explain that they are not completely free to take actions to restrict the imports of particular products, from specific places or produced in certain ways. International agreements have been signed requiring that such matters will follow certain procedures, and agreed criteria of risk assessment.
13. These environmental¹ and food safety concerns have created a powerful political challenge. Finding resolutions to these challenges is the task of both rural and urban interests. Land managers must become better informed about the desires of their fellow citizens for safe, wholesome, nutritious and tasty food, their rights to be concerned about the quality of soil, water and air, their interests in rural environment, biodiversity and landscape, and their wishes to enjoy country sports and recreation. Equally, urbanites must be helped to understand that it is no easy task delivering this complex set of demands from a limited land resource and that it must be done in such a way that allows those engaged to achieve reasonable living standards themselves.
14. ***The ELO considers that the better integration of agriculture and the natural environment and improved food safety are two of the principal internal challenges facing European agriculture. Their resolution will first require changes in attitude, more information, discussion and debate amongst all interest groups. They are not capable of being resolved quickly by any single set of reforms to the Common Agricultural Policy. However, as the CAP provides the principal framework for regulations affecting food production and rural land management, its reform to encourage a better balance between the food production and environmental management of the countryside is a vitally important element of the action which must be taken at EU level.***
15. The issues discussed so far constitute the internal pressures for reform of the CAP. These pressures alone create a formidable task. Yet the challenge faced is considerably more complicated by two further considerations - Eastern Enlargement and multi-lateral trade negotiations under the WTO.

Eastern Enlargement

16. The decision that the EU should embrace new member states from the former centrally planned economies in Central and Eastern Europe was taken at the 1993 Copenhagen summit. These countries are both poorer and more agricultural than the EU average. Their agricultural sectors experienced a severe shock – and in many cases contraction – when the liberalising and privatising reforms were introduced in the early 1990s. Land reform and farm restructuring is still in progress. Considerable investment and restructuring is taking place in the supply and food processing sectors, much of it with the assistance of inward private investment from EU companies, some of it with financial assistance from the EU itself through the PHARE and Sapard programmes. Trade between the applicant states and the EU has developed under the Europe Agreements. Initial fears in the

EU-15 that Western Europe would be flooded by cheaper imports from the East have been shown to be misplaced. Indeed the agricultural and food trade balance has swung significantly in favour of the EU. The most difficult challenges of enlargement are for the applicant countries themselves to resolve. They include the following elements. The consolidation of efficient farm structures within a system of clear property rights of rightful land owners and the development of land rental and purchase markets. The continued development of technical and managerial skills of the rural work force. Further investment in the food chain to improve the consistency and quality of produce. In many of these countries, enormous development of rural employment opportunities is required to absorb the expected further outflow of labour from agriculture. There are also significant environmental concerns both to clean up the mistakes of the past, but also to avoid creating new environmental problems associated with over-stimulated EU agriculture. In addition, there are significant agricultural policy challenges which will have to be overcome during the final period of accession negotiations. Principal among these are the application of supply management measures (milk, sugar and livestock quotas), the appropriate deployment of direct (arable and livestock) payments and the utilisation of the second pillar, Rural Development Regulation in the CEECs.

17. The ELO welcomes the Eastern Enlargement of the EU. Landowners see this political development as a further cementing of the fundamental principles of market democracies. In particular it represents an affirmation that the most effective way for society to deliver food and raw material, as well as to manage the countryside to deliver rural environmental services, is through a decentralised market-based process based on the private ownership and operation of land. Furthermore, the ELO expects that, after suitable transitional arrangements, the new member states will wish to enjoy, the same agricultural and rural policy as applies in the EU-15. To the extent that this entails additional budgetary cost, this must be borne fairly by all of European society and not disproportionately by any one sector alone. The political and economic benefits of enlargement, the freedom, peace, democracy and development will be enjoyed by all, so the costs of achieving it must be borne by all.

A new WTO Round

18. The expected new Round of multi-lateral trade negotiations under the WTO will provide an opportunity for the EU to achieve what it wants from the international rules and disciplines governing international trade. In particular, for agriculture, the EU will be emphasising the multifunctional role of agriculture and its citizens' desires to protect high standards of food safety, environmental protection and animal welfare. The EU negotiating position therefore calls for the so-called Non-Trade Concerns, which deal with these issues, to be a core part of any new Round. As the world's second largest agricultural exporter, the EU is also interested in increasing access to currently highly protected markets and fair, across-the-board, reductions in use of export subsidies and trade distorting domestic supports. Negotiations on these issues are already mandated by Article 20 of the Uruguay Round Agreement on Agriculture. The EU has tabled its proposals for dealing with these issues as follows. To improve import access the Uruguay Round approach of negotiating average and minimum tariff cuts should be used. The EU is willing to discuss further reductions in the use of export subsidies provided that this applies equally to all forms of subsidies including export credits, activities of state trading companies and food aid. On domestic supports, the EU seeks a continuation of the Blue Box category of supports, and ways of ensuring the continuation of appropriate, targeted, least trade-distorting, payments to producers for delivering the multi-functional benefits of agriculture.

19. **The ELO broadly supports these EU proposals. We are particularly concerned with three issues.**

- **First that a satisfactory resolution is found to the threat that EU standards on safety, health, animal welfare and environment are undermined by imported produce not respecting these standards. There is no single resolution to this problem, an internationally acceptable combination of approaches based on harmonising standards, import controls, consumer information including production and processing methods, and compensation must be developed.**
- **Second, a combination of appropriate re-definitions of the Blue and Green boxes, and changes to the basis of supporting EU land managers through targeted, transparent, minimally trade-distorting, payments for the creation and maintenance of environmental and cultural landscape services must be established as an enduring part of internationally acceptable rural policy. Also, trade liberalisation must not undermine animal welfare. To provide the necessary time to achieve these goals it will be necessary to renew the Peace Clause.**
- **Third, and not yet established in the WTO agenda, it is necessary to find a more rational and predictable framework for provision of safety nets for agriculture. Farming is more exposed than most sectors to the uncontrollable forces of nature, especially plant and animal disease, markets and climate. The latter is expected to involve a greater frequency of extreme events. The provision of such safety net mechanisms is overtly a major part of US farm policy and is implicitly part of the justification for EU Blue Box payments. It would be helpful if this issue is dealt with more overtly as part of any new round.**

20. In the light of these domestic, enlargement and trade pressures for further development of the CAP, the rest of this document suggests the main direction and some of the principal elements of such reform as seen by the European Landowners Organisation.

Aims and broad directions of further reform

21. Formally, the Agenda 2000, agreed at the Berlin Councils in March 1999, has determined the evolution of the CAP until 2006. There is disagreement about whether it is desirable or possible to delay further reforms until the end of this period. It was part of the Berlin agreement that mid term reviews would be conducted over the period 2002 – 2003, of the commodity regimes for sheepmeat, cereals and oilseeds, sugar, beef and dairy, and also the operation of the Rural Development Regulation in 2004.

22. In the meantime, domestic, food safety, environmental and budgetary pressures have increased sharply. The timetable for enlargement has also become clearer. It culminates in the difficult decision by the end of 2002 on whether farmers in the CEECs will have access to CAP direct payments. In the light of these new developments the Commissioner for Agriculture and Rural Development has signalled that he intends to draw together these mid-term reviews during a 'year of analysis' in 2001. This is to be followed during 2002 with a set of proposed "suitable adjustments" to the CAP.

23. How far reaching this review process will be remains to be seen. There are a number of considerations which suggest that 2002 is too soon for the EU to decide significant further CAP reform. It is unlikely that the French will be ready to engage in such discussions before their Presidential election is over in May 2002. It is also unclear what timetable the WTO talks will follow. The US 1995 FAIR Act has to be

renewed in 2002, and preparations for a new US Farm Bill have barely started. The Bush administration has yet to signal its priorities for trade policy.

24. The Commissioner's term of office expires in 2005. This is another factor encouraging him to push ahead with a thorough review of the CAP and how it must adapt. The Commissioner's speeches during the early part of 2001 offered hints of some quite strong reform proposals. The following quotations come from his speech at Grüne Woche in Berlin (18/01/01). He suggested that "rational, sustainable agriculture can only exist in harmony with nature". He reflected that the reforms of 1992 and 1999 (towards direct payments from commodity market support) have freed "substantial resources for income support, and for encouraging farmers in their role of protecting the countryside". He suggested that more resources could be deployed to do this if Member States "limit the agricultural aid paid to big farms". A result of (further) reform should be "more funds for rural development: as at present they amount to only 10% of the total". Recognising that already half of EU farmers work on a part-time basis, he urges more efforts to find other sources of employment and income for these farmers and their families. However, by spring 2001, expectations of early reforms were being damped.
25. Given the context summarised above - domestic, enlargement and WTO pressures for reform - plus these indications of the challenges the Commissioner sees for the CAP, and taking note of the general debates of the past six years, future reforms seem likely to involve the following elements⁴.
- i Further **decoupling**² of the main agricultural supports from current production. This might be done by switching more livestock support from headage to area basis (as has been done for Less Favoured Area payments).
 - ii Redirecting support towards paying for public environmental services, by **degressivity**³ or **cross compliance**⁴ or a combination.
 - iii **Redistribution** of income support by modulating⁵, or differentiating, according to farm size.
 - iv **Simplification**⁶ of the CAP 'by significantly reducing the administration required to provide a basic level of payments to the smallest farmers.
 - v Further **reductions in export subsidies**.
 - vi **Increasing import access** - especially for LDC exports.
 - vii **Stimulating rural development** by:
 - promoting higher quality, more value-added, more local and regionally denominated food, and organic production.
 - encouraging more co-operation amongst farmers to market their produce.
 - stimulating new employment and income opportunities in rural areas.
 - viii **Developing more secure safety net**⁷ mechanisms to deal with international commodity and currency market volatility and to help farmers better cope with climatic and biological extreme events. Options range from stimulating and assisting purely private risk management, disaster relief, revenue assurance schemes, to Counter Cyclical Assistance.

Some of these elements are favoured by the ELO. Others are strongly opposed. The positions will be explained for each of these policy elements in turn.

26. It is important to note that certain policy instruments, notably **supply management** instruments such as production quotas and set aside, are not mentioned further in this paper. The ELO sees these as part of the "old" CAP of commodity market support regimes necessitating strong border controls. The CAP reforms of 1992

⁴ The following section contains many items of CAP terminology (decoupling, modulation, degressivity etc.) which are not in common use. The endnotes to this paper provide an explanation of these terms.

and 1999 rejected this approach. It made no sense then for a net exporting region to arrange its domestic prices to be systematically above those of its main competitors. Supply management constrains the most efficient farmers and farming structures. It is judged that there is no reason now to go back to this approach. ***The ELO believes that supply management will continue to have a declining role in the new integrated rural policy.***

The ELO's preferred options for CAP reform.

27. The process of reform is essentially one of renewing the legitimacy of the CAP by recognising a new balance of objectives for the CAP. Consequently, the balance of use of instruments must also change. Key policy choices concern the pace at which this can be done, the nature and extent of compensation offered to those who lose from the policy change, and the degree of EU versus member state financing of support.
28. ***On these issues, the ELO advises first that, given the fragmented structure of agriculture and that land and nature management requires a sensitive approach, rapid, unannounced, changes in policy are undesirable. Second, if society has encouraged investment and particular business structures by one policy, then a change in policy justifies that those affected are compensated to help them adjust to the new system. Third, in the context of the European single market, a common approach and framework for rural policy is essential to restrict the possibility of unfair competition arising from national rural support measures.***
29. There is a broad consensus which the ELO has supported since 1998 that the direction of the change in instruments primarily involves a two-stage shift. First from commodity-based, market support instruments (intervention, supply controls, import restrictions and export subsidies) to direct compensatory payments. Second, recognising that 'compensation' *per se* cannot last for ever, and must be seen as a transitional form of support, the direct payments will either erode and eventually disappear or, as the ELO proposes, they will be transformed into contractual arrangements between the state and land managers to overcome the market failures associated with environmental services and measures to assist rural development. These can, in principle, be justified on an enduring basis.
30. The ELO's position on each of the eight potential elements of reform identified above is as follows.
31. **Further decoupling of supports from agricultural production.** This is accepted as a necessary part of legitimising public support to land managers and thereby regularising the position of agriculture within rules and disciplines for international trade. However, such acceptance is importantly qualified by the observation that because food production and the supply of environmental and cultural landscape services are inextricably linked, perfect decoupling is not possible.
32. **Further recoupling of supports to the provision of environmental and cultural landscape services.** The ELO considers that a very large part of existing support through the CAP can be justified as the necessary price society is willing to pay to land managers who sign up to maintain the countryside and provide the biodiversity, habitat protection and enhancement and cultural landscapes that our urbanised society demands. The challenge is therefore to bring about a switch in the basis of support from production-linked compensation, to systems of contractual payments to supply environmental and cultural landscape services. This switch must be managed in such a way as to allow the beneficiaries of the present system sufficient time to adjust.

33. This switch in the basis of payments could, in principle, be achieved by fund switching from Pillar 1, direct commodity payments to Pillar 2 schemes under the Rural Development Regulation (RDR) through degressivity or modulation, or by applying environmental conditions to the receipt of remaining direct payments (Cross Compliance (CC)). These approaches are not mutually exclusive. Indeed, as the extent of any fund switching from Pillar 1 to 2, however it is achieved, is likely to be an incremental process over many years, it will be necessary to employ some kind of cross compliance on the remaining direct payments if their legitimacy is to be retained. The ELO believes that certain principles must be observed in applying these changes.
34. First, the fund switching must be done on an agreed EU basis. The Agenda 2000 Horizontal regulation (1259/99) provided a mechanism for *individual* Member States to switch up to 20% of direct supports from direct payments to the RDR. This could be done either as a positive act through so-called modulation (see iii below) or, rather negatively, as a result of the non-compliance with basic environmental requirements. However these mechanisms have not yet proved to be attractive to Member States. Most member states have been unwilling to risk making their own arable and livestock production less competitive by reducing payments to their producers by more than a marginal amount. Only the UK (4.5% by 2005 and France with a target of 6%) have made use of this mechanism. Portugal is about implementing a scheme, and Germany is preparing one to revise its Rural Development Plans. Future steps in such fund switching must be done on an agreed uniform basis across the EU.
35. Second, the ELO prefers the approach in which society contracts land managers to supply environmental services through purpose-built schemes. The cross compliance route must be seen as a second-best, transitional arrangement, and then only to achieve compliance with very basic resource protection requirements.
36. Whether achieved through agri-environment schemes under the RDR or via environmental conditions being applied to the receipt of existing direct payments, an essential step in achieving a CAP better attuned to societal demands is the creation of a broad application land management or stewardship programme. In principle such a programme can and should be drawn up for each main farming system and should comprise a set of easily understood rules for that system which has the potential to deliver a measurable improvement in biodiversity, habitat creation and protection and landscape value. Such schemes should, in principle be capable of being applied across the whole farmed territory. It is for the stakeholders in each EU region to define these systems the eligibility criteria and how they fit as the broad, base-level tier of agri-environment schemes. The relationship between such a basic environmental land management scheme and systems of organic farming and integrated pest management will also have to be addressed.
37. The kind of criteria to be considered will depend on the route chosen for the policy redirection. A cross compliance route is bound to involve less demanding conditions. One approach would be to use it to achieve a step-up in environmental awareness. This could be done, for example, by requiring all land managers who receive direct payments to show they have an environmental audit. This would embrace nutrient accounting, full records of all inputs and outputs on their farm and inventories of natural features within their management. Another approach is to define the conditions in terms of good management practice only. On the other hand, a base tier of agri-environment scheme is likely to include criteria on livestock stocking rates, fertilisation, dates for certain cultivations, field margin management, other wildlife strips, and woodland and water management. Such schemes will be voluntary to the individual land manager. As far as possible, payments should be made on the simplest, per hectare basis.
38. The aim of these approaches is two-fold. The first is to persuade citizens - especially taxpayers - of the integrated nature of farming and landscape

management and that without support along these lines treasured landscape and habitats will be lost. The second is to engage the interest of the maximum number of land managers in the idea that enduring receipts from the public purse must, in future be justified by the delivery of desired public benefits. There is a risk that the slow, incremental build-up of more precisely engineered agri-environment schemes applying only to a small fraction of the farmed landscape and, most importantly accounting for only a small fraction of the public receipts of farmers, will not bring about the desired outcomes. The signal to provide environmental benefit will continue to be dominated by the stronger production signal of the much larger crop and livestock direct payments. This will perpetuate the current situation in which production signals are too strong – risking environmental damage - and environmental signals are too weak – resulting in under-delivery of environmental services. From an international perspective, it is also essential to be able to show that serious efforts are being made to switch a significant part of farmer supports to less trade-distorting environmental land management payments.

39. **Redistribution of support** will, inevitably, be an outcome of the changes in emphasis brought about by the measures summarised in steps (i) and (ii). As mentioned above, it is reasonable that those whose income suffers from the withdrawal of payments are given a transition or adjustment period during which payments are gradually reduced. This enables them to adapt their business to the new policy. ***The ELO insists on the principle of competitive neutrality, it does not support explicit schemes to modulate or differentiate either the receipt of payments or the reduction of existing payments based on crude measures like farm size or receipts of particular payments.*** Such modulation is often proposed as a social engineering measure in the misguided view that it will help the 'small' farms who are, erroneously, assumed always to be more deserving and kinder to the environment. It is presumed that crude measures of farm size are a useful indicator of income or wealth status, in reality there is no necessary connection at all between size of farming operation and farm family income or well-being.
40. The ELO's principled objections to these redistribution goals achieved through modulation are as follows. First, the EU has no competence in social affairs concerning income tax or social benefits, this is for the Member States to decide. Second, the elements of modulation already encapsulated in the CAP, or under discussion, have no objectively justifiable basis. Measures based on the tonnage of grains produced, numbers of animals, area farmed or size of certain direct payments received, bear no necessary relationship to the income or wealth level of the individuals concerned. A high proportion of very small (measured by area, animals or even throughput) farmers in Europe have other sources of income in their household. In many cases the farming income may only be a minor part of the household total earnings. Therefore to base thresholds of supports on such indicators as an income redistribution measure has no validity. It will result in taking money away from 'larger' full time farming families to give it to higher-income families who have some part-time engagement in agriculture. Third, if payments are truly provided for the delivery of environmental services, then the larger providers of such services will, naturally, receive larger payments. Any scaling of these payments should relate only to possible size economies in the provision of the services.
41. **Simplification** of the CAP is indeed highly desirable. The successive building of layer upon layer of complexity in the common market organisations and other aspects of the CAP since 1968 has imposed its own cost. Thus steps to simplify CAP regulations are generally to be welcomed. The divorce of the payments from current production is also a welcome and necessary step towards decoupled payments. However, simplification can never be a prime objective of legislation. Its place is as a secondary consideration concerning the cost effective and proportionate administration of regulations justified in their own right to achieve

given, stated, purposes. There are dangers when simplification is welded to superficially attractive ideas, like helping the 'small' farmer, that the result is indeed simple but difficult to justify.

42. Applied at the scale agreed by the Council in June 2001 (that is, to the recipients of _1250 or less, covering about a third of recipients but only two percent of expenditure) simplification seems a pragmatic and sensible measure. However, if as seems likely, the threshold is progressively raised and these simplified payments extend across the enlarged Union, it will become increasingly difficult to explain what these payments are for.
43. **Reductions in export subsidisation and increases in import access** have been discussed in paragraphs 14 and 15 above under WTO. The ELO supports these changes subject to the qualifications that they are part of a balanced multilateral trade liberalisation, and provided that the non-trade concerns are adequately addressed.
44. **Stimulating rural development.** In the context of European agriculture this is a vital element to underpin the economic viability of rural communities. As summarised in paragraph 24, Rural Development actions, of course, include those to stimulate *agricultural* development but they must extend beyond this.
45. The principal headings for **agricultural development** are to promote greater value-added by raising quality and to assist farmers to get a higher share of consumer food expenditure by more effective marketing. Raising value-added may be achieved by a variety of means, examples are: the promotion of local and regionally denominated foods; traditional breeds and production methods; and organic production systems. Routes to improved marketing can be found by establishing better direct links to consumers directly through local or farmers' markets or through producer controlled organisations. The Rural Development Regulation provides mechanisms for assisting these developments. However their success requires at least two other conditions to be met. The first is the provision of the infrastructure – facilities for storage, transport, storage and processing, appropriate regulations and information flows necessary for the web of quality, locally-based activity to develop and thrive. The second is to stimulate the creation of networks of contact between producers, government institutions, community groups and NGOs. There is some scope for elements of the RDR to be used in the former and for the LEADER+ programme to be used in the latter. However, most of the responsibility for providing the enabling infra-structure for rural development will have to be provided by the Member States.
46. Rural development outside agriculture is also vitally important for the viability of the land-based rural economy. A large and rising proportion of 'farmers' are already part-time. As income expectations continue to rise with general economic growth, people with a limited area of land must find more of their income from rural activity beyond the farm gate. It is a sensible use of resources to deploy some Rural Development resources to encourage such development. As rural land management, is so interrelated with a large variety of tourism, leisure, and rurally based service activities, then the policy tools to unblock obstacles to rural development must also be integrated. In the long run, it does not help farmers to insist that the Common Agricultural Policy - which really should be renamed a Common Agricultural and Rural Policy - is restricted only to agricultural measures.
47. **Developing more secure safety net mechanisms.** This is interpreted as predominantly an agricultural producer concern. Of course, to the extent that such producers are increasingly diversifying their income sources through other rural activities, this provides some of the safety net. The founding article of the CAP included reference to the objective of ensuring stability and security of food supplies. This has generally been interpreted as the need to provide stabilisation mechanisms to help agriculture cope with the effects of uncontrollable weather and disease and the vagaries of international commodity and currency markets. Until

the 1992 and 1999 reforms the main method of providing some degree of stability has been through the use, at the border, of variable import levies and export refunds, and domestically by using market intervention tools such as intervention buying and withdrawal. Since those reforms the extent to which these instruments are available has significantly diminished. This has exposed EU agriculture to greater market price volatility. Simultaneously, there has been an increased frequency of incidents of other uncontrolled events - principally animal disease, and global climate change is bringing more frequent extreme weather events (notably floods).

48. The ELO believes that insufficient attention has been focussed on the appropriate mechanisms to manage these risks and uncertainties. There are undoubtedly many actions that individual land managers can and must take to protect themselves. However, the structure of the industry, the nature of the risks and the consequences for the public at large are such that there is a significant role for collective action. Stabilisation has been a central objective of the CAP since its inception, and until the Mac Sharry reforms has been achieved through commodity market regulation. This support is being reduced and farmers are now exposed to greater volatility. The recent failures of animal health, BSE, Swine Fever and Foot and Mouth disease have added to this volatility, and caused considerable amounts of unplanned public support expenditure. The idea that significant public funds may be deployed to help agriculture cope with severe instability in markets is not confined to Europe. In the last three years a very large part of US farm support has been devoted to providing safety nets through crop insurance and Counter Cyclical Assistance, to help farmers with world commodity market collapse and some more local events. The ELO urges the Commission to give more explicit attention to this issue in discussions of further reforms of the CAP. En passant, it should also be noted that given the interdependency of agricultural and environmental outputs the case for some degree of safety net or stabilisation measures can also be made from the perspective of environmental provision. Sensitive ecosystems may not survive the consequences of farming suffering deep swings from prosperity to bankruptcy.

In summary

- 49. The ELO sees the current debate on the future for the European food system and the principal policy which drives it as a tremendous opportunity for land managers. European citizens want and are prepared to pay for high quality food produced in a high quality rural environment which sustains a vibrant rural economy. The CAP is in danger of becoming an instrument impeding the delivery of this vision. Yet with appropriate rebalancing of the priority given to the objectives of the CAP and a corresponding rebalancing the resources devoted to the available instruments, a better integrated European rural policy could make a major contribution to delivering this vision.**

29th June 2001
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End notes on terminology

¹ The words **environment** and **environmental** carry quite different emphasis around Europe. Throughout this document it is used in its broadest sense to refer to all aspects of the natural environment: that is natural resources (soil, water, air), biodiversity and habitats (ie ecology), and landscape. When more restricted aspects of the environment are intended the descriptions indicate this. Environmental 'concerns' or 'bads' usually refer to the negative externalities of agricultural (or other human activity). These are resource depletion or damage, habitat or biodiversity loss, or landscape degradation. Environmental 'goods' or benefits are the beneficial effects of agriculture, or other land management, on natural resource status, on biodiversity and habitat preservation or on landscape quality.

² **Decoupling** refers to the link between any subsidy or support payment and the production, consumption and hence trade in agricultural commodities. The most coupled support instruments are direct price interventions (which raise domestic prices, encourage production, discourage consumption and thus reduce imports or increase exports) or supply management tools (which raise domestic prices by restricting output, discourage consumption and also distort trade). The least trade-distorting instruments would be direct payments to producers whose magnitude was based on an historical production level or land area, which did not change whatever the market circumstances, and which did not even require any particular production. In reality as the supports under discussion are directed to an occupationally defined group, farmers, then perfect decoupling is not possible. Decoupling is therefore a matter of degree.

³ **Degressivity** is the, rather ugly, word given to the idea of agreeing to change the structure of the EU budget for agriculture (FEOGA) by reducing funds in the Pillar 1, 100% EU funded, agricultural support part of the FEOGA and increasing the funds in the Pillar 2, co-financed, Rural Development part of FEOGA. Degressivity was discussed at the Berlin Council, though not proposed by the Commission and does not yet exist. It would be expected to involve agreeing a rate (x% per annum) of cuts in Pillar 1 direct payments (some or all), over an agreed period, with agreed possibilities of excepting certain producers from the payment cuts (eg through a 'franchise' in which the first 5000 of payments are exempt, or other forms of modulation -see below). The other important component of degressivity is the proportion of the funds taken from the direct payments which is channelled into the RDR. There can be no presumption that this is 100%. Degressivity as a change in budget structure would require European Council support.

⁴ **Cross Compliance** refers to the attachment of environmental, or ecological, conditions to the receipt of agricultural support payments. This is already a part of the CAP enshrined in Article 3 of the so-called horizontal regulation 1259/99 of the Agenda 2000 reforms. This article **requires** that member states take the environmental measures they consider appropriate for environmental protection. Such measures may be "support in return for agri-environmental commitments; general mandatory environmental requirements; or specific environmental requirements constituting a condition for direct payments". It is generally expected that such conditions should be equivalent to respecting codes of good agricultural practice. The regulation also requires Member States to have in place a system whereby the payments may be cut if such compliance is not respected. The funds thereby saved, are transferred to the RDR. Most discussions of cross compliance centres around the nature of the compliance conditions and whether their true function is to perpetuate agricultural payments or to achieve environmental amelioration whilst such payments survive.

Conceptually, Cross Compliance is a flawed instrument. It is an attempt to use one instrument to achieve two targets. This is generally an undesirable approach. (The first target is the original purpose of the direct payments – namely compensation for revenue lost. The second target is the delivery of environmental benefits.) As it has been introduced into a situation where there are already positive environmental programmes for delivering positive environmental benefits, it seems logical that the CC conditions refer to basic sustainability requirements for example to protect natural resources by reducing pollution and erosion. However it is unusual that businesses are paid to respect such conditions, usually it is expected that the Polluter Pays Principle should apply. Given these inconsistencies, the best explanation of why cross compliance may, nonetheless, have a useful role to play is that it is a transitional instrument.

⁵ **Modulation** means to vary the pitch (or voice or sound) or to differentiate. It appears in Article 4 of the Horizontal Regulation 1259/99. There it refers to the possibility (not requirement) that Member States, may choose to reduce some direct payments and redirect the money, (together with a corresponding sum from national treasury as the RDR is co-financed), to use for certain purposes under the Rural Development Regulation. These purposes are the three (1992 MacSharry Reform) accompanying measures – agri-environment, young farmers and afforestation, plus less favoured area payments. The word modulation was used for this transfer because it was clearly the intention of the authors that the cuts in direct payments would be modulated – ie applied at different rates to different producers. Indeed the regulation makes reference to the farm labour force, the overall prosperity of holdings and total support payments as criteria for modulation. The confusion has arisen because the UK, which is one of just four countries which are doing it or proposing to do it, with its high proportion of larger farms, opposes (true) modulation. The UK does not differentiate the cuts in direct payments, all payments are cut by the same percentage amount. The other three Member States all have different rates of cut according to various criteria of size and labour intensity of recipients.

A variant on this concept has now crept into the CAP lexicon, namely, **Compulsory Modulation (CM)**. This has, as yet, no legal status, but refers to the idea that all member states should be *required* to make some use of Article 4 modulation. The most important distinctions between this and digressivity is that under CM the fundamental budget structure is not affected, and all the money saved by the payments cuts is transferred into the RDR.

⁶ **Simplification** of the CAP refers to steps taken to reduce the amount of form-filling and sheer administration in implementing the agricultural support regimes of the CAP. This will bring benefits both to farmers and national administration systems. Since the Council agreed in June 2001 to introduce a simplification scheme for small producers the term is likely now to refer just to this, or comparable, schemes. The essence is that recipients will no longer have to provide annually, detailed information about their crop areas and livestock numbers to determine their payments. They will get a fixed sum for an agreed period of years irrespective of their current cropping and stocking. This simplification can therefore also be seen as a *decoupling* of payments and production. To the extent that farmers in the simplified scheme are subsequently exempt from future fund switching this may also turn out to be a way of *modulating* payments.

⁷ A **safety net** is a mechanism deployed to catch those who suffer a fall and to prevent fatal damage. Such mechanisms may be in place the whole time, but are only expected to be used under unusual or exceptional conditions. The mechanism usually involves some constant small payment to maintain the fabric of the net, the insurance premia, and then some much larger costs, payouts, when disaster strikes. The fundamental policy debate surrounds the share of these costs between the public purse and the private producers.