COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 20.5.2008
SEC(2008) 1886

COMMISSION STAFF WORKING DOCUMENT

accompanying the

Proposals for

COUNCIL REGULATION establishing common rules for direct support schemes under the common agricultural policy for farmers and establishing certain support schemes for farmers

COUNCIL REGULATION on modifications to the common agricultural policy by amending Regulations (EC) No 320/2006, (EC) No 1234/2007, (EC) No 3/2008 and (EC) No […]/2008

COUNCIL REGULATION amending Regulation (EC) No 1698/2005 on support for rural development by the European Agricultural Fund for Rural Development (EAFRD)

COUNCIL DECISION amending Decision 2006/144/EC on the Community strategic guidelines for rural development (programming period 2007 to 2013)

Impact Assessment summary

{COM(2008) 306 final}
{SEC(2008) 1885}

1. INTRODUCTION

The aim of the CAP "Health Check" is to assess the experience of the 2003 CAP reform, and to introduce adjustments that simplify and increase the effectiveness of the policy, allowing it to respond to present market opportunities and face new challenges.

First indications from the assessment of the 2003 reform are in general positive, and indicate that a fundamental reform of the CAP for the remaining horizon of the present financial perspectives (until 2013) is neither necessary nor desirable. However, other, parallel market and policy developments, together with experience gained so far from reform implementation, indicate a rapidly changing environment facing EU agriculture and the need for CAP adjustments which could not be foreseen when the 2003 reform was carried out.

The three main policy questions that the Health Check addresses concern the three basic Regulations of the CAP:

Regulation (EC) No 1782/2003 covers all issues related to the core of farm support today, the Single Payment Scheme (SPS),

Regulation (EC) No 1234/2007 covers issues related to the single common market organisation (sCMO),

Regulation (EC) No 1698/2005 covers issues related to Rural Development (RD) policy.

The Impact Assessment (IA) addresses the above issues, and analyses the impact of potential changes in the CAP, examining many existing studies, both internal and external.

Public consultation with stakeholders was organised, including two public seminars, one on the global presentation of the HC, the other on dairy issues. Stakeholders were invited to contribute to the preparation of proposals based on a questionnaire. This resulted in a significant number of submissions with wide-spread representation across Member States (MS) and stakeholders.

2. SINGLE PAYMENT SCHEME

The introduction of the SPS rendered decoupled farm support the central element of the 2003 CAP reform. In implementing the SPS, MS could opt for two basic models: a historic model or a regional model. The current legislation does not include a "regret clause" that would allow MS to adjust their SPS model.

Yet, as more sectors are included in the SPS, within on-going CAP reform, there are fewer a priori reasons to exclude such a possibility. To assess the potential impact from allowing MS to move towards a more flat rate, four alternative options were analysed.

A move towards an *EU-wide flat rate* per hectare was found to imply a fundamental reform and a major redistribution of support among MS. Turning the *SAPS*, the transitional area payment scheme in the new MS, into an EU-wide permanent scheme would contradict the very philosophy of decoupled support because it would not be a system based on fixed entitlements. The two options of assessing a targeted move towards a *flat rate* by harmonising payments in a regional context, either by entitlement or by hectare, was found to address equity issues related to the distribution of support while minimising the impact of significant shifts of support on land values.

Adjustment of Article 69 of the SPS legislation has also been shown to be desirable. Originally designed to facilitate transition towards decoupling, this article could also facilitate the adjustment needs resulting from the changes proposed in the HC. These challenges mainly concern risks that some regions may face with the gradual phasing-out of milk quotas and further decoupling, and the need for policies addressing risk management. Through this revision MS could be allowed to use part of their available SPS support to target particular sectors and regions with specific needs of an economic, social or environmental nature thus mitigating negative effects on income, contributing to the vitality of rural areas and to promoting environmentally beneficial farming practices.

In order to avoid the risk of backtracking from the overall orientation of the CAP towards decoupling needs to be addressed by dividing the resulting national envelopes into two distinct sub-ceilings. One envelope could address the adjustment of decoupled support towards higher flat rate payments in those regions where the expiry of the dairy quotas and further decoupling could create potential risks, or the introduction of risk management measures that meet Green Box criteria. The other sub-ceiling could be used for targeted measures of coupled support or other risk management measures.

As cross compliance creates a link between farm-relevant support and farm-relevant legislation, its scope was screened in order to examine whether the SMR and the GAEC could be better targeted, whether the issues of climate change and water management could be better taken into consideration, and whether environmental benefits from set-aside could be retained through cross compliance. Two options were considered. The first option identified those requirements whose removal would reduce the administrative burden, but not impact upon the current ambition of cross-compliance, such as those not directly linked to agricultural activities and agricultural land, whose non-respect cannot be attributed to an individual farmer, concern MS instead of the farmer's responsibility, and are thus difficult to control under cross compliance.

The second approach considered the broadening of the scope of cross compliance by adding certain important legal acts relevant to farming activities that would contribute to meeting new challenges and/or retaining environmental benefits from set aside. Ways of introducing water management within the scope of cross compliance have also been considered, such as including water management within the GAEC. For retaining environmental benefits from set aside, an additional standard on buffer strips and a strengthening of the current standard on retaining landscape features have been considered to be appropriate.

Partially coupled support is available for some sectors. The remaining coupled support should move to full decoupling to achieve more market orientation and improved competitiveness. In some cases, this may have consequences for the environmental benefits provided by current policy tools, as well as for the vitality of rural areas. The analysis concludes that the biggest impact would be in those sectors and regions where the coupled premiums represent an important share of the farmer's margin, such as the sectors of suckler cows and sheep. In the cereals sector and in other beef production systems, the impact would not be so significant.

On payment limitations, the situation is at present characterised by a small number of very high payments and a large number of very small payments. Introducing individual limits was assessed in order for its potential of improving the equality of distribution of payments between farmers. The analysis shows that such a measure would affect a very small number of holdings in a limited number of MS, particularly in EU-10, and would result in significant cuts in their direct payment levels and the risk of splitting of holdings to avoid the ceilings. Progressive individual limits, on the other hand, maintain the more generalised nature of the measure across the EU, but have significantly milder impacts on cuts in direct payments and income on the affected holdings.

An increase of lower payment limitations was assessed due to the merits this could have in easing the administrative burden for the MS. Depending on where the limit is set, the percentage of beneficiaries excluded from payments could vary greatly within MS. Leaving the choice of setting either a minimum area or a minimum amount to the MS would allow better adjustment to their specific needs.

3. GRASPING MARKET OPPORTUNITIES

The proposed options for adjustments to cereal intervention and set-aside were assessed with respect to their capacity to improve competitiveness and market orientation for the sector while keeping intervention as a safety-net in case of market disruptions, facilitate farmers' response to market conditions, and identify measures that could deliver similar environmental benefits to set-aside where its removal may put them at risk.

Limiting quantities going to intervention at zero for all feed grains facilitates supporting the entire cereal markets if necessary (since cereal prices move in parallel) without the disadvantage of artificially undermining barleys' competitiveness. Introducing tendering would simplify and harmonise cereal intervention rules with those of other CMOs.

Removal of the set-aside obligation would likely bring back into production an area corresponding to roughly half the area currently under mandatory set-aside. It has been suggested that the environmental benefits of set aside could be retained by introducing a fixed percentage of total area as an "environmental compensation/priority" area, containing certain landscape features. However, such a measure would attempt to fix in a similar manner MS a potential problem whose distribution is presently very diverse across MS, and would thus not necessarily compensate for environmental losses in the place that they occurred. If the fixed percentage of set-aside for all farmers is replaced with new standards to reflect the above landscape features, an expanded list in GAEC would ensure better coverage than at present of these features by MS. Furthermore, the strengthening of set-aside within Pillar II would allow the targeting of environmental benefits where they are mostly needed, but the impacts will depend on relevant provisions of existing RD programmes in different MS.

Milk quotas hold back the sector from achieving the objectives of CAP reform since they still reflect concerns of two decades back, instead of responding to present opportunities. The phasing-out of dairy quotas was assessed, and various policy options were compared with the continuation of the dairy quota as a reference. In the continuation option, constrained production combined with growing demand increases the milk price, but market orientation and competitiveness of producers and processors alike is being hampered.

On the other hand, under the expiry option, when quotas are lifted in 2015/16, production jumps to match demand, causing a strong price decrease after quotas expire. Price declines and production responses are smoother under both phasing out options, but the extent of adjustment differs. The lower annual quota increase option allows for a smoother price adjustment throughout the transition period, but in both phasing out scenarios, the butter price falls to intervention price level.

The transition to the phasing out of dairy quotas has social and environmental effects. A smooth transition in the phasing out scenarios prevents rapid restructuring and allows preparing and adjusting accompanying measures to the potential social and environmental problems that could appear.

Finally, for a list of small support schemes, the *status quo* option contradicts the 2003 CAP reform path in terms of competitiveness, market-orientation and simplification of the support scheme. Although full decoupling would have a positive impact on farm income in most regions due to higher transfer efficiency of direct support, nevertheless it could affect specific regions where local production is vital for the viability of the local agri-food chain or for the environment, thus indicating the need for a variable degree of transition for the industry, according to the sector.

Analysis has also been carried out on how to best take account of the farmers increasing need for risk management tools, due to increasing impacts of climate change and the higher degree of market orientation. Introduction of new risk management tools should contribute to stabilising the income of the farm society, while not introducing unnecessary administrative burden or excessively high budgetary costs.

Price risks appear to be sufficiently addressed with safety-net intervention and with the flexibility that decoupling provides; hence there is no need for additional risk management tools to deal with price risks. The extension of SPS to sectors which are currently not included could also provide a positive contribution in mitigating price variability for the agricultural community.

With respect to the potentially growing needs for production risks, an EU-wide scheme cannot be considered feasible at this stage. Such a scheme would be very expensive, and would imply an increased administrative burden for farmers and MS. Given the heterogeneity of the risks and crises that the EU faces heterogeneous measures seem to provide the most suitable solution to help farmers deal with crisis situations. A harmonisation at EU level of the aid schemes currently supported with state aids could contribute to increased transparency between MS, while at the same time allowing the CAP to better meet the objective of contributing to the income stability for the agricultural community.

An introduction of new risk management tools within existing CAP instruments as an option in a revised Article 69 would be budget neutral with respect to the overall EU budget. National contributions would depend on MS preference, but introducing the measure would in any case be optional. On top of this, RD programmes contain measures directly related to risk management for agriculture and forestry, and that provide complementary support for preventive action in the areas of physical investment or human capital formation.

4. RESPONDING TO NEW CHALLENGES

The HC Communication identified a number of new and ongoing challenges facing the CAP (such as climate change, bio-energy, water management and biodiversity) and considers RD to be a key instrument to deal with these challenges. The screening exercise of RD programmes indicates that existing measures are already providing various solutions to address the new challenges and that MS have already included a significant number of related measures in their RD programmes for the period 2007-13.

The analysis of the impact of the proposed options for facing "new challenges" via RD measures focused on the impact of such proposals on improving the EU responsiveness to new challenges via greater MS uptake of second pillar measures. Four options were examined, aiming at targeting additional funds through modulation to existing measures related to "new challenges" with a reporting obligation concerning the new funding and indicators of measures in areas where "new challenges" were considered.

However, the constraints on the RD budget following the 2005 decision on the Financial Perspectives, present an obstacle to the realisation of 2nd Pillar objectives in the current budgetary period. Reinforcement of budgetary resources is also necessary in order to respond to the need for increased efforts to address new challenges identified in the HC Communication.

Analysis of alternative levels of modulation assessed their impact on the net budgetary transfers among MS and the level of their RD funds, as well as the impact on farm income for the farms and sectors involved. Since the manner to distribute modulated funds among MS, once the new MS are also part of the system, is not yet decided, the aim was to illustrate the potential impact of the options addressed. Different options were analysed, assuming an overall increase in modulation, achieved with the same annual steps from 2009 onwards, but taking into account different assumptions about the contribution of new MS. The retained option analysed is a variant of the idea supported by the European Parliament that introduces a progressive element in modulation based on different thresholds of payments, thereby addressing equity issues relating to individual producers limits.

5. CONCLUSIONS

The continuation of present CAP policies shows that the current policy framework, as reformed in 2003, contributes positively to fulfilling the main CAP objectives. The analysis points to areas where adjustments in current policies would lead to more optimal solutions.

With respect to the Single Payment Scheme, the implementation of the SPS and the gradual expansion of decoupling to more sectors render the need to allow MS to consider adjustments in their SPS model towards a more flat rate for payments. Such a move could address the societal concerns of unequal distribution of payments between farmers.

Further decoupling, as well as a continuation of move to producer support of sectors not yet integrated in the SPS, could significantly enhance market orientation of the CAP, but in some sectors decoupling may create the need for transitional measures in order to address economical, social or environmental concerns. Solutions could be addressed through a revision of Article 69 and through transitional periods.

Revising the scope of cross compliance would contribute to easing the administrative burden as well as addressing new challenges that were not as present in 2003. Also, environmental benefits of set-aside could be retained through the combined effect of adjustments in cross compliance and RD measures.

In terms of agricultural markets, the phasing out of milk quotas and removal of set-aside will allow the farmers to better respond to market situations.

Finally, a screening exercise has showed that the present tool kit of measures available under RD programmes appears to be sufficient to address new challenges. The best way to strengthen the role of these measures within the RD policy appears to be the creation of mechanisms that guarantee an increased uptake by Member States, as well as the provision of additional financing through progressive modulation.