The analysis of proposals of the Common Agricultural Policy reform and its impacts for the EU

Analýza návrhů Reformy společné zemědělské politiky a její dopady na EU

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Abstract: The Common Agricultural Policy (CAP) is of the character of a highly protective policy of the EU Member States. It includes a number of measures distorting the market directly and influences the farmers' incomes depending on their production. There have been two reforms of the CAP so far and the third one is prepared with intention to come into force from 2006; it is called Mid-Term Review (MTR). This reform is concentrated on keeping and increasing consumers' credibility and shifting to more competitive agriculture more orientated on market needs. The main Reform proposals include horizontal issues, i.e. Decoupling, Modulation/Degressivity, Cross-compliance, Farm Advisory System, IASC, Rural Development, and market issues concern dairy, cereals, rye, durum wheat, dried fodder, potato starch, seeds, nuts, rice, set-aside, carbon credit, beef. Besides the above mentioned goals, it is necessary to ensure conditions for rural development together with demands on environmental protection and improvement, so-called second pillar of the CAP. The attempt of cross-sectional summary and analysis of the MTR impacts for the EU was made in the article based on results of six studies performed by universities and DG AGRI in Brussels.

Key words: arable crops, decoupling, impacts, modulation, Mid-Term Review, payments

Abstrakt: Společná zemědělská politika (CAP) má povahu vysoce ochranářské politiky států EU. Pokrývá celou řadu opatření, které přímo narušují trh a ovlivňuje příjmy zemědělců vyplácené v závislosti na jejich produkci. Do současnosti proběhly dvě reformy CAP a třetí, která se připravuje, by měla vejít v platnost od roku 2006. Je nazvána Střednědobou zprávou (MTR). Tato reforma spočívá v udržení a zvýšení důvěry spotřebitelů a v přesunu ke konkurenceschopnějšímu zemědělství, více orientovaného na potřeby trhu. Hlavní návrhy MTR jsou soustředěny do horizontálních otázek, tj. decoupling, modulace/degresivita, cross-compliance, poradní systém pro zemědělce, IASC, rozvoj venkova a tržní otázky se týkají mléka, obilovin, žita, tvrdé pšenice, sušených krmiv, bramborového škrobu, osiv, ořechů, rýže, úhoru, uhlíkový kredit, hovězího masa. Vedle výše uvedených cílů je třeba zajistit podmínky pro rozvoj venkova společně s požadavky na ochranu a zlepšování životního prostředí, tzv. druhý pilíř CAP. V článku je učiněn pokus o průřezovou sumarizaci a analýzu dopadů MTR na EU vytvořenou na základě výsledků šesti studií zpracovaných univerzitami a Generálního ředitelství pro zemědělství v Bruselu.

Klíčová slova: plodiny na orné půdě, decoupling, dopady, modulace, Střednědobá zpráva, platby

INTRODUCTION

The Common Agricultural Policy (CAP) plays an important role not only in the EU budget but also in the lives of all people that live in the EU or use its agricultural products over the world. The CAP has come through two reforms so far, MacSharry's reform in 1992 and Agenda 2000 (came into force in 2000). It was reformed because of internal pressures (CP expenditures increased, the EU became a net exporter, huge intervention stocks) and external pressures (WTO – Uruguay Round: decrease of export refunds, decrease of import levies, decrease of domestic support; milk quota system in 1984).

Both above mentioned reforms tried to help the CAP to become more effective and to reduce its expenditures. Much has been achieved. Market balances have improved and agricultural incomes have developed favourably. A sound basis for enlargement and the current WTO negotiations has been established. Yet in many areas, gaps remain between the objectives set for the CAP and its capacity to deliver the outcomes expected by society.

Now, the CAP stands before third reform, so called Mid-Term Review (MTR) that should come into force from 2006. The MTR is proposed to be more market-oriented, more competitive, focused on higher quality, simpler and more transparent and more justifiable to both taxpayers and consumers.

The Greek presidency took the finalising of the MTR negotiations in first half of 2003 as its prime goal and it is to achieve its adoption on Italian presidency in the 2nd half of 2003.

From the first draft of the MTR in June 2002, there have been written six studies about the MTR, many documents were published and many positions were stated. There can be seen a great shift in proposals and in seeking solution that would be acceptable for all countries. If we consider that the MTR must reflect also the EU negotiating position in the WTO and the EU enlargement, we can see difficulties from several points of view.

MATERIAL AND METHODS

To have an overview, it is useful to state main objectives of the MTR:

– to improve competitiveness of the EU agriculture
– to promote a more market oriented and sustainable agriculture
– a better balance of support for rural development.

There are five main elements of the reform:

1. The introduction of single decoupled payment based on aids received by farmers in 2000–2002.
2. Reduction of all direct payments from 2006–2012 by up to 19% and shift of part of the "saved" money to Rural Development with 1% raising to 6% and other "saved" money are targeted at financing of the proposed reforms for cereals, dairy and other concerned sectors.
3. Tighter cross-compliance rules (i.e. respecting of environmental aspects, food-safety, animal welfare and occupational safety rules) for receiving direct aids.
4. New measures intended to improve and to strengthen Rural Development.
5. Various market measures, mainly concerning 10% cut in dairy prices linked to 2% quota & extension of the quota regime until 2014/15.

Proposals on the CAP reform submitted in January 2003 are mainly in line with those submitted in June 2002. However, the most important new proposals are placed into two areas:

– first, dairy: the European Commission (EC) made more concrete proposals and
– second, modulation/degressivity proposals: the EC suggests only 1% of funding to be shifted to Rural Development (contrary to 3% outlined last year).

The reason is a new agreement from October 2002 to limit the CAP market expenditure from 2007–2013.

The EC Proposals can be summarised in two greater groups of issues: horizontal and market. Horizontal issues include Decoupling, Modulation/Degressivity, Cross-Compliance, Farm Advisory System, Integrated Administrative & Control System and Rural Development. In the subject of market issues, there are concerned dairy, cereals, rye, durum wheat, dried fodder, potato starch, seeds, nuts, rice, set-aside, carbon credit, beef.

DISCUSSION

Horizontal issues

1. Decoupling

Decoupling means the detachment of direct payments form production. The single payment is proposed to be introduced from 2004 onward (paid between December 2004 and April 2005, i.e. from the 2005 EU budget). This amount will cover direct aid payments for cereals, oilseeds, protein crops, flax & hemp, linseed, set-aside land, grin legumes, all beef & sheep premiums, Nordic grain drying supplement, durum wheat top-ups, potato starch, seeds, rice, dried fodder and milk production. Excluded from decoupling are crop-specific elements of aid for protein crops, quality durum wheat, rice, nuts, energy crops, dried fodder, flax & hemp, potato starch. The basis for calculation of single payment per farm is the average of aid granted in 2000, 2001, 2002 (there are also exceptions and measures for unusual cases that occured in this period). Farmers may use the land covered by single payment for any agricultural activity except for permanent crops and set-aside of 10% (10-year non-rotational basis) must be respected.

This single payment will be broken down into "entitlements". Each entitlement will be calculated on the base of reference amount per holding divided by the number of hectares (including forage area) in the reference period. Requests for payment or entitlement will be accompanied by an eligible hectare defined as any agricultural area of the holding. Eligible hectares will not include the area under permanent crops, forests and the area used for non-agricultural purposes by 31st December 2002. For livestock production without an equivalent land base or where the entitlement is above EUR 10 000, a special payment will apply with corresponding conditions. National ceilings for the single farm payment and the special payment will be established. The 1% of this amount at Member State level will be reserved for hardship cases. Payments will only be made to farmers actively producing or maintaining land in good agronomic conditions. As regards the WTO aspects, the new single farm payment will be green box compatible.

Entitlements may be transferred, with or without land, between farmers within the same Member State. Any entitlement which has not been used in a period of a maximum of 5 years, apart from force major and exceptional circumstances, shall be allocated to a national reserve.

On the decoupled payment, the proposal was not intended to pay farmers for doing nothing; it is necessary to stress the keeping rules of cross – compliance and new opportunities for entrepreneurial farmers. Decoupling will improve the income situation of many farmers in marginal areas by providing greater farming flexibility.

2. Modulation/Degressivity

To improve the balance of support between market expenditures and rural development, modulation/degressivity will be introduced for the period of 2006–2012. New market reforms will be achieved through a new system of degressivity: all the CAP direct aids will be reduced progressively rising from an initial 1% to a maximum 19% in 2012. The reduction will not concern holdings with amounts up to 5 000 EUR, it will be fully applied to amounts above 50 000 EUR, a lower reduction will be made from 5 000–50 000 EUR. Modulation part resulting

Table 1. Degressivity and Modulation. Percentage reduction of direct payments

		2006	2007	2008	2009	2010	2011	2012
A	% general reduction in direct payments	1	4	12	14	16	18	19
B	% total reduction applying successively to the different branches of direct payments							
	from 1 to 5 000 EUR	0	0	0	0	0	0	0
C = (A + E)/2	from 5 001 to 50 000 EUR	1	3	7.5	9	10.5	12	12.5
D = A	above 50 000 EUR							
E	of which % of the direct payments destined for the Rural Development budget							
	from 5001 to 50 000 EUR	1	2	3	4	5	6	6
	above 50 000 EUR	1	2	3	4	5	6	6
F	Of which of the direct payments destined	0	1	4.5	5	5.5	6	6.5
	for financing future market needs	0	2	9	10	10	12	13

Notes: A = Degressivity, B to D = By tranche of direct payment, E = Modulation – Destined for Rural Development budget, F = Destined for financing future market needs

Source: Explanatory Memorandum. Commission of the European Communities, Brussels, 21. 1. 2003

from degression, starting at 1% in 2006 rising to 6% in 2011, shall be made available to the Member States as an additional Community support for measures to be included in their rural development programming. These amounts are proposed to be reallocated among Member States according to agricultural area & employment and GDP per capita in purchasing power parity. Degression and modulation would not apply to the new Member States until the phasing-in of direct payments reaches the normal EU level.

Only 42.2% of the EU-15 farm holdings will be affected by modulation & degressivity proposals in the MTR – and 36% of the total "modulated" amounts will come from dairy sector.

Table 1 above shows the system of reduced payments granted to a farmer in a given year.

If a 20% shift of funds from market measures to Rural Development schemes was to be achieved and Brussels ceilings still respected, the Commission would have had to propose an eventual 33% net reduction in aid payments for the larger farms, which would be unacceptably high. Future reforms for sugar, olive oil, cotton, tobacco and possibly wine and fruit & vegetables are due this year, further adjustments, i.e. higher rates of degressivity, might be needed in order to finance those reforms.

Modulation and degressivity will not concern new Member States until phasing-in of direct payments reaches the normal EU level.

3. Cross-Compliance

Cross-compliance rules mean application of the European standards regarding environment, food safety, animal health & welfare and occupational safety related to farm level. Beneficiaries of direct payments will also be obliged to maintain all agricultural land in good agricultural conditions.

Sanctions will be applicable in any case of non-compliance on a beneficiary's farm. The sanction will have a character of partly (in cases of negligence up to 10% or up to 20% in repeated cases) or full reduction of a payment (where the breach is seen to be intentional). This will be applied as a whole-farm approach the system will cover all sectors and will be related also to unused agricultural land.

4. Farm Advisory System

This system is compulsory for all farms receiving more than 15.000 EUR in direct aid or holdings with a turnover of more than 100.000 EUR within 5 years (starting in 2005). Other farmers will enter the system on a voluntary basis. The system is aimed at advising farmers on how standards and good practices are applied in the production process. Farmers may benefit up to 1.500 EUR to help them to participate in the farm advisory scheme, stipulating that the EU – funding for this measures may not exceed 80% of the total cost (it was 95% in previous draft). Support for farm audits will be available under Rural Development. This new system will cover in practice about 7% farmers (it was 30% before changes proposed in 2003).

5. IACS

Integrated Administrative and Control System (IACS) must be adjusted to reflect decoupled payments, i.e. the system will in future be more relevant to administrate payment entitlements. The introduction of the single farm payment will lead to a simplification of key component of the present IACS. The current system will be used to facilitate cross checks between payment entitlements and surfaces needed to activate them. To the new IACS, the system for identifying agricultural parcels therefore remains fundamental.

Applications for aid will be under administrative controls relating to cross-compliance, to the eligibility of surfaces and the existence of the corresponding payment entitlements. These controls should be complemented by on-the-spot checks. Altogether, they would give rise to aid reduction or exclusions where condition have not been met.

The control systems already existing in Member States to verify respect of the statutory management requirements and good agricultural conditions may be used in the framework of IACS, with which they will also have to be compatible.

Rural development

The Commission proposes expansion of measures under Rural Development to cover food safety, animal health and animal welfare, without changing the basic framework under which Rural Development support is implemented. All new measures are targeted at farmer beneficiaries. It will be up to Member States if they include these measures within their rural development programmes. The new measures will comprise:

1. On food quality, a twofold concept: the introduction of incentives to participate in the national or the EU-wide quality assurance schemes up to 1 500 EUR a year for 5 years; support for producer groups to inform consumers about and to ‚promote the products under quality schemes – public support up to 70% eligible project costs.

2. For "meeting standards, Member States can offer a temporary and degressive support to help their farmers to adapt to the introduction of demanding standards for up to 5 years of maximum 10.000 EUR per holding.

3. On animal welfare: the possibility to aid farmers who commit themselves for at leas 5 years to improve welfare of their farm animals and which go beyond the usual good animal husbandry practice, whereby an annual payment of up to 500 EUR per livestock unit would be based on the additional costs and income foregone from this commitment.

Market issues

Dairy

The intention is to prolong the reformed dairy quota system until 2014/15 campaign to provide a stable perspective for dairy farmers. It is necessary to reduce the support price for milk with a corresponding quota increase of 1% per year in 2007 and 2008. Over five years, intervention price cuts of 3.5% year for skimmed milk powder and 7% per year for butter will occur. Intervention purchases of butter will be suspended above a limit of 30 000 tonnes per year. All dairy payments will be integrated into the single farm payment. The high impact of proposals will affect four out of every five dairy holdings across the EU, i.e. 80 % of dairy holdings will face reduction in direct payments.

As far as dairy quota system is concerned, the reform should be extended to better reflect price realities and the need to further differentiate the levels of support for butter and skimmed milk powder.

Cereals

The intervention price should be cut by 5% to 95.35 EUR from 2004/2005 to ensure that intervention is a real safety net. Area payments for cereals and other relevant arable crops will be increased from 63 EUR to 66 EUR/t. These will be included in the single farm payment.

To avoid a further accumulation of intervention stocks, rye shall be excluded form the intervention system.

The aid for selected seed species will be integrated into the single farm payment.

The supplement for protein crops of 9.5 EUR/t will be converted to 55.57 EUR/ha with a Maximum Guaranteed Area (MGA) of 1.4 mil. ha.

A new premium of 45 ha/ha for energy crops for up to 1.5 mil ha will be introduced. Non-food crop production is no longer permitted.

Durum wheat

The supplement for durum wheat in the traditional production zones will be reduced from 344.5 EUR to 250 EUR per ha and included in the single farm payment. The specific aid for other regions will be phased out over 3 years starting in 2004. A new premium will be introduced to improve quality of durum wheat (40 EUR/ha) in traditional production zones within the MGA there currently applying.

Starch potatoes

One half of direct payment (55.27 EUR/t) for producers of starch potatoes will be included in the single payment. The other 50% will be maintained as crop specific payment for starch potatoes. The minimum price is abolished. Production refunds for starches and certain derived products will no longer be applied.

Dried fodder

Support in the dried fodder will be redistributed between growers and the processing industry. Direct support to growers (68.83 EUR/t for dehydrated and 38.64 for sun-dried) will be integrated into the single farm payment. Degressive aid starting from EUR 33/t in 2004/2005 will be applied for fodder industry and phased out over 4 years.

Rice

A 50% cut in the intervention price to 150 EUR/t is supposed to stabilise market balances. The current direct aid will be increased to 177 EUR/t. Of this, 102 EUR/t will become a part of the single farm payment, the remaining 75 EUR/t will be paid as a crop specific aid. A private storage scheme will be introduced.

Nuts

An annual flat rate payment of 100 EUR/ha for up to 800 000 ha MGA may be topped up by Member States by annual maximum amount of 109 EUR/ha.

Table 2. EU-25: Expenditure forecasts for heading 1a – Reform proposals (mil. EUR)

Heading 1a	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
EU-25 Ceiling	42 979	44 474	45 306	45 759	46 217	46 679	47 146	47 617	48 093	48 574
EU-25 Expenditure	41 681	43 642	44 395	45 156	46 123	47 568	48 159	48 805	49 451	50 099
of which EU-15	41 320	41 339	41 746	42 183	42 802	43 569	43 513	43 513	43 513	43 513
of which CC-10	361	2 303	2 649	2 973	3 321	3 999	4 646	5 292	5 938	6 586
Difference	1 298	832	911	603	94	–889	–1 013	–1 188	–1 358	–1 525
Degression				228	751	2 030	2 420	2 810	3 200	3 343
of which available for rural development				228	475	741	988	1 234	1 481	1 481

Source: Explanatory Memorandum. Commission of the European Communities, Brussels, 21. 1. 2003

Beef

Although decoupling will have major implications, no specific measures are proposed. As far as this sector is concerned, horizontal measures will reinforce cross-compliance requirements, incl. stipulation that permanent pasture on 31. 12. 2002 must be maintained in that state, while also providing new "quality" opportunities within Rural Development measures.

Impact of suggested proposals

It can be said that the MTR proposals would entail an improved allocation of resources between commodities and greater income transfer efficiency. The cereal production can be expected to decline owing mainly to the implementation of the decoupling of direct payments, the carbon credit proposal and the cut in support price level. Wheat would appear to be less affected than coarse grains as it should benefit from better world market price prospects than most coarse grains.

Even if most analysis foresee the oilseed production to decline slightly, more probably the carbon credit payments could to lead to an increase in the production of energy crops, particularly of oilseeds, mainly at the expense of cereal production.

In the livestock sector, the implementation of decoupling would entail some decline in beef and sheep production as it would favour extensification of production systems, generating and increase in market prices with positive income effects for the livestock farms concerned. However, this income increase would be broadly offset at the sector level by the negative income impact of the decline in coarse grains market prices due to the abolition of rye intervention.

The proposed measures involve saving which is estimated at 337 mil EUR for 2006 and about 186 mil EUR as from 2010 for the EU-15.

For the new accession countries, the financial impact in 2010 is for an additional expenditure of around 88 mil EUR which increases annually to reach 241 mil EUR in 2013, as a result of the increasing share of direct aids in their total expenditures.

A reduction in the direct aids for the EU-15 from the financial year 2007 is proposed in order to maintain total expenditures under the new ceiling for the financing of market measures in EU-25 (see Table 2).

Above mentioned adjustments are necessary to ensure that the EU is able to provide a sustainable and predictable policy framework for the European model of agriculture during the next years.

CONCLUSION

The goal of proposed changes is to make the CAP acceptable not only for European agriculturists but also for the society as a whole. Proposals submitted within the MTR allow a great flexibility in production decisions and significantly simplify the manner by which support is provided to producers while guaranteeing their income policy, they facilitate the enlargement process and help to better defend the CAP in the WTO. By reorienting support towards more extensive agricultural practices and less trade-distorting domestic support, the proposals are expected to reduce export availability, thereby contributing to stronger world market prices, which is in line with the agricultural sector in developing countries.

The MTR core are the horizontal and market issues. Decoupling is intended to increase competitiveness of agricultural products; the single farm payment per farm will be introduced. Modulation will lead to improvement of balance support between market expenditure and rural development. The system of degressivity will introduce the principle of progressive contributions according to the overall amount of direct payments received by a farm in order to ensure that reductions in direct payments are balanced and simple to apply.

The proposed mechanism for generating savings ensures new financial needs that can be met in a balanced manner across the farming sector. If the budget savings were not generated in a fair, transparent and predictable manner, the EU could face stalemate on further agricultural decisions. This would make it very difficult for farmers to plan, since, in addition to further reform efforts, they would not be able to anticipate how such efforts would be financed.

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