



Institute for
European
Environmental
Policy

**TOWARDS THE CAP HEALTH CHECK AND THE
EUROPEAN BUDGET REVIEW**

THE PROPOSALS, OPTIONS FOR REFORM, AND ISSUES ARISING

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The material provided in this document is based on speeches made by Mariann Fischer Boel over the last 18 months, reports in Agra Facts, and informal personal communication. It in no way anticipates or reflects the official position of any of the institutions mentioned, and is based on an analytical interpretation of the material by the authors.

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1 INTRODUCTION

This paper discusses the prospects for agricultural policy reform in the European Union arising from the 2008 Health Check of the CAP and the review of the European Budget, due to be completed in 2009. Its aim is to locate the expected proposals of the Health Check in recent and potential future evolutions of the CAP; to review the proposals and situate them in a broader context of concurrent political processes and EU policy priorities, and to discuss the extent to which they will frame the nature and trajectory of the debate; to consider the key players; and to discuss some of the issues that arise and desirable outcomes for 2013 and beyond.

It provides a briefing to inform discussions at a ‘CAP Retreat’, organised by the German Marshall Fund of the United States and the William and Flora Hewlett Foundation to be held in Brussels in October 2007, and involving key stakeholders drawn from civil society.

2 LOCATING THE HEALTH CHECK

The CAP Health Check is due to be formally launched by the European Commission (with DG Agriculture in the lead¹) on 20 November 2007 and concluded over the course of 2008. Although the proposals have not yet been formally published, the current Agriculture Commissioner, Mariann Fischer Boel, has drip fed their contents to audiences across Europe in speeches made over the last 18 months². As a result, stakeholders and commentators have a fairly detailed insight into the Health Check’s likely content, scope and tone.

A literal interpretation of the Commissioner’s speeches would suggest that the Health Check is limited in scope, the aim of which is to adapt the CAP to an evolving set of circumstances over the period 2008 - 2013. Its title - ‘the Health Check’ - testifies to the Commission’s modest ambitions for the exercise and the Commissioner has consistently used a soothing tone when talking about the expected proposals. She states that the Health Check’s purpose ‘is not to change the essential direction of the CAP’³, and that it ‘was never meant to be about further fundamental reform’⁴. Rather, it will ‘assess whether the reformed CAP is working as it should, and will make adjustments and streamline it where necessary to reduce bureaucracy and red

¹ DG Agriculture is the executive body within the European Commission responsible for agriculture and rural development policy, and the Health Check.

² See Agra Facts 77-07, 22.09.07, for a special edition on the details of the Health Check proposals based on a leaked version of the Commission’s draft Communication, ‘Preparing for the Health Check of the CAP Reform’.

³ Mariann Fischer Boel The CAP in the European scenario, International Forum on Agriculture and Food, Cernobbio, Italy, 20 October 2006, SPEECH/06/622.

⁴ Mariann Fischer Boel The European Model of Agriculture, National Parliaments Conference, Helsinki, 12 October 2006, SPEECH/06/589.

tape'⁵. She has also simultaneously represented it as 'an opportunity to fine tune our toolbox'⁶ and 'an ideal opportunity to make sure our agriculture is really in line with society's needs and expectations'⁷.

Indeed, she has characterised the Health Check as an exercise to tie up a number of loose ends from the last reform, such as the incomplete transfer to fully decoupled payments. Thus it is presented as the first opportunity for the European Commission, Member States and stakeholders to reflect on the successes and failures arising from the last round of CAP reform in 2003 which resulted in some rather substantial changes to the CAP. In short, the proposals appear to be orientated towards short term, pragmatic and administrative revisions to the CAP in its present guise.

The Health Check, however, is not being conducted in a vacuum, and to engage with it on this constrained agenda would be a missed opportunity. There are a number of concurrent political processes at play, which means that in reality, the scope and ramifications of the Health Check are likely to be much broader than an exercise in the simple tweaking of existing measures would seem to imply. The forthcoming review of the European budget, launched this year and due to be concluded in 2009, and the ratification of the EU Reform Treaty, scheduled to come into force in 2009, are important in this regard. The Budget debate is likely to precipitate a comprehensive discussion on the totality of EU spending, of which the CAP is allocated the largest single share. The comments of the Budget Commissioner, Dalia Grybauskaitė, at the launch of the consultation on the EU Budget Review on 12 September, that the provision of traditional agricultural support should not be taken for granted, suggest that a strong case will need to be made for the rationale underpinning European expenditure on agriculture. The Health Check provides one such opportunity to begin to develop and rehearse these arguments.

The likelihood that the Health Check will act as a trigger for a much broader debate about the intrinsic rationale for the CAP, its objectives, and the appropriateness and effectiveness of its measures, is manifest in the way in which key stakeholders are beginning to engage with the Health Check and the Budget Review. The speech of the French President, Nicholas Sarkozy, on the 11 September 2007, at a meeting of livestock farmers in Rennes is evidence of this⁸. In his speech, he made a commitment to use France's Presidency of the EU in the second half of 2008, which is concurrent with the Commission's planned schedule for the completion of the Health Check, to facilitate a debate about far reaching reform. Whilst the reform rhetoric perhaps conceals a more conservative approach to CAP reform, his

⁵ Mariann Fischer Boel European agricultural policy facing up to new scenarios, Confederazione Generale dell'Agricoltura Italiana, Taormina, Italy, 23 March 2007, SPEECH/07/182.

⁶ Mariann Fischer Boel The European Model of Agriculture, National Parliaments Conference, Helsinki, 12 October 2006, SPEECH/06/589.

⁷ *Ibid.*

⁸ Reported in Agra Facts 72-07; Sarkozy sets out vision of a 'new' CAP, Agra Europe, 11 September 2007; Sarkozy changes French stance on CAP, Financial Times 12 September, 2007; Sarkozy opens door for CAP reform, EurActive.com, 12 September 2007, <http://www.euractiv.com/en/cap/sarkozy-opens-door-cap-reform/article-166651>.

characterisation of the Health Check and the Budget Review as a joint platform for a debate on the future of the CAP is fairly typical, and he is not alone in eliding these two agendas.

Mariann Fischer Boel and others have been insistent that the Budget Review should not be driven by immediate budgetary concerns, arguing that ‘policy must drive thinking on the European budget’, and that spending programmes on agriculture and rural development should not be designed retrospectively to fit the available budget⁹. In this way, clarity over policy objectives and the instruments needed to achieve these should precede an assessment of the budget required for implementation. In turn, the Budget Review, in outlining the likely financial allocations and spending priorities, will provide an indication of the possible scope of a future CAP. This needs to be a complimentary and iterative process. It will provide a framework for a wide ranging debate on the future of the CAP, in advance of the next substantial round of CAP reform, expected in 2013. Critical examination should be focused on the needs of rural communities, and specifically the role in which the land use sector, and notably agriculture, will play in the fight against climate change and biodiversity decline.

In the remainder of this paper, we introduce the expected proposals under the Health Check and discuss the concurrent political events and EU policy priorities that are likely to influence the debate. We proceed to unpack some of the issues arising from both the Health Check and the debates that will be precipitated by the Budget Review. In a final section, we discuss the options and likely trajectory for reform up to 2013 and beyond.

2.1 The 2003 CAP Reform

The last round of CAP reform took place in 2003 as a result of a ‘Mid-Term Review’ (MTR) of the version of the CAP which came into place following the Agenda 2000 reforms. Under the MTR, Franz Fischler, the then Agricultural Commissioner, launched fairly ambitious proposals with limited prior discussion¹⁰.

The overriding aim of the 2003 reform was to create a more competitive, market responsive agricultural sector founded on the principles of high environmental and

⁹ The Agriculture Commissioner has argued that ‘Thinking about policy must drive thinking about the European budget. If we put things the other way round, either the cart will not move, or it will tip over, and we won’t have a CAP that can meet the very real challenges of the future.’ Mariann Fischer Boel, The Future of the CAP, Agra Europe Outlook Conference, London, 27 March 2007, SPEECH/06/197.

¹⁰ On this occasion, the reform proposals focused on Pillar One of the CAP. This Pillar covers the direct payments farmers receive as well as classic interventionist market management tools. It is financed by the European Agricultural Guarantee Fund. Pillar Two refers to the rural development sphere of the CAP. Rural development is broadly defined to include measures which promote the economic, environmental and social well being of the EU’s rural areas. A dedicated fund, the European Agricultural Fund for Rural Development (EAFRD), provides the financial backbone to Pillar Two and was set up in 2005, instituting a change in the structure of rural development funding. The legal foundation for rural development support in the EU is provided for by Council Regulation 1698/2005 of 20 September 2005 on support for rural development by the European Agricultural Fund for Rural Development, OJ L 277, 21.10.2005.

animal welfare standards¹¹. At its heart, was a substantive, although incomplete, move towards decoupling for some of the key commodities within the CAP, many of which are governed by their own individual regimes known as Common Market Organisations (CMOs)¹². Decoupling severed the link between production and direct payments, thus removing the incentive to produce any particular good. The 2003 reforms also created a new mode of payment delivery, the Single Payment Scheme (SPS), introduced in 2005 in some Member States and in 2006 in others. A simplified system applies in most of the new Member States, known as the Single Area Payment Scheme (SAPS).

Some CMOs not addressed by the 2003 package have since been modified, including sugar, tobacco, olive oil and fruit and vegetables. Negotiations between the Member States and the Commission on a reform to the wine CMO are underway. The mechanism through which to achieve higher standards is cross compliance. Recipients of the Single Payment may face a reduction to their payment if breaches to cross compliance standards occur. These standards have come into force in stages, the first set in 2005, followed by others at the start of 2006 and 2007. These standards, in the main, reinforce preexisting legislation, such as the Birds Directive (Council Directive 79/409/EEC) and the Nitrates Directive (Council Directive 91/676/EEC) and are collectively referred to as Statutory Management Requirements (SMRs). Farmers are also required to respect a set of basic farming standards known as Good Agricultural and Environmental Condition (GAEC)¹³. The GAEC standards were introduced partly to ensure a minimum level of maintenance of agricultural land in order to deter land abandonment, a potential threat in an era of decoupled subsidy payments. The reform also sought to maintain the area of pasture in the EU, partly to temper a mass conversion to arable production if incentivised by market prices, and, less directly, to preserve the environmental benefits associated with certain grasslands.

Taken as a whole, the 2003 model is relatively recent, and thus there has been little time for the structural, socio-economic and environmental impacts of the measures to manifest themselves. As a result, the evaluation of impact has been limited, rendering it difficult to collate evidence to mount a systematic defence or critique. Indeed, the fact that the present incarnation of the CAP has been in existence for less than three years is frequently cited by some Member States in the forum of the EU Agriculture Council, in part, to ward off debate that could result in further CAP reform.

¹¹ The legal document implementing the reform is Council Regulation 1782/2003 of 29 September 2003 establishing common rules for direct support schemes for farmers, OJ L 270, 21.10.2003.

¹² The 2003 reform allowed Member States to retain coupled payments for arable crops (up to 25 per cent of the national ceiling), for hops (up to 25 per cent), for sheep and goat payments (up to 50 per cent), and for beef and veal payments (up to 100 per cent).

¹³ GAEC provide a framework for Member States to introduce standards for soil erosion, soil structure, soil organic matter and the minimum maintenance of agricultural land.

3 THE EXPECTED PROPOSALS OF THE HEALTH CHECK

At the time of writing, DG Agriculture has finalised its draft Communication on 'Preparing for the Health Check of the CAP Reform'. It is now being circulated amongst relevant Directorate-Generals. The analysis that follows is based on the draft proposals which could be amended following the Commission's internal consultation process. Following the adoption of the Communication in November, there will be a short period of public dialogue, involving the Member States, the European Parliament and civil society. Formal legislative proposals are likely to be tabled in spring 2008 and may come into force fairly rapidly thereafter. More sensitive measures may take longer to be resolved resulting in new or amended legislation not coming into force until 2010 or 2011. This would mean that certain measures may not be implemented until after the ratification of the EU Reform Treaty and the inauguration of a new College of Commissioners, which are both due to take place in 2009.

The proposals are expected to fall into four main categories:

- Adjustments to the Single Payment Scheme (SPS), to make it more effective, efficient and simple, and associated measures, including cross compliance, along with consideration of the scope for further decoupling;
- Proposals covering the main market regimes, including dairy policy and arable set aside;
- Issues concerned with modulation, expenditure and the budget, and the respective roles of Pillar One and Pillar Two of the CAP;
- Addressing new challenges, in relation to climate change, the growth in biofuels and water management, through adaptation to risks and opportunities.

These are discussed in more detail below. The evidence has been drawn from speeches made by Mariann Fischer Boel over the last 18 months, reports in the agriculture press and personal communication. Section five seeks to unpack these proposals in the context of a broader policy debate and to highlight some of the issues they raise.

3.1 The Single Payment Scheme (SPS) and Decoupling

It is thought that the Commission intends to cement the SPS and to respond to some of the more trenchant criticisms of the scheme by strengthening its rationale. This is also likely to be accompanied by a reduction in the extent to which Member States are permitted to continue with coupled payments, a vestige of the CAP regime prior to the 2003 reform. Decoupling was a key aim of the MTR and one which the Commission now appears keen to realise.

Simplification in the method of calculating single payments will be proposed. It is thought that the Commission favours an adoption in all Member States of the 'regional average' model which involves flat rate payments per hectare for all farms in a region. The proposals are expected to include calls for Member States to move towards a 'flatter rate' of support from 2009 – 2013. Most of the old Member States

(EU-15) have opted for the ‘historic’ model, the important exceptions being Germany, Finland and the UK¹⁴. This reflects a desire to maintain continuity in the amount received by the farmer since payments are based on historical receipts. Flat rate area payments are the favoured option of the twelve new Member States which joined the EU in 2004 and 2007. In principle, the regional model is easier to justify, not least because it promotes a more equitable distribution of payments on the basis of an objective criterion. The wholesale adoption of this model would result in a greater redistribution of payments from larger to smaller farms and counteract the concentration of very large payments on a small number of farms. It is also, in principle, simpler. The issue is sensitive, however, not least because of its redistributive effects.

It is thought that upper and lower limits will be set on SPS payments. There will almost certainly be a proposal to eliminate the smallest claims with a new cut off expressed either in monetary or in area terms in order to promote administrative efficiency. A proposal to raise the minimum eligible area for farms receiving the SP to 0.3 hectares seems likely. The proposals are also likely to suggest the reduction in direct payments to large farms to address public perceptions about the distribution of CAP payments. This is expected to be one of the most controversial elements of the proposals, due to intense opposition from key Member States, including the UK and Germany¹⁵. Movement in the US on this issue under the forthcoming US Farm Bill (2007 – 2012), currently under discussion in the US Senate, may have provided a stimulus for EU action. In the version of the Bill agreed by the House of Representatives, those farmers earning more than \$1 million a year will not be eligible to receive any farm program payments¹⁶.

The Commission is thought not to support an absolute cap on payments, although the establishment of three tiers has been suggested. One reason for tapering may be to render restructuring and the subdivision of farm holdings, in order to circumvent the capping rule and maximise income from the Single Payment, less attractive. If implemented, this proposal could result in a 10 per cent reduction to payments between €100,000 and €200,000; 25 per cent to payments between €200,000 and €300,000; and 45 per cent to payments over €300,000¹⁷. These tiers are provided as examples only and ‘degressive capping’ is not formally mentioned. Unconfirmed

¹⁴ In the UK, Defra, the Department for Environment, Food and Rural Affairs, has been heavily criticised for choosing to implement a dynamic hybrid payment model, which led to significant delays in the payment of Single Payment claims and resulted in a fine from the Commission amounting to around €90 million. See, for example, the EFRA Committee (2007) The Rural Payments Agency and the Implementation of the Single Payment Scheme: Government Response to the Committee’s Third Report of Session 2006–07, HC 956.

¹⁵ An analysis by farmsubsidy.org of a €300,000 payment limit shows that just 1,880 farms (0.04%) would be affected in the EU-15, saving €978,745,000 from the CAP budget. Most of these farms are in Germany (1,430) and the UK (330). See Thurston, J. (2006) Capping the CAP – The effect of payment limits on farm subsidies. Paper prepared by farmsubsidy.org.

¹⁶ House Committee on Agriculture (2007) 2007 Farm Bill Commodity Title: Investing in a Strong Safety Net that Ensures a Stable Food Supply. Fact Sheet for the 2007 Farm Bill, Washington.

¹⁷ Rough estimates suggest that approximately 25,000 out of a total of seven million holdings in the EU-15 would be affected by the proposals. See Agra Facts 74-07, 18.09.07.

calculations suggest that this proposal could result in a shift of approximately €1 billion a year to Rural Development spending, although speculation surrounds the likely destination of money saved from the application of these ceilings. One possibility is that the money would be available for use in the Rural Development Programmes of the Member State in which the caps are applied. Alternatively, it may be retained in Pillar One and recycled through Article 69 of Council Regulation 1782/2003¹⁸.

The Commission is certain to propose a reduction in the number of coupled payments retained by a Member State. Abolishing the option in the arable sector – currently only applied by France and Spain – is expected given high cereal prices. Other sectors may be excluded, however, as it is understood that the Commission believes that partial coupling may still have some relevance in certain regions where production levels are low but remain economically and environmentally important. The principle of full decoupling is generally perceived as positive. Viewed through the trade liberalisation prism of the WTO, it is regarded as more equitable, and in general, results in less pressure on the environment as the incentive to maximise production is removed. Exceptions, however, do occur.

There is a significant argument in favour of retaining coupled payments for suckler beef cattle because of the environmental benefits of this form of production relative to more intensive methods. Outdoor grazing animals play an important part in landscape and biodiversity management. Many Member States have retained this payment for environmental or other reasons. DG Agriculture has itself hinted at retaining a 100 per cent coupled suckler cow premium¹⁹, although this outcome is by no means certain given that it is anathema to the decoupling orthodoxy. Support for this specific production system could also be delivered through a targeted Pillar Two measure, such as the agri-environment measure (Article 39 of Council Regulation 1698/2005), the natural handicap measure (Article 37 of Council Regulation 1698/2005) or through Article 69 of Regulation 1782/2003. Relatively equal merit can be ascribed to all of these options at this stage.

The obligations accompanying the SPS are confined to cross compliance and the maintenance of the area of permanent pasture. Most cross compliance measures consist of mandatory measures in environment, animal health and animal welfare which will apply to all farmers irrespective of whether they receive the SP or not. Cross compliance is contentious and some Member States will exert pressure to

¹⁸ Article 69 of Council Regulation 1782/2003 allows a Member State to siphon off up to ten per cent of SPS/coupled payments and redirect the funds ‘for specific types of farming which are important for the protection or enhancement of the environment’, or for ‘improving the quality and marketing of agricultural products’. Eight Member States currently make use of this option although there is little information on the exact objectives surrounding implementation. A good example is Scotland, where Article 69 provides around £20m of funding per year for the Scottish Beef Calf Scheme. The resurgent interest in Article 69 allows for a redistribution of funding to those sectors that genuinely need it and offers a way to protect the most vulnerable production sectors, many of which play an important role in maintaining high nature value farming. Under the Health Check proposals, Article 69 may be adjusted to confer greater flexibility, and provisions could be made for money to be targeted at certain production areas in a Member State rather than at the sector as a whole.

¹⁹ Agra Facts 54-07, 03.07.07.

reduce its impact and simplify the process, largely on administrative grounds. As such, there is likely to be strong resistance to any proposals to expand the list of Statutory Management Requirements (SMRs) or broaden the scope of Good Agricultural and Environmental Condition (GAEC). DG Environment and environmental NGOs, however, are likely to press for the judicious inclusion of more environmental obligations, such as rules on sustainable water use. There have also been calls to strengthen the way in which Member States choose cross compliance standards to ensure they address identified environmental priorities²⁰. In its 2007 report²¹, the Commission initiated the implementation of proposals for improving the controls and sanctions of cross compliance. It is thought that simplification will be further advanced under the Health Check proposals which will consider increased and improved targeting as a way of making cross compliance more effective.

3.2 Market Regimes

Given the switch to decoupling there are growing demands from farmers for some kind of safety net against low prices, especially if the further reduction in intervention support and export subsidies in the medium term goes ahead as anticipated. In response to this, new mechanisms for the management of risk to buffer farms against low prices, such as subsidised crop insurance may be signposted, as a medium term option rather than as an immediate proposal²². In the meantime, the Health Check is likely to encourage Member States to use measures in Pillar Two to establish risk management measures as a way of providing targeted solutions to varying risks across regions and sectors.

In the arable sector, the key proposal is likely to be the permanent abolition of compulsory set aside, which is currently set at 10 per cent. As a precursor, a set aside level of zero per cent for autumn 2007 and spring 2008 sowings was approved by agriculture ministers at a Council meeting on the 26 September²³. High cereal and oilseed prices boosted by poor harvests, rising global demand, and the boom in bioenergy driven by EU energy policy, remove the economic rationale for set aside and have received support from farming organisations²⁴. Conversely, environmental

²⁰ See, for example Farmer, M., *et al.*, (2007) Cross Compliance: Practice, Lessons and Recommendations, Deliverable 24 of the CC Network study for DG Research, SSPE-CT-2005-022727.

²¹ Report from the Commission to the Council on the Application of the System of Cross Compliance, COM (2007) 147, 29.03.2007.

²² The European Commission has raised the possibility of using a suite of risk and crisis management tools to replace, either wholly or partially, all ad hoc or emergency payments. See Communication from the Commission to the Council on risk and crisis management in agriculture COM (2005) 74, 09.03.05.

²³ Press Release - Commission proposes to set at zero the set-aside rate for autumn 2007 and spring 2008 sowings. IP/07/1329, Brussels, 13 September 2007.

²⁴ See Farmer's Weekly, 03.09.07, for a report on the positive response from the UK's National Farmer's Union (NFU) to the Commission's proposals on set-aside.

interests have been vociferous in their concerns over the loss of set aside²⁵. Set aside land provides a range of environmental benefits by providing a habitat for farmland biodiversity, improving water quality through reduced pesticide and fertiliser applications, and decreasing the risk of soil erosion by increasing soil cover, which also promotes carbon sequestration²⁶.

The Agriculture Commissioner has stated that she will listen to the concerns of NGOs regarding the environmental contribution of set aside during the Health Check²⁷. DG Environment, who may be able to exert some influence on the outcome of this particular debate, could argue in favour of maintaining a rate of between two and four per cent set aside next year²⁸, and environmental lobby groups have already floated a number of regulatory or incentive options to safeguard the environmental benefits associated with set aside if it is completely abolished. The Commission is thought to favour the delivery of these benefits through voluntary measures, and the proposals suggest the strengthening of existing rural development support to forms of land, water and ecosystem management that promote environmental benefits, such as maintaining permanent pastures and protecting riparian strips.

The Commission will propose the end of milk quotas by March 2015. The pathway would be smoothed by transitional measures, for example, a progressive increase in the quotas of all Member States in advance of this date so that they become less binding. This would allow milk production to move between Member States and between regions in those Member States that have prevented this in the past. This is likely to result in greater farm level and regional concentration of production, and a reduction in dairying in the Less Favoured Areas (LFAs), with significant social and environmental implications. Under the Health Check proposals, the Commission recognises the challenge of retaining a minimum level of production in mountainous areas, and suggests that rural development measures could provide a means to add value to these products. Some form of more specific support may also be required, and Article 69 of Council Regulation 1782/2003 could be amended so that money is targeted at certain production areas within a Member State rather than at the sector as a whole.

²⁵ See, for example, Mark Avery, Conservation Director of the Royal Society for the Protection of Birds, 'If our countryside were scruffier ...', The Independent, 6 September 2007; Agra Facts 70-07, 05.09.07 which outlines DG Environment's concerns over the potential loss of environmental benefits, in particular for biodiversity, as provided by the current 10 per cent rate of compulsory set aside.

²⁶ Two recent reports discuss the environmental benefits of set aside. See Hodge I., Reader M., Revoredo C., (2006) Project to Assess Future Options for Set-Aside. Report for the Department for Environment, Food and Rural Affairs, University of Cambridge, Department of Land Economy; Silcock P., Lovegrove C., (2007), Retaining the Environmental Benefits of Set-Aside - A Policy Options Paper. Report for LUPG, Cumulus Consultants Ltd.

²⁷ Press Release - Commission proposes to set at zero the set aside rate for autumn 2007 and spring 2008 sowings. IP/07/1329, Brussels, 13 September 2007.

²⁸ Agra Facts 70-07, 05.09.07.

3.3 Modulation and the Budget

Notwithstanding transfers to Pillar Two, the Pillar One budget will remain constant until 2013. In a recent speech, the Commissioner appeared to signal that Pillar Two is the future of the CAP, noting that ‘this is where the music is playing’²⁹. She believes that Pillar Two can only be strengthened by increasing compulsory modulation. The Health Check proposals pave the way for an increase in the level of compulsory modulation, from 5 per cent in 2008, and rising thereafter by 2 per cent per annum, from 2010 until 2013. This would result in compulsory modulation being set at a rate of 13 per cent in 2013, eight per cent higher than the rate currently provided for under Council Regulation 1698/2005. It has been estimated that each two per cent rise in the rate of compulsory modulation would result in the transfer of 500 - 600 million EUR per year to Rural Development spending across the EU³⁰. Although it is understood that there is no mention of voluntary modulation in the proposals, it is not clear whether the Commission will support the continuation of ‘voluntary’ modulation, which the UK uses to transfer larger sums to Pillar Two³¹, in the longer term. Initial reactions from a number of Agriculture Ministers at the Informal Council meeting in Porto on the 16 – 18 September, suggest that Member States, including France, Ireland and Spain, which broadly support the retention of a strong Pillar One, will be opposed to such a rise in the rate of compulsory modulation. Member States such as the UK and Denmark are thought to be in favour of the increases.

Single Payment Scheme payments in the EU-15 may need to be reduced before 2013 as convergence in the level of payments between the old and the 12 new Member States occurs over a period of ten years. The CAP budget was fixed in the 2007 – 2013 financial perspectives, and a declining ceiling, coupled with an increase in the cost of phasing in the Single Payment in all 12 new Member States, means that the time will come when forecast spending will exceed budgetary allocations. The necessity to reduce payment levels, however, may be less pressing than first appeared in 2003 because high commodity prices have reduced the need for export refunds and interventions, and cut the cost of financing Pillar One. It is thought that degressivity may not be triggered until 2009 or 2010 if market prices stay buoyant. The potential accession of Croatia, Macedonia and Turkey also requires consideration, given the large number of farmers in these countries. In the future, it may be argued that the Community’s cohesion policy and the structural funds are the more appropriate tools for assisting farmers in these countries to meet EU standards and to become competitive with more established Member States.

²⁹ Comments of Mariann Fischer Boel at a question and answer session at a conference organised by the Land Use Policy Group, UK, and the Bundesamt für Naturschutz, Germany, on Future Policies for Rural Europe and Beyond – Delivering Sustainable Land Management in a Changing Europe, 19 September 2007.

³⁰ Agra Facts 74-07, 18.09.07.

³¹ The maximum rate of voluntary modulation is 20 per cent and is provided for under Council Regulation 378/2007, OJ L 95 5.4.2007. Along with the UK, this option is used by Portugal.

3.4 Responding to New Challenges

The Commissioner has highlighted that she intends to examine climate change which she recognises as the most pressing emergent challenge to be addressed by Europe's agriculture sector. The Health Check will indicate the role that regulation, rural development policy and crisis management may play in managing agriculture's contribution to, and mitigation of, climate change³². Actions for the agriculture sector with regard to biofuels and water management could also be covered.

The draft proposals are likely to examine ways in which the CAP can be adapted to take account of these broader issues over the period up to 2013. One option may be to include climate change and water management objectives within revised cross compliance requirements. Alternatively, the options for rural development spending could be extended to provide incentives for adaptation to and mitigation of climate change, including support for biodiversity corridors and carbon sequestration, improved water management, and 'the provision of environmental services in the area of biofuels'. Support may also be provided for the development of second generation biofuels. In the context of high crop prices, it is likely that the €45 per hectare payment for bioenergy crops will be abandoned.

4 THE HEALTH CHECK IN A BROADER POLITICAL CONTEXT

4.1 The EU Budget Review

The EU Budget Review formally commences before the Health Check. The EU President, José Barroso, and EU Budget Commissioner, Dalia Grybauskaite, presented a document entitled 'Reforming the budget, changing Europe'³³ on September 12, opening a public consultation that will close in April 2008. The document considers the policy challenges facing Europe, and whether these are adequately reflected in spending priorities. A number of fundamental questions are raised about the added value of European spending, and the effectiveness, efficiency and transparency of budget delivery. The consultation paper opens the way for considerable scrutiny of the rationale for all EU expenditure, and not least, the amount allocated to the CAP and the value for money it provides³⁴. Whilst DG Budget has launched the consultation, at this stage, the extent to which DG Agriculture will engage directly in a CAP based discussion is not known.

³² Mariann Fischer Boel – Farming's role in mitigating climate change. Conference on 'Adapting to Climate Change - launching of the Green paper'. Brussels, 3 July 2007, SPEECH/07/455.

³³ Communication from the Commission, Reforming the Budget, Changing Europe: A Public Consultation Paper in View of the 2008/2009 Budget Review, SEC (2007) 1188, 12.9.2007.

³⁴ See Barroso's pledge for an open EU Budget debate. Financial Times, 13 September 2007.

Following the consultation, the Commission will report on the outcome of the Review in late 2008 or early 2009, concurrent with the ratification of the Treaty and the change in the College of Commissioners³⁵. It is expected to map out the structure and direction of future EU spending and therefore to influence the priorities of the EU's multi annual financial framework for the post 2013 period³⁶. That said, it is almost certain that the Budget Review will not lead to a premature overhaul of the EU budget before 2013. An earlier commitment established by France and Germany in 2002, and subsequently endorsed by the other Member States, set a ceiling for Pillar One of the CAP until 2013.

Budget negotiations tend to be highly charged affairs, and despite months of careful preparation, the final budget agreement can emerge in a fervour of last minute activity. At the EU Summit in December 2005, the occasion on which the last financial framework was agreed, France and the UK engaged in a vociferous debate over CAP expenditure. This resulted in a cut to the proposed rural development budget of around 20 billion EUR and the UK relinquishing some of its rebate³⁷. The Budget Review has its origins in these negotiations, with the then UK Prime Minister, Tony Blair, raising the fundamental question of EU spending priorities. A direct result was a request by the European Council for the Commission to 'undertake a full, wide ranging review covering all aspects of EU spending, including the CAP, and of resources, including the UK rebate'³⁸. The consultative Budget Review, which spans a period of several years, should provide the opportunity for Member States to engage in considered critique rather than the purely dogmatic arguments that tend to characterise EU Summits.

³⁵ It is expected that Barroso will seek a second five year term as President of the European Commission which may constrain his desire to push forward radical proposals for a reform of the budget to avoid offending Member States whose support he will be counting on.

³⁶ The current financial framework and its predecessor are set for a period of seven years, and run from 2007-2013 and 2000-2006, respectively. The financial framework sets a ceiling on expenditure for each budget heading. There are currently six budget headings: sustainable growth; natural resources; freedom, security and justice; citizenship; the EU as a global player; and administration. The European Commission, European Parliament and the Council of Ministers are all involved in drafting the budget. The budget requires the unanimous approval of all Member States before the Parliament has the final say. It needs to vote in favour of the budget for it to be signed into law. There is some speculation that the financing period from 2014 onwards will be set for five years so that it is synchronised with the term of office of the Commission College.

³⁷ The UK rebate was first negotiated by Margaret Thatcher at the Fontainebleau Summit in 1984 and means that the UK receives back around two thirds of its net contribution to the EU budget (Peet, 2005). Many Member States, led by France (who bankrolls around a third of the rebate), have exerted pressure for the rebate to be abolished, stressing that the UK is a more prosperous Member State than it was at the time of the introduction of the rebate. At the 2005 Summit, the UK agreed to reduce its rebate by 20 per cent over the 2007-2013 financial framework.

³⁸ Council of the European Union, Financial Perspective 2007-2013, 19 December 2005.

The EU Budget and the CAP

- In 2007, the total EU budget is 126.5 billion EUR, which equates to approximately 2 per cent of EU public expenditure.
- Of the six budget lines, the greatest proportion is allocated to Sustainable Growth (43.3 per cent of the total budget) and to Natural Resources (44.5 per cent of the total budget).
- The CAP, including agricultural expenditure and direct aids, and rural development, sits within the Natural Resources budget line, along with the Environment.
- Within the Natural Resources budget line, the CAP accounts for approximately 43.6 per cent of the total EU budget, and the Environment, 0.2 per cent.
- EU spending on the CAP amounts to 55.1 billion EUR in 2007.
- Around 77 per cent of this is allocated to Pillar One, and the remaining 23 per cent to Pillar Two.
- The value of Pillar Two is further augmented by national co-financing. Pillar One is not co-financed.

Source: EU Budget 2007, EC (2006).

See Annex 1 for a more detailed breakdown of the 2007 EU Budget by budget line.

Given that the CAP absorbs the greatest proportion of EU expenditure, it is likely to come under considerable scrutiny during the Budget Review and the subsequent negotiations for a post 2013 financial framework. The European Commission is well aware of the criticisms levelled at the size of the CAP budget. In a 2004 document³⁹, the Commission argued for the need to place CAP spending in context, emphasising that the share of the CAP in the total EU budget is falling and that the proportion of EU GDP spent on the CAP is less than one per cent. The Commission, reflecting an Inter-Institutional Agreement with the European Parliament and the Council, is now less defensive and appears willing to engage in a rational and transparent debate about the future role of the policy and its funding.

There are number of topics in relation to EU expenditure on the CAP which are likely to emerge in the debate. If the review truly is to be searching and radical, they all need to be adequately addressed before a decision is taken on the budget, and the vested interests of Member States come to the fore. These questions are raised in section seven.

³⁹ DG Agriculture (2004) The Common Agricultural Policy Explained.

During the forthcoming negotiations, it is fairly certain that pressure is likely to be exerted to significantly decrease or even eradicate direct aids to farmers⁴⁰. The subsequent redistribution of the money currently allocated to direct aids (some 42 billion EUR per annum) is less certain. It is unlikely that all this money will simply be siphoned to rural development expenditure, rather that a large proportion would leave the rural domain. In this regard, a net cut in the overall CAP budget is almost a fait accompli. This raises questions about whether the public interest is advanced by a more liberal market based approach with limited leverage on agricultural activities. One scenario is that it simply exits the EU budget altogether as part of an EU wide drive to decrease overall EU expenditure and the contributions of individual Member States. Another equally plausible scenario is that this money is redirected to the competitiveness and cohesion budget headings, in support of innovation, research, job creation and competitiveness, as set out in the Lisbon Agenda⁴¹. Although some might argue that this should be the overriding focus for EU level action, it should not compromise the vision set by the EU's Sustainable Development Strategy (SDS)⁴².

As well as policy reviews, spending programmes and the principles of sound financial management, politics will come into play in the discussions over the size and orientation of a future EU budget, and the positions adopted by the government of individual Member States will be crucial. In the past, a key delineator of a Member State's position on CAP expenditure has been whether it is a net contributor to, or net beneficiary of, the EU budget as a whole, and how much of the overall budgetary flow is returned to it in the form of CAP payments⁴³. A number of net contributor Member States are keen to reduce their input to the EU budget, which they would like

⁴⁰ For a lucid argument on the rationale for CAP expenditure from a subsidiarity perspective see Grethe, H (2006) Environmental and agricultural policy: What role for the EU and the Member States?

⁴¹ The European Council agreed a strategic goal for the EU 'to become the most competitive and dynamic knowledge based economy in the world, capable of sustainable economic growth with more and better jobs and greater social cohesion' in Lisbon in March 2000 (Presidency Conclusions, Lisbon European Council, March 23 and 24, 2000). The strategy was relaunched in March 2005 following a review which stated little progress had been made. See: Communication from the Commission to the Council and the European Parliament Common Actions for Growth and Employment: The Community Lisbon Programme, COM (2005) 330, 20.7.2005.

⁴² The SDS was first adopted by the European Council in Göteborg in 2001. It was renewed in 2005, following a review, and seeks to set a coherent strategy for the EU to meet its sustainable development commitments. It identifies a link with the Lisbon Strategy. See: Council of the European Union Review of the EU Sustainable Development Strategy (EU SDS) – Renewed Strategy, 9 June 2006, Brussels.

⁴³ Contributions to the EU budget are derived from a variety of sources, the largest of which are payments by Member States based on their respective GDPs. This means that the richer Member States contribute more to the EU budget than they receive through EU spending. Germany is the largest net contributor, with France, UK, Italy, Netherlands, Sweden, Austria and Denmark all making a positive contribution. Among the older Member States, Spain, Ireland and Portugal are net beneficiaries, largely due to the criteria used in the allocations of the CAP budget, including agricultural area, contribution of agriculture to GDP and the size of the agricultural workforce (EurActiv 18.07.05. Who finances the EU budget?).

to keep below one per cent of EU GDP⁴⁴. At present, it just exceeds this figure. Such a standpoint is likely to be at odds with the principle of redistribution to poorer Member States, often cited as an example of EU added value. This is particularly resonant given the recent accession of Bulgaria and Romania, and the possible accession of the current Candidate Countries, Turkey, Croatia and Macedonia, indicating that the EU budget may become rather stretched if net contributors are keen to reduce their input. The renationalisation of agricultural spending is therefore the favoured option of some Member States and has been championed by the European Parliament. DG Agriculture opposes it strongly, fearing that it will undermine the key principles of the CAP.

4.2 The EU Reform Treaty

A mandate for the EU Reform Treaty was agreed by Heads of State at an EU Summit in June 2007, with a draft text forming the basis for negotiations in an Intergovernmental Conference launched by the Portuguese Presidency in July⁴⁵. It reflects the determination of the Member States to move beyond the institutional impasse created by the failed 2004 EU Constitutional Treaty and a desire to modernise a number of aspects of the EU's policy machinery. The Member States have agreed to ratify the Reform Treaty in time for the European elections in June 2009. For some Member States, such as Ireland, a referendum is required in accordance with their constitutional requirements. The ratification process is likely to be politically contentious, and for many Member States a public relations exercise may be required to persuade their citizens of the benefits of the Reform Treaty.

Depending on the timetable and ease of ratification, the Treaty has the potential to have considerable implications for the Health Check and the Budget Review. In the first instance, it could potentially absorb the energies of many Member States and divert interest, albeit temporarily, from the bigger policy questions in relation to the Budget Review. President Barroso has also signalled that securing the approval of the Treaty is the EU's overriding priority, which may serve to distract him from other agendas.

Even if the Health Check is completed by the time of the ratification of the Treaty, the Treaty's implications for future decision making are significant. The most influential element is the extension of the European Parliament's powers in facilitating the adoption of new pieces of agricultural legislation. Once the Treaty enters into force, many, but not all, items of agricultural legislation will be subject to the co-decision procedure. Co-decision means the European Parliament has to vote in favour of the legislation in question for it to enter into law. At present, the alternative consultation procedure applies to agricultural legislation, meaning that the Parliament must deliver its Opinion, through a majority vote, before the legislation can be adopted. However, opposition to a piece of legislation on the part of the Parliament does not preclude the Council from subsequently adopting it. Therefore, in the absence of co-decision

⁴⁴ Peet, J (2005) The EU budget: A way forward. Policy Brief, Centre for European Reform, London.

⁴⁵ Draft Treaty amending the Treaty on European Union and the Treaty establishing the European Community, Note by Presidency of Intergovernmental Conference, Brussels, 23 July 2007.

powers, the Parliament's primary influence lies in its ability to prolong the adoption of legislation by repeatedly postponing the delivery of its Opinion.

The other significant change relates to the balance between, on the one hand, EU legislation agreed through the full co-decision procedure, and on the other, those detailed measures agreed through implementing committees of Member State representatives – the so-called 'comitology' system. Despite a recent reform of the comitology system, the European Parliament still has less influence over implementing legislation than over legislation agreed through co-decision. The Reform Treaty would define more narrowly the circumstances when implementing Regulations or Decisions could be agreed through comitology. The effect of this is likely to mean that a greater proportion of CAP related legislation will have to pass through the full legislative process, giving the Parliament an incentive to delay the passage of controversial Health Check measures until after the Reform Treaty comes into effect.

This change would significantly alter the legislative process, in particular, slowing the adoption of legislation on matters the European Parliament may take issue with. In terms of agriculture, voluntary modulation has been a contentious matter in recent times. The European Parliament voted against the Commission's proposal in November 2006 after a protracted period in which the Parliament delayed the delivery of its Opinion. Modulation will feature in the Health Check, and it is not unreasonable to assume that the Parliament may have strong feelings about the eventual proposal. This means that DG Agriculture, wishing to make best use of the consultation procedure before it expires, will be keen to push through all legislative proposals arising from the Health Check before the Reform Treaty is ratified. However, for its part, the European Parliament could choose to delay giving its Opinion on Health Check related legislation until the Treaty is ratified, thus potentially pushing back the timetable for introducing any changes that arise from the Health Check.

4.3 The WTO Doha Development Round

The WTO provides a backdrop to EU domestic agriculture policy. The Doha Development Round commenced in 2001 and the timetable for its conclusion remains uncertain, although the aim is to reach a political agreement by the end of 2007. Work on the detailed modalities for enacting the agreement will commence thereafter. Progress has been rather uneven to date, however, the Chair of the agriculture negotiations, Crawford Falconer, precipitated a much needed impetus in July 2007, with the publication of a paper setting out the grounds for compromise on the three key areas of the talks: domestic support, market access and export subsidies⁴⁶.

The achievement of any kind of agreement now largely depends on the willingness of the EU, represented by EU Trade Commissioner, Peter Mandelson, the US, officiated by Susan Schwab, and a group of vocal developing countries, namely Brazil and

⁴⁶ Revised Draft Modalities for Agriculture, 1 August 2007, Committee on Agriculture Special Session.

India, to seek out compromise. A number of Member States, notably France, have regularly commented on the Commission's negotiating stance during the Round, arguing for the EU not to exceed its negotiating mandate set out by the 2003 CAP reform agreement and which they argue has already been overstepped.

It appears that an agreement in the Doha Round is likely to be of limited influence to EU domestic policy in the immediate future. It is not thought that it will accelerate the reform process, or go beyond what is already proposed. Even if there is an agreement, which would result in increased market exposure, the abolition of export subsidies, and the further decoupling of CAP payments, the pressure for more CAP reform is likely to be minimal given that the EU has pre-empted the outcome in several respects⁴⁷. It has already publicly committed itself to eliminate export subsidies by 2013. Decoupling was partially introduced as part of the 2003 CAP reform, a process which will be extended still further in the Health Check. The 2003 reform sought to boost the competitiveness of EU farms, with the possible reduction in import tariffs likely to pose a stern test for EU farmers. A reduction in tariffs would exert the most significant impact on extensive beef production, leading to an influx of beef from Brazil and Argentina and a decline in the size of the EU herd. Farmers in marginal areas are most likely to be effected and if decimation of the extensive beef sector is to be avoided, some type of support will be necessary. Proposals include the use of Article 69 of Council Regulation 1782/2003 and the possibility of treating beef as a sensitive product under the WTO framework.

To date, the reform of EU policy has been driven domestically rather than as a response to multi-lateral trade agreements. Pressure to adapt the CAP to changing needs has been exerted by stakeholders within the EU and this appears to be a greater influence on the direction of policy than WTO commitments, which have largely been accommodated for and anticipated by previous rounds of reform and the Health Check agenda. Notwithstanding the trajectory and pace of reform thus far, if there is an agreement which affects agriculture to a significant degree within the Doha Round, a further set of policy amendments may be needed.

The expected sequence of policy events that may serve to influence broader CAP reform is summarised in Figure 1.

⁴⁷ Potter, C (2007) Agricultural Trade Liberalisation and the Rural Environment. Background conference paper for 'Future Policies for Rural Europe 2013 and Beyond – Delivering Sustainable Rural Land Management in a Changing Europe', Brussels, 19 – 20 September 2007, organised by the Land Use Policy Group, UK and the Bundesamt für Naturschutz, Germany.

Figure 1 Expected Timeline of Significant Policy Events

Date	Commission Timetable	EU Presidencies	Biodiversity and Energy Policy	International Events
12 September 2007	European Commission Communication ‘Reforming the Budget, Changing Europe’, SEC (2007) 1188. Launch of consultation process on the EU Budget review.	Portugal (July - December 2007)		
October 2007				Start of US Farm Bill, 2007 - 2012
20 November 2007	European Commission to adopt a Communication on ‘Preparing for the Health Check of the CAP Reform’.		Commission white paper expected on adaptation to climate change.	
December 2007	Consultation on the Health Check proposals.		European Commission to propose framework Directive on renewable energy, to replace and repeal existing Renewables Directive, COM(2004)366 and 2003 Biofuels Directive (2003/96/EC).	UN climate change conference, Bali, Indonesia (COP13). Discussions on climate change targets post 2012. Aim to reach political agreement in the WTO Doha development round.
		Slovenia (January - June 2008)		

Date	Commission Timetable	EU Presidencies	Biodiversity and Energy Policy	International Events
Spring 2008	Adoption of final Health Check proposals and any new or amended legislation by the Agriculture Council.			
April 2008	Close of public consultation on the EU Budget review			
January 2009	EU Budget review – publication of concrete proposals. New Commission College.	France (July - December 2008) Czech Republic (January - June 2009)		
June 2009	Ratification of EU Reform Treaty.	European elections MEPs elected to European Parliament		
2010	Completion of EU Budget review.	Sweden (July - December 2009) Spain (January - June 2010)	EU target to halt biodiversity decline, (Presidency Conclusions, Göteborg European Council, June 2001).	
October 2012				US Farm Bill 2007 - 2012 expires.
December 2012				End first commitment period of Kyoto Protocol.

Date	Commission Timetable	EU Presidencies	Biodiversity and Energy Policy	International Events
December 2013	End of current financial framework.			
2020			<p>Binding goal for renewable energy sources to constitute at least 20% of the total energy mix.</p> <p>Binding minimum target of 10% for the share of biofuels in overall transport fuel mix.</p> <p>EU GHG emissions to be cut by 20% compared to 1990 levels.</p> <p>These targets are set out in an ‘Energy Policy for Europe – The Need for Action’ approved by the European Council, spring 2007.</p>	

5 UNPACKING THE ISSUES

5.1 The Single Payment Scheme (SPS) and Decoupling

The system of direct payments, the SPS, lies at the heart of the contemporary CAP. It embodies a compensatory logic as the payments are offered in place of production linked support. By introducing decoupled payments, some of the weaknesses of the old regime were addressed. In principle, these payments are not trade distorting, they are more efficient in transferring resources to farmers, more transparent and a better platform against which to attach other policy measures, such as cross compliance, than the previous market support measures. Questions about the future of the SPS are, however, numerous and the scheme's continued existence or ultimate demise in the longer term will depend on the relative importance attached to each and their resolution.

It is important first to consider the strength of the rationale underpinning the SPS. Its compensatory mantle requires critical examination, given the provision of these payments to farmers in new Member States who have not been deprived of previous price support under the CAP. Even if this renders its compensatory logic somewhat inconsistent, it is clear that without these payments in the new Member States there would have been blatant inequity and market distortion. As a result, the ten year phase in of the SPS is a clear compromise which in turn raises the question as to whether a time limit should be imposed on the provision of compensation. If, on close scrutiny, the compensatory logic appears weak or compromised, a strong rationale for future intervention needs to be established.

Second, attention should be turned to questions of social equity, and to the extent to which the system generates inequities within and beyond the agricultural community, and thus serves to undermine broader social goals in Europe. Generally, policy seeks to provide income support on the basis of current need rather than to support those who have benefited in the past. The Commission and several governments clearly would prefer a greater measure of equity and a limit on the scale of payments to individual farms, but this has not been easy to reconcile with the delicate distributional issues within the EU and CAP budget. The capping of payments raises a number of issues, including whether capping would confer any benefits for environmental management and what these would be contingent upon.

Third, the extent to which the SPS can be considered to be trade distorting should be considered. On the one hand, there is the economic argument that a truly decoupled payment is independent of farm decision making and whilst providing wealth to the producer, through its capitalisation into land prices, it does not support production. Conversely, producers receive the SPS without constraints on the way in which they apply it to their business and many clearly see it as integral to their farm income. This renders it difficult to argue that a level playing field exists between farmers in Europe and those, particularly in the developing world, who do not receive such a benefit.

Alternatively, it can be argued that the SPS provides compensation for European producers because they are subject to more regulatory and quasi-regulatory constraints than their competitors overseas. In effect, and on the basis of this argument, it is a payment to provide multifunctional goods and services, respect animal welfare standards, and shoulder other burdens unrewarded by the market. If this supersedes the compensatory logic as the primary rationale for this payment, then this needs to be articulated more clearly and fully justified with recourse to detailed evidence of the weight and distribution of these burdens. Indeed, if Europe's fundamental interest is in protecting certain socio-cultural and environmental attributes of agriculture, this would appear to imply a form of 'recoupling' of payments to explicit goals of this kind, with the SPS or its successor directed towards those who 'supply' these multi-functional good and services relative to the size of their payment. Measuring the number and quality of the goods supplied, assessing the cost of provision, and ascribing a value to them all present significant challenges, however. Furthermore, the negotiation of recoupling payments to explicit social and environmental goals would be difficult, not least because the provision of support to promote the continuation of small scale farming - a social goal - clearly contravenes the strictures of the WTO under current definitions of free trade⁴⁸.

The principle of 'recoupling' suggests more convergence between the goals of Pillar One and Pillar Two, irrespective of whether they remain independent or not. It also raises questions about whether full decoupling in all sectors is an appropriate outcome of the Health Check. Whereas it is difficult to see any justification for the continuation of coupled payments in sectors such as cereal production, the reverse argument exists in the case of suckler beef. Decoupled payments provide no incentive to maintain suckler beef animals in the numbers and in those locations where they make a significant contribution to landscape and biodiversity management. Without such support, producers are reliant on LFA and agri-environment payments, both of which are built on a compensatory logic. These payments are intended to cover only the additional costs of complying with environmental prescriptions or to compensate for significant physical handicaps, and are not designed to provide an incentive for keeping the system in place.

The merits of different models of the SPS have been debated at Member State level and choices have been made, although there has been no corresponding analysis or review at the European level. The merits or drawbacks of different approaches as implemented in practice have not been exposed, nor have their impacts been examined. It is arguable that the multi-variant approach to decoupled payments allows the system to be tailored to legitimate national objectives, or conversely, that this diversity reflects national goals and preferences, and thus weakens the rationale for a European funded SPS. To some, this disparity gives rise to concern that the common policy is being renationalised. In the main, environmental interests argued for the regional rather than historic approach to the SPS, which appears more coherent with land management objectives. There is a pressing need to verify whether this preference, based on clear principles, is substantiated with evidence of what is happening in practice in the short period since 2005.

⁴⁸ Under the WTO, the legitimacy of supporting the production of environmental public goods is recognised, but measures to protect small farmers competing in the market are seen to be trade distorting under current definitions.

Cross compliance has become a popular target of criticism from several quarters. Farming organisations frequently complain about bureaucracy, the burden of additional costs and the inequity of double penalties. They often overlook the fact that farms are subject to EU legislation with or without CAP payments and nearly all of the costs arise from the need to comply with the legislation rather than from cross compliance itself. The loss of payments has, thus far, been very limited.

Other critics, by contrast, argue that cross compliance adds little value to improving environmental, food safety and animal welfare standards, based largely as it is on existing measures. In practice, the effects may be substantial but not easy to measure⁴⁹. For example, there has been an apparent improvement in implementation of a range of EU legislation affecting farms in several Member States as a result of cross compliance. The inspection regime and accompanying threat of financial sanctions appears to have improved compliance at the farm level.

The debate appears to be moving towards an argument for an increase in the number of obligations, although this raises a number of questions. First, it is important to consider whether this is, in principle, an effective mechanism for delivering environmental and other outcomes. Cross compliance is best suited to basic, uniform standards that can be easily applied across the whole of the territory in question, irrespective of different agricultural or environmental conditions. It is perhaps less effective at promoting management practices that focus on the delivery of a desired goal, and require targeted, specialist advice and a long term commitment on the part of the farmer. If cross compliance is an effective mechanism for raising standards, and standards could be raised still further through the addition of more conditions, a consideration of the risk of a dilution of their effectiveness is required. It is entirely possible, that if additional requirements are added, such as the Water Framework Directive (Council Directive 2006/60/EC), governments could be prompted to assume a minimalist approach to implementation in order to protect their farmers.

Second, whilst there may be common agreement on the effectiveness of the tool, one must also debate the merits of adding further cross compliance obligations at a time when direct payments seem likely to decline. Expanding the number of requirements seems acceptable so long as the majority of CAP funds are distributed through Pillar One, an argument often referred to as ‘greening the CAP’. If more can be delivered through Pillar One, this helps to free up funding in Pillar Two for more targeted objectives. The use of the Single Payment as a way to reimburse farmers for delivering environmental, animal welfare and other objectives is, however, centrally flawed under the present system, since the Single Payment is calculated on the basis of historic CAP receipts and not according to the cost of delivering these outcomes.

5.2 Market Regimes

Obligatory set aside, currently accounting for about 3.6 million hectares, will be abolished following the Health Check presenting a pressing need to reflect on what

⁴⁹ See, for example, An evaluation of the environmental effects of cross compliance, IEEP 2007, for DG Agriculture (forthcoming).

measures might be taken to capture the environmental benefits of set aside and to collect evidence on the effectiveness and efficiency of alternative options. The case for a purely environmental land management obligation applying to all farms that receive significant public support requires discussion. ‘Ecological Compensation Areas’, adopted in Switzerland since 1999, provide one model in a highly supported system⁵⁰ and support for such a scheme is provided by the European Environment Agency and NABU, the German partner for Birdlife International⁵¹. Alternatively, the US ‘Conservation Reserve Program’ may represent another option which could be implemented in Pillar Two. Once set aside is abolished it will be difficult to reestablish leverage over agricultural land use unless an alternative is already in place. Indeed, in the absence of such a large scale intervention of this kind in European land use, Europe’s ability to meet objectives for biodiversity, and specifically the target to bring a complete halt to biodiversity loss by 2010 as stipulated in the EU Strategy for Sustainable Development (CEC, 2001), may be severely compromised.

The Commission has signalled its intention to bring an end to milk quotas by 2015 which is likely to trigger considerable restructuring in the milk sector, with fewer larger farms and more regional concentration. The social and environmental impacts arising from this restructuring will need to be considered along with an exploration of the measures that will be needed to mitigate any adverse effects⁵².

5.3 Pillar One and Pillar Two

As their objectives converge, the desirability of maintaining the two separate Pillars of the CAP requires critical assessment, as compared to an alternative scenario which postulates a radical change in architecture for 2013 and beyond. The relative simplicity of Pillar One and its reach in terms of the leverage it creates on almost all farmers confers it with certain advantages, and it could, in principle, be recoupled to new objectives. Many Member States are attached to the symbolism of Pillar One and may be more comfortable with a reform that retained this envelope and the

⁵⁰ To qualify for area-related production subsidies, Swiss farmers are required to manage seven per cent of their farm as an ECA, or 3.5 per cent in the case of specialised cultures. Features that qualify as ECA include hay meadows, litter meadows, traditional orchards and hedgerows and management prescriptions are defined. Studies have demonstrated that this measure has produced biodiversity benefits, particularly in litter meadows and hedgerows, and that they contribute between 50 and 80 per cent of the diversity of farmland plants and arthropods, although they comprise only 20 per cent of the total UAA. See, for example, Herzog *et al.*, (2005) Effect of Ecological Compensation Areas on floristic and breeding bird diversity in Swiss agricultural landscapes. *Agriculture, Ecosystems and Environment*, **180**, 189 – 204; Knop *et al.*, (2006) Effectiveness of the Swiss agri-environment scheme in promoting biodiversity. *Journal of Applied Ecology*, **43**, 120 – 127.

⁵¹ See, for example, NABU (2005) *Nachwachsende Rohstoffe und Naturschutz: Anforderungen des NABU an einen naturverträglichen Anbau* www.nabu.de/imperia/md/content/nabude/energie/biomasse/1.pdf; European Environment Agency (2006) How much bioenergy can Europe produce without harming the environment? Report 7/2006, Copenhagen.

⁵² An evaluation of the environmental impacts of milk quotas is currently underway by Alliance Environnement, for DG Agriculture, contract no. 30 CE-0067379/00-89, due for publication in May 2008.

tradition of 100 per cent EU funding, even in the wake of dramatic change in policy content. Since Pillar One reaches almost all farmers it provides an entry point for pursuing EU policy objectives such as sustainability that could be lost if it were replaced by a more selective system based on voluntary agreements, as in Pillar Two.

A counter argument is that the clear objectives that have been built up in Pillar Two are now absent under Pillar One, particularly with respect to the environment. It lacks the discipline of the programming approach, the prior assessment of needs, a system of monitoring and evaluation, regular review periods, national contributions to costs and other attributes of a more targeted approach. Pillar One is rooted in an historical logic less attuned to the future agenda, and this is set to increase further if we enter a period of high commodity prices, as seems likely. Furthermore, it is directed solely at agricultural producers, unlike Pillar Two, which, in principle at least, reaches a wider rural community. Pillar Two also brings together agriculture and forestry in a way that is helpful in an era when climate change concerns suggest a more integrated approach to land use.

Many governments have been reluctant to increase the scale of funding for Pillar Two very rapidly in the past, but it is the extent to which this constitutes a barrier to developing this strand of the policy in the future that is, as yet, unclear. If the more administratively cumbersome procedures in Pillar Two are a major impediment to greater use of this model, ways of simplifying delivery without losing the benefits of targeting and clear objectives need to be developed.

The expected proposals in the Health Check are relatively contained, but it seems clear that the debates being unleashed are fundamental and deep-rooted. The positions taken, by governments and civil society, will be a function of different agendas, and the relative importance attached to economic, social and environmental issues. The following section discusses the key players.

6 KEY PERSONALITIES

Mariann Fischer Boel, the Commissioner for Agriculture, is the figurehead for the Health Check and will continue in this role. She has adopted an unusually open style but has less experience and less time to establish political credibility than Fischler enjoyed at the time of the Mid Term Review. He was a wily negotiator and blended vision with an acute sense of political tactics. Her comments indicate that she will fight for the continuation of the Pillar One budget at a substantial level, she has signalled that she believes that Pillar Two represents the future of the CAP, although she has refrained from articulating a clear vision of what Pillar Two may look like in the medium term. It is understood that she is not seeking a second term, and her lack of personal investment in the future debate is, in some ways, evident. Klaus-Dieter Borchardt, her Deputy Chef de Cabinet, is also a high profile figure. The analyses of policy options are being led by John Bensted-Smith, Director of the Economic Analyses and Evaluation Unit of DG Agriculture.

The European Parliament will be formally consulted on the Health Check proposals along with the Member States. The Agriculture and Rural Development Committee of the European Parliament, which is chaired by Neil Parish, a British Conservative and a farmer, will be responsible for leading the debate and for coordinating the Parliament's response in the subsequent negotiations. The Committee will appoint a rapporteur who will be responsible for drawing up the committee report, which will recommend whether the proposals are accepted or whether amendments are sought on the basis of the evidence presented. Rapporteurs are often the most lobbied focus points in the whole of the EU's decision-making process. DG Environment is anticipated to take significant interest in several issues of the Health Check, notably set aside, cross compliance and the rate of modulation. They will have some purchase on the Commission's collective view, and the capacity to win one or two significant points on an agenda of this scale.

Whilst consultation on the Health Check proposals has not formally commenced, in recent speeches, notably at the Young Farmer's Conference held in Brussels in April 2007, the Commissioner has actively solicited the views of farming organisations, in an attempt to instigate an engaged dialogue on the Health Check and the Budget Review⁵³. After November, the focus will move more to the positions of Member States and the NGOs will need to work actively on the key players including France, Germany, the UK, Spain, Italy and others. Work on the Health Check and the broader debate about CAP reform has started in some Member States and papers have been published by the UK Treasury and Defra; a joint position statement was issued by David Miliband, UK Secretary of State for Environment, Food and Rural Affairs and Paolo de Castro, Italian Minister of Agriculture on the 19 March 2007 signalling that the Italian and British share a common position on the future of the CAP; the Swedish Government (document not in the public domain); the French Ministry of Agriculture, the Committee for European Integration Department of Analyses and Strategies, Warsaw, Poland⁵⁴; and the German Federal Ministry for the Environment, Nature Conservation and Nuclear Safety.

Although they may not be directly consulted on the Health Check proposals, civil society groups have the capacity to influence the framing, content and nature of the debates. Discussions over the future of the CAP have begun to be conducted in a variety of fora, including blogs⁵⁵ and the publication of vision papers⁵⁶. This needs to

⁵³ See, for example, Mariann Fischer Boel's speech at the Young Farmer's Day, Brussels, April 2007. [Giving a voice to the future of farming in the EU](#). SPEECH/07/225. Ulster Farmer's Union, Belfast, May 2007. [The future of the CAP: Planning starts now](#). SPEECH/07/269.

⁵⁴ See for example: HM Treasury and Defra, 2005. [A vision for the Common Agricultural Policy](#). London, UK; Defra, 2007 [Communiqué on Italian and British shared positions on the future of European agriculture policy](#); French Ministry of Agriculture. [La PAK, un modèle équilibré à mieux comprendre](#); Bukiewicz, W., Grochowska, R. and Hardt, L., 2007. [The future of agricultural policy in light of the EU budget review in 2008/2009](#). Material for discussion. Office of the Committee for European Integration Department of Analyses and Strategies, Warsaw; [Nature: Our Future. How rural regions benefit from environmental protection and conservation and how EU agricultural policy could contribute](#), Federal Ministry for the Environment, Nature Conservation and Nuclear Safety (BMU), 2007, Berlin.

⁵⁵ See, for example, <http://caphealthcheck.eu/>; <http://commonagpolicy.blogspot.com/>.

be maintained as an extended campaign over the medium term, given the prospect of more fundamental questions being posed in the Budget debate and in the run up to 2013.

7 TOWARDS 2013 AND BEYOND

The Health Check and the European Budget Review will stimulate a wide ranging debate which will set the framework for future CAP reform. Substantive changes to the CAP are widely anticipated following the conclusion of the current financial perspective in 2013. The 2014 – 2020 financial perspective is, at present, a fairly blank ledger sheet, as there is no guarantee that historical patterns of expenditure will provide a precedent for future spending. This was clearly indicated in the comments of the EU Budget Commissioner at the launch of the consultation on the EU Budget review. The CAP will be in competition with other demands on the EU budget, with some stakeholders assessing the pros and cons of supporting farming as opposed to the environment more directly, or whether innovation, research, job creation and competitiveness emerge as the overriding focus of EU level resources.

It is almost a *fait accompli* that the total CAP budget will be cut in real terms in 2013 as Europe's agriculture sector continues on its trajectory of greater market orientation. Unless there is a significant shift in funding from Pillar One of the CAP to Pillar Two through higher rates of modulation coupled with co-financing from the Member States, EU spending on agriculture will experience a downward trend. The scale of the cuts is not yet clear. However, farm incomes, the viability of farm businesses of different sectors and sizes, and the volume and intensity of production will each be affected, with concomitant environmental and social impacts. The impact on the competitiveness and viability of farm businesses will be differentiated and small, marginal farmers will be most vulnerable. It seems likely that global demand for cereals and bioenergy crops will remain strong, for several years at least, and as a result, commercial arable farms will benefit. Many will be viable with reduced levels of support or none at all. Livestock producers will face correspondingly higher feed prices and it is less clear how demand for their products will hold up.

The burden of adjustment to a changing market and less well resourced Pillar One can be expected to fall most heavily on smaller farms, livestock producers and those outside the arc of good arable land. These are the producers who are less influential in the agricultural lobby but who are most sensitive in social and environmental terms. Many of the arguments for intervention in agriculture in developed countries such as those in the EU, rest on the social and environmental benefits of appropriate forms of production. If the producers who are most closely associated with these benefits are in the process of further decline, and land is drifting into arable production, the purpose of agricultural support will be further questioned. For those reasons it seems

⁵⁶ Birdlife International's 'Vision for the EU Common Agriculture Policy', is due to be launched on the 3 October 2007.

unwise to assume that the CAP will provide support for virtually all categories of producer as it does at the present time.

Furthermore, the long tradition of supporting agricultural production at a European level and leaving responsibility for forestry largely to the Member States, with the exception of some limited aid within Pillar Two, may look less appropriate in a world in which carbon capture and storage is a growing preoccupation. There is a European interest in preventing deforestation, encouraging appropriate rotation lengths and cutting regimes, and in well judged afforestation. Whereas there is unlikely to be an appetite for introducing CAP style subsidies for the forestry sector, there is a good argument for bridging the divide between agriculture and forestry in European policy and addressing land use in a more integrated way.

At a global scale, negotiations within the WTO historically have taken place with the EU, the US and occasionally the Cairns Group in the front row, with most other countries occupying the seats behind. This too is changing, with Brazil, China and India now playing a central role in the prolonged process of seeking an agreement in the WTO Doha Round. As time passes, developing countries can be expected to take a more prominent position in the negotiations and their agenda will be pursued with vigour in disputes and challenges to the existing order as well in any new multilateral agreements. For the EU, this implies further decoupling, further concessions on market access, potentially lower levels of support to domestic producers and a stronger focus on demonstrable public goods where support is provided.

In short, the uncertainties for the CAP beyond 2013 are not confined to the anticipated decline in the budget. Some other engrained assumptions about the policy need to be treated with caution or outright scepticism. Agriculture policy is in a time of flux, as demonstrated by some of the recent debates in the US leading up to the 2007 – 2012 Farm Bill. While it would be naïve to overestimate the commitment of European governments to prioritise social and environmental concerns over the traditional drivers of agricultural policy, the political logic of such a trajectory is difficult to dismiss.

A new CAP for beyond 2013 will need to address the agenda of the time. If it is to be robust, however, it is evident that it will require the mobilisation of compelling arguments in relation to four key points: the case for agricultural exceptionalism to justify the receipt of significant European public funds; the existence of clear objectives for a future CAP or common rural policy which are tied to rural needs; a critical examination of whether existing or new measures fit these objectives; and the expenditure needed for those measures that are retained in a future CAP or the policy that emerges from it. In other words, is public intervention in agriculture justified? If so, should the policy be common? Should it be agricultural? What are its objectives? And how much will it cost? These questions will dominate thinking in the run up to 2013.

The case for agricultural exceptionalism rests on a number of arguments, most of which fall broadly under the heading of ‘public goods’. Although not strictly a public good, one of the most frequently deployed relates to the issue of food security. Support for production is worthwhile to prevent consumers and the food industry from relying on the market in a world of increasing uncertainty. Under this line of

argument, food is unlike other commodities in that it is entirely essential, and a premium for security is as prudent as other forms of insurance. The power of this argument depends greatly on the perceived and actual risks of relying on the markets and the commodities in question; security of supply for grain, for example, is more important than for beef, avocados or wine. Furthermore, security can be achieved in a variety of ways, for example, by retaining a minimum level of grain in strategic stores. If markets become tighter and more volatile, possibly exacerbated by a less predictable climate, security of supply will gain legitimacy as an objective. Nonetheless, it applies only to a limited band of commodities, the producers of which seem most likely to benefit from rising grain demand.

As a result of its dominance in territorial terms, agriculture in Europe has a disproportionate social and environmental footprint on land use, the environment, animal welfare, public health and rural livelihoods. It gives rise to both negative and positive externalities, such as biodiversity loss, water pollution and greenhouse gas emissions on the one hand, and climate change mitigation and the provision of environmental goods, on the other. Certain types of farming, notably High Nature Value farming systems and those in Natura 2000 sites, are beneficial for biodiversity, and have many positive externalities associated with them, in relation to soil, water and landscape. Environmental public goods and services are also provided in the wider agricultural landscape and are of critical importance in the most fragmented and degraded areas. Field margins, fallow land, hedgerows, and semi-natural and woodland patches are important in enhancing functional connectivity in intensive agricultural landscapes, providing important habitats, feeding grounds and ecological corridors to facilitate species dispersal. In addition, agriculture and forestry together have the potential to contribute significantly to mitigating climate change, through increased carbon sequestration in soils and vegetation, and the displacement of fossil fuels through the use of agricultural waste products in the production of biogas and the growth of feedstocks for second generation biofuels.

The ambition for the future CAP should not simply be to reduce the externalities of agriculture and agricultural policy, but to shift them from the negative to the positive end of the spectrum. With this transition, comes the provision of environmental and social public goods and thus an underlying rationale for support for agriculture. The public goods argument for exceptionalism is stronger, however, if the focus is on those agricultural sectors and land uses that do generate public goods, including forestry, rather than on all forms of production, including intensively housed livestock where such public benefits are outweighed by costs.

Social and environmental objectives are linked but are not the same. In respect to socio-cultural concerns, an aim is to buttress certain areas and sectors from the full impact of restructuring, especially in those areas where the culture is rooted in conditions of production. Farmers often embody this cultural heritage and if they are displaced by a more competitive structure, this will represent a socio-cultural rather than an economic loss. Such an argument, however, can become inflated into a defence of all agricultural employment, which is an entirely different and indefensible position. It will be a considerable challenge to define social objectives in a coherent way that capture genuine public concerns and preferences without degenerating into unreconstructed agricultural protectionism. Experience with LEADER and other targeted rural development measures needs to be brought to bear in this question.

Environmental objectives are perhaps more compatible with the logic of the WTO but are not entirely straightforward. One set of concerns is embedded in agriculture itself and another extends to the wider rural landscape. The first set includes the values placed on production systems and practices that themselves produce environmental benefits, such as traditional farmed landscapes and features, species rich grassland and HNV grazing systems, organic farming and more radical approaches such as permaculture. This is the 'joint production' of public and private goods and the aim of intervention is to secure these because the market presents inadequate incentives. Over time the market may change, for example, through a willingness to pay for the full costs of joint production, and the need for intervention may alter. At present, however, the prospect is for further decline of the more traditional HNV sector and further intensification in agriculture, resulting in a clear need for substantive intervention.

The second strand is the provision of sustainable rural land management by actors other than farmers. These activities include currently, woodland, nature reserves, new forms of carbon sequestration, floodplains and water supply zones, forms of recreational and even abandoned land. These benefits can be defined in different ways but rarely can be regulated into existence. Some level of provision can be generated through the market but given the intense and growing pressures on land use much of the provision will need to be incentivised more directly. The environmental objectives are thus partly agricultural and partly rural in nature, mirroring the focus of Pillar Two rather than Pillar One.

Increasingly, a number of commentators are questioning whether a centralised policy, in the form of the CAP, is appropriate in a changing reality, and argue that arguments of economic efficiency do not support the current allocation of responsibilities between the EU and its Member States. Whilst a clear case exists for the assignment of responsibility to the EU level in a common market, in the context of the declining economic relevance of market price support and the changing nature of direct payments, it is argued that the assignment of the responsibility for the funding and administration of direct payments to the EU level conflicts with the subsidiarity principle. In terms of rural development policies, disproportionate centralism and interventionism may constitute higher transaction costs and result in regulation not being aligned to national or regional priorities. Many rural development measures are of a local nature in terms of the problems they address, the public good preferences that lie behind them, and the measures that have been developed. In addition, the cost of providing a resource that is non uniform in its distribution varies significantly between regions and common rules can be cumbersome. Given these arguments and the strong historical bias in the distribution of the current Pillar Two budget some commentators have concluded that Member States themselves should be responsible for the design, implementation and funding of rural development measures.

However, a common agricultural or rural policy, funded in part from European monies, can be justified on a number of counts. There is a high proportion of land under farming, forestry or nature management which is subject to a substantial layer of common policy objectives and EU legislation. Many of these objectives reflect the transboundary character of certain environmental issues associated with farming. A common framework allows the EU to exercise a legitimate role in compensating for

unequal costs in the provision of European public goods, whether these are protected areas within Natura 2000 or forests that need to be maintained to lock up carbon. Where regions or countries make a disproportionate contribution there is a means of sharing this burden more equally. Member States have entered joint commitment with respect to the Kyoto Protocol and the subsequent need to mitigate emissions and increase carbon sequestration. They are now in the process of negotiating further commitments on the production of renewable energy, including biofuels. A common framework for addressing land use issues linked to agriculture and forestry in particular has clear value in these circumstances. As farmers and other land managers receive a higher proportion of their income from activities other than conventional commodity production, questions of competitive advantage become more important. A common framework provides a measure of transparency and does not have to impose uniformity.

There is growing support for widening the scope of the CAP so that the focus is on a broader array of issues than are currently addressed under Pillar Two. Agriculture and forestry remain at the core of the policy field but with less focus on commodity production. In the debate leading up to 2013, there needs to be a fresh look at the needs of rural areas and the expectations of those areas from the rest of society. Rural policy represents a cluster of related concerns and issues that should not be lost in the more diffuse world of regional policy. Land use questions need to be brought closer to the forefront of policy but without embarking on an EU role in land use planning, which is best addressed at a more local scale. Does this lead one to conclude that the issues of the future are sustainability, North- South equity, the development of poorer regions in Europe, the protection of biodiversity and a more equitable distribution of the budget? If so, the more selective approach of Pillar Two seems a potential platform for adapting to most of the new agenda, but it would need to be harnessed to public benefit in a more rigorous way than at present.

ANNEX 1. THE 2007 EU BUDGET

Budget Line	in billion €	% of total
Sustainable Growth	54.9	43.4%
Competitiveness, including:	9.4	7.4%
Education and training	0.9	0.7%
Research	5.5	4.3%
Competitiveness and innovation	0.4	0.3%
Energy transport networks	1	0.8%
Social policy agenda	0.2	0.2%
Cohesion, including	45.5	36.0%
Convergence	35.3	27.9%
Regional competitiveness and employment	9	7.1%
Territorial cooperation	1.1	0.9%
Natural resources, including:	56.3	44.5%
Environment	0.2	0.2%
Agricultural expenditure and direct aids	42.7	33.8%
Rural development	12.4	9.8%
Freedom, security and justice (including fundamental rights and justive, security and liberties, migration flows)	0.6	0.5%
Citizenship (including culture, media, public health and consumer protection)	0.6	0.5%
EU as a global player, including:	6.8	5.4%
Pre-accession	1.3	1.0%
European neighbourhod	1.4	1.1%
Development cooperation	2.2	1.7%
Humanitarian aid	0.7	0.6%
Democracy and human rights	0.1	0.1%
Common foreign and secutiry policy	0.2	0.2%
Stability instrument	0.1	0.1%
Administration, including:	6.9	5.5%
European Commission	3.3	2.6%
Other institutions	2.6	2.1%
Compensations to new EU countries	0.4	0.3%
Total	126.5	100.0%

Source: EU Budget 2007, EC (2006)

GLOSSARY

Common Agricultural Policy (CAP)

The set of policy principles, regulations and payment mechanisms adopted by the European Union that consolidates efforts in pursuing agricultural goals such as promoting reasonable pricing of food products, a fair standard of living for farmers and stable agricultural markets.

Council of the European Union

The Council of the European Union (the ‘Council of Ministers’ or the ‘Council’) is the EU’s main decision making institution. It comprises the ministers of the Member States and thus is the EU institution in which the governments of the Member States are represented. The Council, together with the European Parliament, acts in a legislative and budgetary capacity. It is also the lead institution for decision making on the common foreign and security policy (CFSP), and on the coordination of economic policies (intergovernmental approach).

Cross Compliance

The current mandatory form of cross compliance was introduced under the Mid Term Review of the CAP in June 2003. It is a system requiring farmers to observe certain standards in the areas of environment, public, animal and plant health and animal welfare in return for direct payments under the Single Payment Scheme.

In order to achieve cross compliance, and to avoid any reduction in the total level of direct aid received, the farmer must concur with 19 Statutory Management Requirements (SMRs) and a number of standards aiming to ensure the ‘good agricultural and environmental condition’ (GAEC) of agricultural land.

Decoupling

The process of severing the link between the subsidy a farmer receives and the production or price of a specific farm product. This was a key principle of the 2003 CAP reform.

Doha Development Round

The Doha Development round negotiations were launched by ministers of the World Trade Organisation (WTO) member countries in November 2001 with the aim of further liberalising global trade and extending the benefits of globalisation to developing countries.

European Commission

The European Commission (formally the Commission of the European Communities) is the executive branch of the European Union. It operates in the method of a cabinet

government with 27 Commissioners, one for each country of the EU, led by a Commission President (currently José Manuel Barroso). The present Commission took office in late 2004 and is serving a five year term. The Commission is responsible for proposing legislation, implementing decisions, upholding the Union's treaties and the general day-to-day running of the European Union.

European Parliament

The European Parliament is the democratic arm of the EU as its members are directly elected by the people of the Member States. Through the Members of Parliament (MEPs), the EU's citizens can be involved in the making of Community policies and laws affecting their daily life. Each revision of the Treaties has seen an increase in the power of the European Parliament in relation to the other institutions. At present, the European Parliament is firmly established as a co-legislator and is involved in finalising Community Directives, Regulations and other policy. It is composed of 732 members and is directly elected every five years in each Member State. The Parliament meets in plenary session in Strasbourg and Brussels. The powers of the Parliament depend on the decision-making procedure being used.

Good Agricultural and Environmental Condition (GAEC)

In order to achieve cross compliance and to avoid any reduction in the total level of direct aid received, the farmer must concur with a number of standards aiming to ensure the 'good agricultural and environmental condition' (GAEC) of agricultural land (as well as Statutory Management Requirements). GAEC consists of a total of eleven standards relating to the protection of soils and the maintenance of habitats.

Modulation

The mechanism by which EU farm spending is transferred from market related support payments to rural development policy measures (i.e. from Pillar One to Pillar Two of the CAP).

Mid Term Review (MTR)

In 2002, a Mid Term Review of the EU's Common Agricultural Policy was initiated and concluded in June 2003. As an outcome of the MTR, a substantial reform of the CAP was initiated. The key components of this reform were: decoupling of direct aid and production; the introduction of cross compliance; and transfer of money from Pillar One of the CAP to Pillar Two via 'modulation'.

Pillar One

The Agenda 2000 reforms established two 'pillars' of CAP expenditure. The market and income support measures are referred to as Pillar One. This covers direct payments to farmers and market related subsidies, including those under the CMOs, such as export subsidies. Pillar One receives approximately 77 per cent of the CAP budget.

Pillar Two

In the Agenda 2000 reforms, rural development policy was confirmed as the 'second pillar' of the CAP, with the purpose of improving the economic, social and environmental situation of all rural areas. It receives approximately 23 per cent of the CAP budget. A dedicated fund, the European Agricultural Fund for Rural Development (EAFRD), provides the financial backbone to Pillar Two and was set up in 2005.

Presidency

This is the chairmanship of the European Union Council. The Presidency rotates every six months among the Member States, according to a set schedule. The Presidency chairs most Working Groups, the Committee of Permanent Representatives (composed of the Member States' ambassadors to the EU) and meetings of the Council of Ministers. The Presidency plays a key role in setting the Union's agenda and working towards an agreement.

The Member State holding the Presidency of the European Union Council is responsible for bringing the items on the political calendar to a successful conclusion. Each Presidency lasts for six months, and is expected to act independently, in the interest of the EU. Two fledgling Member States, and one Member State, will hold the Presidency during the critical period of the Health Check and Budget Review. Slovenia will be the first of the 2004 new Member States to act as President, from 1 January 2008, and is likely to progress the consultation procedure and bring legislative proposals to the Council. There may be a number of sensitive issues to resolve, and it is possible that certain elements will be pushed back into the second half of 2008, at which point the Presidency rotates to France (1 July 2008). France will have a strong interest in the outcome of the Health Check, and it will be interesting to see how it handles its Presidency. Responsibility then transfers to the Czech Republic, another new Member State, on 1 January 2009, for the potentially politically volatile Budget Review portfolio.

Set Aside

Set aside is the temporary removal of arable land from production in response to policy requirements rather than agronomic considerations. It was initially introduced in the EU in the 1980s to limit the production of cereals. Since 1992 it has been obligatory, and producers are required to set aside a certain percentage of their declared areas in order to be eligible to receive direct payments.

The rate of obligatory set aside was initially decided every year, but in 1999/2000 it was set permanently at 10 per cent. In the new Member States that opted for the Single Area Payment Scheme, farmers are exempted from the obligation of set aside. In September 2007, the Commission proposed that the rate of obligatory set aside be set at 0 per cent for 2007/2008.

Single Area Payment Scheme (SAPS)

Option offered to the 12 new Member States to aggregate all the direct payments into one single ‘basket’ (national financial envelope) to be distributed to farmers on the basis of a single criterion which is the number of hectares of the holding. All of the new Member States, except Malta and Slovenia, use this scheme.

Statutory Management Requirements (SMRs)

In order to achieve cross compliance, and to avoid any reduction in the total level of direct aid received, farmers must concur with 19 Statutory Management Requirements (as well as GAEC requirements). The SMRs are based on pre-existing EU Regulations and Directives. They relate to environmental, animal identification and public and animal health requirements.

Single Payment Scheme (SPS)

The scheme delivering direct aid payments to farmers in the EU-15, Malta and Slovenia, introduced following the MTR of the CAP.