



ENVIRONMENT AND RURAL DEVELOPMENT COMMITTEE

AGENDA

8th Meeting, 2004 (Session 2)

Wednesday 17 March 2004

The Committee will meet at 10.00 am in Committee Room 2

1. **Inquiry into the implementation of CAP Reform:** The Committee will take evidence from—

Panel 1

John Kinnaird, President, NFU Scotland;
Becky Shaw, Crofting Environment Officer, Scottish Crofting Foundation; and
Stewart Jamieson, Board Member, Scottish Organic Producers Association

Panel 2

Peter Cook, Retained Consultant, Scottish Agricultural College; and
Dr Janet Dwyer, Reader in Rural Studies, University of Gloucestershire.

2. **Renewable energy in Scotland:** The Committee will consider a paper from the Convener regarding the Enterprise and Culture Committee's inquiry into renewable energy in Scotland.
3. **Subordinate legislation:** The Committee will consider the following negative instruments—

the Sea Fish (Prohibited Methods of Fishing) (Firth of Clyde) Order 2004, (SSI 2004/55);

the Domestic Water and Sewerage Charges (Reduction) (Scotland) Regulations 2004, (SSI 2004/68);

the Less Favoured Area Support Scheme (Scotland) Regulations 2004, (SSI 2004/70); and

the Sea Fishing (Restriction on Days at Sea) (Scotland) Amendment Order 2004, (SSI 2004/81).

Tracey Hawe
Clerk to the Committee
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The following papers are attached:

<p><u>Agenda Item 1</u></p> <p>Submission from NFU Scotland</p> <p>Submission from the Scottish Crofting Foundation</p> <p>Submission from the Scottish Organic Producers Association</p> <p>Submission from Peter Cook</p> <p>Submission from Dr Janet Dwyer</p> <p>A paper from the Committee adviser and SPICe is attached (<i>for members only</i>)</p>	<p>ERD/S2/04/08/1a</p> <p>ERD/S2/04/08/1b</p> <p>ERD/S2/04/08/1c</p> <p>ERD/S2/04/08/1e</p> <p>ERD/S2/04/08/1f</p> <p>ERD/S2/04/08/1g</p>
<p><u>Agenda Item 2</u></p> <p>A paper from the Convener is attached</p>	<p>ERD/S2/04/08/2a</p>
<p><u>Agenda Item 3</u></p> <p>The Sea Fish (Prohibited Methods of Fishing) (Firth of Clyde) Order 2004, (SSI 2004/55)</p> <p>The Domestic Water and Sewerage Charges (Reduction) (Scotland) Regulations 2004, (SSI 2004/68)</p> <p>The Less Favoured Area Support Scheme (Scotland) Regulations 2004, (SSI 2004/70)</p> <p>Extract from the Subordinate Legislation Committee's 9th Report 2004 (<i>to follow</i>)</p> <p>The Sea Fishing (Restriction on Days at Sea) (Scotland) Amendment Order 2004, (SSI 2004/81)</p>	<p>ERD/S2/04/08/3a</p> <p>ERD/S2/04/08/3b</p> <p>ERD/S2/04/08/3c</p> <p>ERD/S2/04/08/3d</p> <p>ERD/S2/04/08/3e</p>

SUBMISSION FROM NFU SCOTLAND

IMPLEMENTATION OF CAP REFORM

Summary

1. In summary the views of NFU Scotland on CAP Reform in Scotland are:
 - a) Farmers welcome the opportunity that CAP Reform brings, allowing them to operate in a more market-orientated environment, making management decisions based on what is best for their businesses and reflecting what their farms are capable of, rather than the requirements of subsidy schemes.
 - b) NFU Scotland welcomes the decision by the Scottish Executive to use the historic basis for the Single Farm Payment. This will provide stability in the level of support to individual businesses, needed to allow them to adjust to the more market-oriented environment in which they will operate under the new CAP regime.
 - c) However, NFUS believes that in the long-term, a transparent and objective basis for support must be maintained. NFU Scotland is of the view that a Land Management Contract model, as envisaged in the Forward Strategy For Scottish Agriculture, recognising and rewarding the provision of social, economic and environmental benefits should be the long-term objective. NFUS believes the choices made by the Scottish Executive in how CAP Reform is to be implemented are compatible with this objective.
 - d) The Scottish Executive need to clarify what it is hoped a beef national envelope will achieve. The Scottish beef industry does not need a national envelope if it is less than effective, creates anomalies, cannot be withdrawn, or creates more bureaucracy.
 - e) NFU Scotland believes that in the long term, a beef support scheme permitted under Scotland's Rural Development Plan offers a more sustainable support mechanism that will allow the social, economic and environmental benefits of suckler cows to be recognised.
 - f) NFU Scotland believes that Scotland should be making use of the full scope of rural development measures to achieve the aims of the Forward Strategy for Scottish Agriculture. Whole farm Tier 2 Land Management Contract (LMC) type measures could be developed to achieve this.
 - g) There are a large number of outstanding issues and details that remain to be addressed following the announcement on CAP Reform implementation in Scotland.

Historic Single Farm Payment

2. The historic based model of decoupling will provide the stability in the level of support to individual businesses required to allow them to adjust to the more market-oriented environment in which they will operate under the new CAP regime. The alternative of a flat-rate area based approach advanced by some would not have provided this stability or provided a transparent and objective justification for support in the long term. NFU Scotland is of the view that a Land Management Contracts model, as envisaged in the Forward Strategy for Scottish Agriculture, recognising and rewarding the provision of social, economic and environmental benefits, should be the long-term objective. The choices made by the Scottish Executive in how CAP Reform is to be implemented are compatible with this objective.

Beef National Envelope

3. NFU Scotland believes that the same principles of decoupling should apply to the beef sector as in all other sectors, but that the situation is complicated by the fact that payments such as Beef Special Premium have become integrated into the price paid for store cattle. The indirect effect of past support schemes will not be reflected in the Single Farm Payment received by the seller of store cattle. It is widely believed that there could be changes in the distribution of cattle production and a reduction in cattle numbers in many fragile areas of Scotland. This is a situation that NFU Scotland believes must be addressed. However, there appear to be several objectives for the beef national envelope and NFUS is not convinced all these objectives can be delivered through one scheme. The intention to use a beef national envelope requires more investigation. The Scottish beef industry does not need a national envelope if it is less than effective, creates anomalies, cannot be withdrawn, or creates further bureaucracy.
4. NFU Scotland believes that, in the long-term, Scotland's Rural Development Plan offers a more sustainable support mechanism that will allow the social, economic and environmental benefits of suckler cows to be recognised.

Land Management Contracts

5. Much wider use of the Rural Development Regulation (RDR) should be made in Scotland. NFUS favours a review of the Scottish Rural Development Plan, with a view to introducing Land Management Contracts. The announced provisional modulation rate of 10%, depending on what happens to match funding, should act as the trigger for such a review. With a new Scottish Rural Development Plan in 2007, effective dialogue with the EU Commission is required to ensure that the new Rural Development Regulation offers the flexibility to enable a move

in Scotland to use Land Management Contracts that reward the social and economic as well as environmental benefits of agricultural activity. As we move towards a more market-orientated environment, the RDR has the potential to help support those benefits of farming which are not paid for by the market place, to provide a real choice for farm businesses and crofts and thereby benefit the countryside and wider rural economy.

CAP Implementation Issues

6. There are a large number of outstanding issues and details that have not been answered by the announcement on CAP Reform implementation in Scotland. The answers to many of these points will not be available until the implementing regulations are published. The main issues for crofters and farmers will be:
 - The appeal arrangement required for the situation where there is disagreement between farmers or crofters and SEERAD over the Department's assessment of the value of their single farm payment.
 - Who will be eligible for the National Reserve and how value for entitlements will be determined. New entrants to farming, those who have developed their businesses and those who have substantially changed their business will look to the National Reserve for an allocation of payment entitlements.
 - How entitlements will be calculated where an individual has held land in different regions of the United Kingdom.
7. In the first year of the Single Farm Payment, farmers will experience a cash flow problem as a result of the change to a single payment compared to receiving support through a number of different support schemes paying out at different times of the year. There is provision in the CAP reform package for a 50% advance payment where, due to exceptional conditions, farmers face severe financial difficulties. We believe that the move from multiple payments to a single payment will cause severe financial difficulties for many farm businesses and therefore the option to make an advance payment should be used.

Rural Development and Structural Funds

It is not clear from the EU Commission's proposal for the EU financial framework for 2007 to 2013 how much money will be available for the new Rural Development Fund. However, although the increase in Rural Development spending in the new 10 EU countries may make it difficult to get Scotland's disproportionately low share of funding corrected, this should still be our objective.

SUBMISSION FROM THE SCOTTISH CROFTING FOUNDATION

IMPLICATIONS OF THE IMPLEMENTATION OF CAP REFORM IN SCOTLAND

Policy overview

“The single greatest impediment to developing a multi-functional agriculture is the lack of a coherent funding system that explicitly links public funding to the production of public goods.”^[1]

This reform of the Common Agricultural Policy and the rural development measures arising as a result of it have far-reaching implications for rural Scotland. Yet these decisions must not be merely confined to the ‘industry’ – with £360M per annum of direct support payments, the stake of the taxpayer in the future of agriculture and rural areas must be recognised. The Scottish Crofting Foundation believes that public money should support multi-functional agriculture. By this we mean, agriculture which delivers not only a product that the market wants, but in doing so, also directly or indirectly provides a range of public benefits:

- Environmentally sustainable farming systems,
- management and enhancement of important habitats on moorland, wetland, rough grassland and grassland, arable crops and stubbles, machair and scrub and an opportunity for the many species that depend on this diversity of management,
- a varied and attractive landscape – important for leisure, access and of course the tourism industry and
- vibrant rural communities.

The policy direction within the Executive’s Forward Strategy for Scottish Agriculture - agriculture at the heart of rural development, contributing to a high quality environment and with support focused towards with ‘multi-functional’ farming - demands doing more than just trying to maintain the status quo. The status quo has, over recent decades, seen agricultural production become increasingly concentrated in a decreasing number of agricultural enterprises, intensification of production in some areas and losses or declines in valuable high nature value, extensive agricultural systems in others. For many High Nature Value farming systems, this is make-or-break time – this reform either providing a nail in the coffin, or a bright future for environmentally sustainable agriculture.

It is likely that agriculture in hill, upland, peripheral and fragile areas will decline under a decoupled support system with attendant losses of rural community, rural business and infrastructure and a negative effect on the environment unless there is significant direction of support from other measures put in place. In particular, the role of the agri-environment and the Less Favoured Area Support scheme in supporting continued agricultural activity in these areas is crucial.

^[1] The Scottish Executive: ‘Custodians of Change’, Para 100

It is clear from the high-level commitments of the Partnership Agreement that there is an intention to ensure that the public money spent on agriculture delivers support in an integrated way to ensure environmentally sustainable farming systems and healthy rural economies.

Agriculture in the crofting area is fragile, yet agricultural management is linked with the high environmental status of the area, a diverse and valued landscape and retention of rural communities in some of the most remote areas in Scotland. Important non-market goods are being delivered by high nature value agricultural systems in the Highlands and Islands for as little, in some areas, as £9 / Ha of public money. This reform is make-or-break time for many of these economically fragile systems.

The implication of implementation decisions announced and detail to be developed

Decoupling

In our response to the CAP reform consultation, the Scottish Crofting Foundation supported decoupling of support payments **subject** to safeguards being put in place to support and retain valuable systems in the north, the west and fragile hill and upland areas. We believe that decoupled agricultural support has the *potential* to lead to more environmentally sustainable farming systems and should eliminate much of the regulatory and administrative burden faced by farmers and crofters and to enable greater market orientation.

However, we recognised at the time that decoupling and the market rationalisation it will bring, create risks for agriculture in more remote and upland areas and for smaller agricultural units. It is **imperative** that a decoupled system of support payments is combined with measures, which properly recognise the additional costs and difficulties associated with agricultural activities in least favoured areas, and recognise and retain agricultural systems, which contribute to the high environmental value of the uplands and peripheral areas of Scotland.

Historic basis

The Scottish Crofting Foundation welcomes the Deputy Minister's recognition in the 12th February announcement and subsequently in discussion before this committee that the historic basis of payments is not justifiable in the longer term and should be reviewed at the earliest opportunity. The Minister recognised that this is not a long term solution, but part of a process of evolution: this view is shared by the SCF.

Direct support payments are currently very unevenly distributed, with the more intensive systems in receipt of the largest support payments, while the more extensive receive less. This system, as of course is to be expected, bears no relationship to the delivery of public goods – it would be surprising and entirely by chance if it did. What this means, in effect, is that the management of agricultural land is rewarded at enormously different levels at the moment – without any

reflection on the public benefits delivered by any particular system. In Fife, the average payment per hectare for every hectare of agricultural land is £181; in Lothian the figure is £144. Whereas, in Shetland land management is carried out for only £24/Ha, in the Highland area this falls to £15/Ha and in the Western Isles, the figure is £9. We do not believe it to be the case that a farmer in Fife delivers 20 times the public benefit of a crofter in the Western Isles.

There is also a marked discrepancy between the nearly 10,000 smallest producers (or 47% of Scottish producers) who between them currently receive 4.2 % of the total budget and the 389 largest farming enterprises, which while accounting for 1.9% of Scottish producers, receive 17.3% of the total annual budget. While these differences may be expected in a production-based system, they become increasingly difficult to justify once the link with production is broken. Hence the reason that the SCF and others have been advocating and continue to advocate a gradual move away from a purely historic payment model.

A particularly serious concern in the Highlands and Islands is the tradability of entitlements, giving rise to fears that trading of massively varying entitlements could create a situation analogous to the housing market. This could lead to local people and young people being outbid by those with much higher entitlements per hectare and land use and communities stagnating if entitlements are activated against land with a low level of minimum activity, such that the investor may not need to live in the area. We welcomed recognition that this issue will need to be considered further and issues such as ring fencing or a stronger enforcement of crofting legislative controls are currently being discussed.

National envelope

The Scottish Crofting Foundation welcomes the decision to use a National Envelope for beef to mitigate against the effects of decoupling in the short term and ensure protection for systems which are important for the protection and enhancement of the environment. Many extensive and high nature value farming systems, with a good cattle/sheep mix are found in upland and remote areas and we believe it is crucial to retain and encourage mixed agriculture in these areas through targeted use of the beef National Envelope. Many of these systems are very fragile and will be lost unless immediate and effective support is made available when payments are decoupled.

A study conducted by the Scottish Agricultural College for HIE^{2[2]}, showed the strong correlation between cattle and cropping - suggesting that retention of cattle in an area will lead to retention of mixed agriculture with a cropping element. The study predicted that without a National Envelope targeted at the hill, upland and fragile areas, a significant drift of cattle from the currently mainly store- producing areas in the West to the currently predominantly finishing areas in the East should be expected.

Although we would eventually see support for cattle-keeping in marginal and peripheral areas being directed through Pillar 2 mechanisms, given the fragility of

^{2[2]} 'HIE Masterclass Report', Oct 2003, Peter Cook and Andrew Copus

these systems, we believe that the National Envelope measure offers an immediate opportunity to safeguard and retain worthwhile agricultural systems while deliberations over the future shape and integration of RDR measures takes place. It would be significantly more expensive to try and reintroduce these high value systems once they are lost. Retaining what is good is a priority of environmental management – the precautionary principle demands that we do not allow environmentally important systems to be lost.

Modulation

The Scottish Crofting Foundation believes that Pillar 2 and the Rural Development Regulation offer significant scope to support multi-functional agriculture. The efficacy of Pillar 2 to effectively support rural development in the Highlands and Islands depends upon revisions of the SRDP to create a system which suits the needs of agriculture in the Highlands and Islands in supporting and maintaining agricultural systems which deliver numerous public goods.

It is on account of our concern over existing mechanisms and their targeting that we advocated a franchise of 5000 Euros be applied to national modulation as well as to the European proportion, which recognises the rural development importance of small units.

In the new policy context, post decoupling, there is no longer a strong economic rationale for agricultural activity in many hill, upland and peripheral areas, and on small units, which face significant diseconomies of scale. It is imperative, in the discussions on the future priorities and allocation of rural development funding that the real costs of continuing beneficial agricultural management in the marginal areas is taken into account.

As an example, say a unit runs 20 cattle and 400 sheep in an extensive and environmentally sustainable system. Subsidy receipt would roughly be £10,800. A fairly typical return on this enterprise in a peripheral or upland area might be in the region of £4,500. In a decoupled system, the rational economic actor will try and reduce his business, within the scope of cross compliance measures until he can keep as much of that missing £6300 as possible. If society believes that his continued environmentally sustainable activity is worthwhile, logically we would be required to support him to the tune of at least £6300 to bring him to break-even level were he to continue his current beneficial practices.

It must be appreciate that the maintenance of existing good systems will cost significantly more under a decoupled support system than has previously been the case.

SUBMISSION FROM THE SCOTTISH ORGANIC PRODUCERS ASSOCIATION

1. Overview

- 1.1 The Scottish Organic Producers Association (SOPA) is pleased to submit its written evidence to the Committee in support of the Inquiry panel hearing on 17 March 2004. This evidence is based on our recent response to the Scottish Executive's consultation document on CAP reform measures (January 2004).
- 1.2. Like all other organic certification bodies, SOPA is primarily interested in the future impact which the CAP reform measures will have on the scale and diversity of Scotland's organic farming industry. This needs to be considered alongside the implementation of the Scottish Executive's current Organic Action Plan for Scotland, launched a year ago, which now includes the imminent introduction of a more substantial and wide-ranging level of support for producers via the Organic Aid Scheme(OAS). SOPA's general view is that the CAP reform measures can potentially be used to further enhance the OAS. We also believe that over time the strategic emphasis of the CAP reform measures on the wider application of less intensive and more environmentally responsible farming methods will in turn lead to a larger and more diverse network of organic producers and processors across Scotland. This may well take between 5 and 10 years to materialise, but is something we would strongly welcome.

2. Decoupling:

- 2.1 In general terms, SOPA supports the Minister's decision to opt for a fully decoupled system of farm support across Scotland. As far as organic production in general is concerned, we have not been convinced of the case for partial re-coupling or the use of a National Envelope for ring-fencing some or all of the existing Pillar 1 subsidies. We recognise that decoupling and the introduction of the single farm payment system means that changes to cropping and stocking levels necessary for organic production should no longer incur farmers in financial penalties (through the loss of historic subsidies) as a result of converting. This should also give organic farmers the freedom to respond more pro-actively to market signals and gain greater recognition for the animal husbandry and environmental benefits they are creating as part of a package of 'public goods' supported by Pillar 2 funds.
- 2.2 SOPA welcomes the fact that the cross-compliance basis of the single farm payment system will incorporate a new definition of land as being in 'good agricultural and environmental condition'. We will re-confirm this in our response to the Executive's latest consultation on the future definition of GAEC, which we understand will be based on an existing EU framework covering soil erosion, levels of organic matter, soil structure, and minimum level of maintenance. As a registered organic certification body (reference UK3 on the DEFRA register), SOPA recommends that in finalising the new cross compliance requirements, including the new GAEC definition, the Executive makes due reference to the organic certification standards used by ourselves and other organic certification bodies. In this context, organic certification lends itself well to measuring systems of good practice, and by law the standards used by OCBs have to be backed by EU regulation. The SOPA standard is currently being upgraded to comply with the requirements of the UK Accreditation Service as specified in EN45011.
- 2.3 Concerns associated with decoupling have been expressed regarding its future level of public acceptability and potential problems arising from a possible perceived

degradation of the countryside landscape arising from the ending of subsidised production in favour of a more 'natural' system such as organic farming. In its first annual report to Parliament on the implementation of its Organic Action Plan the Scottish Executive has re-affirmed its commitment to double the area of arable and improved grassland in organic conversion or production to 30% of Scotland's total organic land area by 2007. In addition, latest statistical evidence from the Soil Association indicates that consumer demand for organic produce in the UK is still rising at 10% per annum and in 2003 exceeded £1 billion in turnover for the first time. As a member of the Executive's Organic Stakeholders Group, SOPA hopes that future annual reports on the Organic Action Plan will cover the economic and environmental benefits of organic husbandry in terms of the impact of decoupling on agricultural land management. One particular indicator used in this monitoring should be the higher retention of farm labour on organic farms located in vulnerable rural communities.

2.4 The main issue for SOPA members arising from decoupling is that the future single farm payment system should be applied from 2005 in an equitable manner. SOPA has argued that there must be sufficient flexibility over the use of the reference period for calculating single farm payments. Those organic farmers who were in conversion during the 2000-02 period (i.e. the vast majority of all Scottish organic producers) and whose stocking levels were subsequently at their lowest and their cropping systems in a maximum state of flux while in receipt of Organic Aid Scheme support in that period should not be penalised in comparison with others who opted for conversion more recently. SOPA therefore welcomes the availability of an alternative reference period of 1997-99 and the potential use of a financial National Reserve for Scotland to compensate for commitments in this earlier period, as provided for under Article 40 of the CAP reform Agreement regulations. We note that SEERAD is likely to consult organic sector bodies further on the National Reserve issue, assuming that the EC Implementing Regulations allow discretion at a Scottish level.

2.5 We recognise that in some geographically discrete areas of Scotland, e.g. Shetland, it might be feasible to adopt an area-based approach to calculating single farm payments where a relatively uniform pattern of organic farming exists with no transitional/hardship cases justifying the use of an alternative reference period for individual farm holdings. However, whether in Shetland or elsewhere, SOPA would urge full consultation by SEERAD with the local Organic Producers Group in taking this forward. There is no guarantee that all Producers Group members would accept an area-based uniform hectare reward for cross-compliance, especially given that this is essentially a redistribution of historic subsidies awarded on a very different basis.

3. Dairy Decoupling

3.1 SOPA has endorsed earlier submissions made to SEERAD by the Scottish Organic Milk Producers Association (SOMPA), in particular the request that the derogation on the reference period for single farm payments be applied to the dairy sector in the same way as to others.

4. Set Aside

4.1 We understand that although the CAP reform Agreement requires entitlement to single farm payments to take account of arable hectare under set aside, organic farmers who manage the entirety of their land holding organically will be exempt from this. This concession is apparently based on the assumption that the potential environmental benefits of set-aside are being achieved in other ways through organic husbandry. From 2004 the Organic Aid Scheme will, for the first time, offer 5 year on-going

payments to any registered organic producer on the basis of demonstrable environmental benefits arising from their farming operation. As yet, there has been no discussion at Organic Stakeholders Group meetings on the relevance of this new level of OAS support to the set-aside requirements of the CAP reform measures. SOPA would be delighted if the future dispensation from set-aside applicable to single farm payment entitlement on arable land covered by entirely organic farming operations were extended to partially organic also.

5. National Modulation

- 5.1 In common with other organic certification bodies, SOPA attaches the highest importance to the application of national modulation as provided for under the CAP reform measures. We believe this is fundamental both to enhancing the scope of Pillar 2 support for rural development measures in general and widening and strengthening the use of Organic Aid Scheme grant support in particular. SOPA therefore welcomes the Minister's decision to opt for the maximum 10% national modulation, in addition to the prescribed EU modulation, to generate the resulting additional funding. We note that under this Option, after taking account of matching Treasury funding, the projected total amount of rural development funding available to the Executive will amount to £87.4 million in 2005 rising to a maximum £96 million in 2007.
- 5.2 At present, Scottish Executive policy is to treat any support for Scotland's organic industry as part of its wider agri-environment strategy. Thus, on 18 August 2003 the Minister's announcement of future improvements to the Organic Aid Scheme was given a subsidiary role to a number of new rural development measures within the Environmentally Sensitive Area (ESA) Scheme and Rural Stewardship Scheme (RSS), even though the OAS changes were considerably more complex.
- 5.3 In its written response to the Executive's earlier consultation (May 2003) on the future development of the Organic Aid Scheme, SOPA commented :

"The main issue of concern to SOPA is whether the revised OAS will help or hinder potential organic producers making the business decision to convert in the first place and whether they will remain in organic production without OAS support. Unlike the Rural Stewardship Scheme which relates very largely to achieving one-off change in land management defined by an end point in time, OAS is tied to an ongoing annual production process with very specific windows during the calendar year for starting to convert specific livestock or cropping regimes."

We are pleased to note that SEERAD is now more aware of this issue, and the introduction of ongoing payments in 2004 will offer some measure of new assistance. However, SOPA remains concerned that in 2004 we will see a further short-term reduction in the total number of organic certification bodies' licensees in Scotland, based on current trends among producers coming to the end of their 5 year OAS conversion grants. In 2003, out of 47 SOPA licensees resigning, withdrawn, or transferring to another OCB, 75% had decided to discontinue organic farming. A key factor in this trend has been the reduced level of grant available to hill farmers with unimproved grassland under the provisions of the new OAS compared to the old. While this may be seen as evidence that the Executive's intention to shift more organic production to lowland largely-arable farms is already working, SOPA remains concerned that the detailed application of the new OAS will deter a significant number of farmers from going organic.

- 5.4 Recent findings from research work commissioned in 2003 by SEERAD, coupled with the current work of the Scottish Food and Drink Organic Action Plan funded by Scottish Enterprise and involving all of the OCBs in Scotland, has highlighted the need to strengthen the infrastructure of Scotland's organic industry if the goals set in the Executive's own Organic Action Plan are to be realised. Recent innovations such as the new 'organic zone' on the www.scottishfoodanddrink.com website will help strengthen the supply chain between organic producers, processors, retailers and consumers, but SOPA's view is that better marketing of Scottish organic produce requires a more sustained level of research and investment over the long term. This is borne out in a recent report to SEERAD by SQW / ADAS (March 2004)
- 5.5 Concern exists among *bona fide* organic producers who are currently fully converted that the CAP reform measures could easily lead to a major distortion of the market for Scottish organic produce - thereby directly threatening the livelihood of those established farmers relying on organic premiums - as many non-organic farmers are attracted into going organic through a combined package of Pillar 1 (decoupled single farm payments) and Pillar 2 (OAS and RSS) funding. SOPA strongly recommends that SEERAD should address this issue in safeguarding the interests of existing producers. We suggest that for all new organic entrants a sliding scale equalisation is applied to any combination of single farm payments and OAS over a given number of years, giving a strong weighting of OAS ongoing payments in favour of producers who are already fully converted.
- 5.6 SOPA also recommends that under CAP reform the opportunity to extend the scope of OAS through additional national modulation offers real scope for the Executive to introduce new incentives for producers to invest in on-farm processing and marketing of organic produce. Evidence collected in 2003 for the SQW / ADAS research project commissioned by SEERAD demonstrates this need. Scotland's organic supply chain is underdeveloped and highly vulnerable. The Scottish Organic Milk Producers Association, formed in 2003, comprises 26 members but represents the entire production of wholesale organic milk in Scotland; significantly, it is the only sector specific body aiming to develop better markets for Scottish organic produce. There is no equivalent body for producers of Scottish organic beef, lamb, venison, cereals, or fruit and vegetables. The same deficiency applies to Scottish organic processors. If the CAP reforms are meant to create a more dynamic rural economy, more organic farmers should be encouraged to add value to their produce, and in SOPA's experience establishing new organic farming co-operatives will only succeed if their membership gives equal recognition to processors as well as producers.
- 5.7 Taking all these factors into consideration, SOPA recommends that the Executive should work through the Organic Stakeholders Group in developing a number of models for extending and refining the scope of the Organic Aid Scheme. This should be linked directly to the use of enhanced rural development funding coming on stream with effect from January 2005 via additional national modulation. An agreed set of recommendations from the Organic Stakeholders Group based on the modelling exercise should go to the Minister this year, and SOPA would like to see this given a high priority.
- 5.8 SOPA welcomes this opportunity to discuss with the Committee the recommendations and comments contained in this written evidence. The CAP reform measures are of huge significance for the long term restructuring of farming across Scotland, and SOPA is fully committed to engaging in this process.

SUBMISSION FROM PETER COOK

Inquiry into the Implementation of CAP Reform in Scotland

Introduction

- I am an agricultural economist and business adviser with 18 years experience of carrying out economic impact assessments (especially on CAP change) and advising farmers, advisers, public bodies and policy makers. I have been an adviser to two House of Commons Committees. I am also a farmer.
- Specific work on the current CAP Mid Term Review;
 - Study into the impact of the proposals for agriculture in the HIE area. Included looking at the impact of use of National Envelopes, Partial Decoupling, etc. Study highlighted economic impacts (regional output, expenditure and jobs) of different options. Included feedback sessions for farmers and other stakeholders throughout the Highlands.
 - Presentation of study results to EU DG Agriculture livestock policy staff in Brussels.
 - Presentations to two seminars in Brussels, assessing impact of the MTR reforms for peripheral areas of Europe.
 - Contribution to studies into impact of the reforms on east coast Local Authority areas and SW Scotland.
 - Part of 3 man SAC team preparing assessment of pro's and con's of each implementation option, relative to full decoupling, for SEERAD agricultural policy staff prior to launch of their consultation exercise.
 - Assessment of impact of the proposed reforms for feed companies, the beef sector, arable farming.
 - Presentation of details of the reforms to a number of farmer meetings.
 - Calculation of the impact of the reforms for a range of individual farmers.

Impact of the MTR Reforms on Scotland: Key Points.

- Our study suggests that over a 10 year period, **full decoupling** would result in the following changes in Scotland and the HIE area.

	% Changes 2001-2010	
	Full Decoupling Scenario	
	<u>HIE</u>	<u>Scotland</u>
No. of Holdings	-1.8	-2.7
Av. Holding size	+1.4	+1.9
Improved Grass	+3.3	+10.0
Total Crops	-36.5	-27.0

Beef breeding cattle	-13.4	-5.0
Feeding cattle	-14.9	-10
Dairy cows	-30.7	-22
Breeding ewes	-16.4	-10
Total sheep	-26.2	-19.3
Total pigs	-27.6	-5

- These changes would reduce the value of agricultural output from Scotland and the Highlands by 10% and 20% respectively. Full time worker equivalents would fall by 19.1% and 14.9% respectively.
- What is happening? Very simply stated, breeding livestock numbers fall in the most severely disadvantaged areas. This in turn reduces the need for cropping in those areas and the remaining stock are spread over a larger area to be managed under more extensive low cost systems. In the better areas of Scotland cereal and oilseed cropping declines because without an attached area payment it is not competitive. This land is turned over to grass and absorbs some of the stock which moves off the hills. The fall in stock numbers over Scotland as a whole is not enormous, but there is a change in the regional location of those stock.
- Why might this happen? If subsidy is decoupled from animals and acres the unsubsidised profitability of the enterprise becomes much clearer. Individual farmers now have the option of retaining their historic subsidy levels without being required to maintain their previous cattle, sheep and crop levels. Lots of beef cows and ewes in the hills and uplands are not profitable (without subsidy) and at least some farmers will decide to cut numbers. Given time however farmers in the less disadvantaged areas of Scotland may find ways to keep breeding stock at lower cost. The creation of a large decoupled payment may allow some farmers to retire/semi-retire/re-structure thus allowing others to expand. This may help facilitate the major shift in systems and stock numbers inherent in the projections above.
- Note that the decline in dairy cow numbers is not strongly related to the MTR proposals, but to the long term decline as a result of steadily increasing yields and lower milk prices. The MTR deal is broadly neutral for dairying: the milk price fall (due to intervention price cuts) is expected to match the new direct payment.

The Impact of the Beef National Envelope: Key Points

- The maximum beef envelope for Scotland is around £19M. This can only be applied to schemes which enhance quality or the environment, though how this might work is still unclear.
- If the envelope were applied to every beef cow in Scotland the payment would be roughly £39 per cow. If applied only to LFA cows it would be £47 and if only applied to HIE area cows it would be around £141 per cow.

- The study for HIE looked at two options – 1. Applying the envelope across Scotland and 2. Applying only to HIE cows. The results of this for the Scottish beef herd were projected as follows.

Full decoupling -5%

“All Scotland” BNE -0%

“HIE Only” BNE -8%

- The application of an envelope to all Scottish cows may only have a small impact on slowing the decline in numbers. £40 per cow (compared to typical current Suckler Cow Premium of £150 per head) is not really enough to have a significant effect on long term decisions, yet it is likely to create a significant bureaucratic load.
- The application of the envelope to only HIE cows has a significant effect. In the Highlands it completely stops the decline in cow numbers (a fall of less than 1% compared to almost –15% under full decoupling). However, for Scotland as a whole it might lead to a bigger reduction in cow numbers than under full decoupling. Non HIE producers see their historic beef payments cut by 10% but don't get anything back. As a result they make more radical changes to their beef systems than under full decoupling, where they at least receive their full historic payments. The better areas of the Highlands (Moray Firth, etc) soak up cows from lowland Scotland, but lack capacity to make up for the decline in the rest of Scotland.
- In summary, the Beef Envelope has limited scope as a tool for maintaining the scale of the Scotch Beef Industry. It can have an impact on specific regions or types of production if applied in a targeted fashion.
- If the aim is to maintain cattle in the most peripheral areas of Scotland for environmental and social reasons, then the best tool may be a targeted scheme created under the Rural Development regulation and funded by a modest level of modulation.

Farm Level Reaction

- The impact of the MTR changes depend on how farmers react to the concept of decoupling.
- Take beef cow producers as an example. With subsidy, a typical hill cow producing a weaned calf may generate a gross margin of around £200. When subsidy is removed the cow makes zero margin (and hence a loss once fixed costs are deducted). What will farmers do when subsidy is not attached to the keeping of the cow?

- In the short term probably nothing. Producers will eat in to their Single Farm Payment and, as long as the overall picture is a profit, they will make no change.
- In the medium term “overcapacity” cows and acres of crop may go. Many producers expanded numbers and acres to capture more subsidy. Where this resulted in high costs (extra buildings rented, lots of feed bought in, high land rents paid) these extra cows and acres may be chopped to make the whole business more profitable.
- Also in the medium term some farmers will look for new ways of running enterprises, to get the cost of wintering cows or of growing an acre of crop, down to competitive levels.
- In the long term there will be restructuring; some producers will go out of production while retaining their Single Farm Payment, while others will find ways to expand profitably, without subsidies, on to the acres released.
- We have worked through options for many producers post-decoupling and the results are often stark. One farmer with 220 cows and 700 ewes expects to increase his annual profitability by approximately £50,000 per annum by getting rid of his cows and two employees. He saves all the costs of maintaining that number of cows, but retains their historic subsidy. Despite the loss of calf sales and a sizeable reduction in his LFASS income, the potential financial benefits are large. This “downsizing” by one business creates an opportunity for others as his financial projections include contracting out the 202 Ha of land once used by the cows at a fairly modest £70 per Ha.
- A critical part of the essential restructuring of the industry will be the ability of producers who retire or “semi-retire” to find simple ways to contract out their land to those who wish to expand. If they want to keep their Single Farm Payment they cannot rent out their land as their entitlements go with the land. SEERAD’s view on what will be acceptable is critical here.

**SCOTTISH PARLIAMENT ENVIRONMENT AND RURAL
DEVELOPMENT COMMITTEE INQUIRY INTO CAP REFORM:**

**EVIDENCE FROM PANEL MEMBER, DR JANET DWYER
Reader in Rural Studies, University of Gloucestershire**

1. I appreciate the invitation to give evidence to this important inquiry. The recently agreed reform of the Common Agricultural Policy is likely to have important impacts and implications for Scottish agriculture and the wider rural economy and rural environment of Scotland. However, at present there remain many uncertainties about precisely what these might be, and how government policies can best be designed to make the most of the opportunities offered by reform as well as seeking to minimise any adverse impacts.
2. This evidence covers the three main strands of the recent Ministerial announcement concerning the options so far decided, for implementing CAP reform in Scotland. These are:
 - **Decoupling** and the choice of a historic basis for award of the new Single Farm Payment to producers as well as the likely form of cross compliance conditions attached to it;
 - The use of the **national envelope** measure to support 'quality calves' for beef production as a means of directing additional aid to suckler cow producers;
 - The decision to increase voluntary **modulation** to enable a combined EU and national rate of 10% modulation to apply by 2007, in order to facilitate the launch of the new Land Management Contracts across Scotland as part of a revised Scotland Rural Development Programme, beyond 2006.

In addition, a short note is added about the importance of continued monitoring and analysis of farmer adaptation to the policy changes and the need to support the sector in getting to grips with, and making the most of, the opportunities that it presents. Finally, I have annexed to this submission a paper written jointly by myself and Professor Henry Buller, in January this year for a conference in Hereford which, although referring to issues in England, examines some of the broader implications of CAP reform that will be directly relevant to the remit of the Scottish Parliament's Inquiry.

Decoupling

3. It is wholly in line with the UK's established support for decoupling during the negotiation of the reform package that all countries in the UK have now chosen to implement fully decoupled payments from 1 January 2005, whereas a range of other EU Member States will be opting for only partially decoupled support, or delayed decoupling. In the UK context, by choosing Single Farm Payments based upon historic receipts alone, the Scottish Executive has opted for a *relatively conservative system* which minimises the redistribution of aid between individual producers, in the short term. This contrasts with the hybrid system proposed for Northern Ireland where a small proportion of payment will be redistributed on an area basis, and the transitional hybrid system proposed for England, where the

basis of payment will be shifted gradually from a historic to a flat-rate area basis over 8 years.

4. The economic models that have examined the implications of full decoupling on agriculture around the UK have all suggested that it will tend to reduce the profitability of production systems across the country, and that in particular, beef production will see the greatest decline in profitability among livestock sectors, while in the arable sectors, wheat will be relatively more profitable than other crops but all crops will have reduced profitability to the extent that significant areas of current crop land would no longer be worth cropping. When considering the implications of these models for Scottish agriculture it is important to remember that the models share a number of characteristics that mean their predictions are likely to be more dramatic than actual impacts, in reality. These are:
 - The models tend to discount the ‘cushioning’ effect that the SFP will undoubtedly have on farmers’ interpretations of profitability and in particular, when considering the profitability of their existing farming systems. Although in strictly economic terms, the SFP should not affect production decisions it seems likely to cushion farmers’ immediate need to adjust current production systems in line with their changed profitability. Also, the models assume that farmers change their systems in order to maximise their profits, whereas it is well-known in practice that this frequently doesn’t happen. Thus we might expect that in reality, the sharp changes in profitability indicated by the models will not stimulate immediate or widespread farming change. One Herefordshire farmer, commenting on this at a conference that I helped to organise in January, said the following:
‘at present, my farming operation is barely profitable – we spend all year getting further into the red, and then the IACS cheque arrives at the end of the year and we go back into the black. I can’t see that things will be any different after the reforms – we will spend all year getting into the red and then the SFP payment will arrive, and keep us going again. I’m not convinced the change will really give us many more options’.
 - The models are generally static ones that do not consider likely changes in market conditions for various products over the coming few years. These changes include a number of expected trends in particular sectors that will affect their profitability as well as currency fluctuations that have impacts both on the levels of SFP that farmers will receive, as well as their relative competitiveness in export markets across the rest of Europe. In this context, there are reasons to expect improved prospects for certain UK sectors in the coming 1-2 years, notably in the beef sector, as BSE export restrictions are lifted, the Over Thirty Months scheme for disposal of older stock is removed and markets generally regain more of the confidence that they lost in the late 1990s. For this reason, we should be a little cautious in interpreting the models as a sign that suckler beef production across much of Scotland will disappear, following decoupling.
5. In opting for a historic payment basis, the Scottish Executive has chosen a system that will be simplest for farmers to cope with in the short term because their receipts should not significantly change. However, the system is likely to

become both more complicated to administer (for farmers and government officials) as time goes on and land changes hands between producers, as well as becoming more clearly difficult to justify, because payments per hectare of land will differ greatly between individual producers and yet the basic requirements for receipt of these payments will not vary in the same way. The Minister has acknowledged these possibilities in his statement and indicated that the Executive is seeking to promote a review of the new systems across the EU within the next few years. It seems likely that such a review would be supported by DG agriculture within the Commission, also, so this appears reasonable. However, if there is no review and further reform by 2010, then the Scottish system may prove both unwieldy and increasingly lacking in public support.

6. The proposed system for cross compliance, including the new thinking on 'good agricultural and environmental condition' (GAEC) appears to make a positive move in the direction of ensuring that all eligible land management increasingly incorporates good environmental practice. However, the gaps between current practice and the carefully calculated and thorough approaches described in the suggested GAEC definition point to a significant need for farmers to be able to access appropriate advice and training over the coming year, if they are to be able to take up this significant challenge. The Executive needs to move swiftly to promote widespread awareness among farmers of the new conditions as they are being agreed, and to offer help where necessary to enable farmers and others involved in day-to-day farm management operations to become proficient in the many procedures and techniques they will need to use if they are to ensure they meet GAEC from 1 January 2005.

National Envelope

7. The decision to use this in the beef sector to help support suckler systems needs to be taken forward with care, in view of potential changes in the market situation for beef producers in Scotland. If markets improve, it would be undesirable for the payments to encourage over-production of calves from suckler herds on marginal land since this could have environmental disbenefits as well as knock-on effects upon the longer term profitability of farming structures in these areas. Further instability could result if dairy producers decide to move more into calf production as milk prices decline, across Scotland. These considerations point to the need to ensure that the NE decision can be made temporary and kept under constant review, once implemented, to ensure that it is achieving the desired effects in economic and environmental terms. Ideally, the NE option should be phased out over time and replaced by appropriately tailored environmental management payments under the RDP, as its budget expands beyond 2007.

Voluntary Modulation

8. This decision is, in my view, very welcome. It is probably the single most important factor in helping to boost the Scottish Executive's wider public policy objectives as set out in the partnership agreement. The Pillar 1 reforms could promote more sustainable farming through cross compliance and benefits for the wider rural economy if farmers can use their SFP increasingly to think about diversifying and producing more quality products. However, it is only through Pillar 2 of the CAP – the rural development programmes – that these specific changes can be explicitly targeted and supported through policy instruments.

Thus it is important to link the changes in direct payments with an immediate and significant commitment to actively promote rural development and sustainable land management through the implementation of Scotland's planned Land Management Contracts system, and through enlarging Scottish use of the menu items in the EU Rural Development Regulation to enable support for broader economic development 'beyond the farm gate', to complement this.

9. Across the EU there are many good examples of schemes using RDP funding to achieve more sustainable rural economies and rural land management, and Scotland needs to take the initiative and develop more programmes and projects in this field, particularly as future EU Structural Funding for rural development in Scotland is predicted to decline significantly beyond 2006. Integrated schemes working through a basis of broad territorial partnerships between farmers and others within local communities have a proven track record in promoting more sustainable and self-reliant economic development in Europe. The moves in Brussels to simplify the EU Rural Development Regulation and to enable it to be delivered through more integrated systems, such as have been pioneered in the LEADER initiative, after 2006, should be very helpful to the Scottish situation.

Making the most of the changes resulting from reform

10. It is very important that the Executive should take steps:

- To help farmers and their families take stock of the implications of the changes for their farm enterprises in both environmental and economic terms, and review their future business options in that light. This will require time and imagination, as well as the confidence to make changes where these look to be necessary or beneficial. In Ireland, the government has announced its intention to support a major advisory and extension programme to help farmers to consider and adapt to CAP reform as it takes place. While Scotland's broader public spending priorities might not allow for such a generous initiative, increased investment in helping farm families to prepare for the new system and consider their future options could prove cost-effective in the longer term, in helping to stimulate positive structural changes in rural economies and ensuring that farmers can meet the requirements of the new obligations being placed upon them, under cross compliance.
- To monitor the ways in which farmers actually begin to change their practices and systems following the introduction of the new policy framework, and design responsive policy delivery systems that can be adapted as these changes become apparent, to ensure that they continue to deliver effectively against broader goals for Scotland's rural areas. We urgently need to build a better understanding of farmers' actual adaptation to the new policy climate and its implications for the wider rural economy and environment. This will be an essential ingredient in preparing the new Rural Development plans and programmes for the next programming period beyond 2006.

ANNEX to Evidence to Scottish Parliament Inquiry into CAP reform

Background Paper – Making the CAP fit for Herefordshire

Dr Janet Dwyer¹ and Professor Henry Buller²

1. Introduction – the context and process of the reform

Context

Last summer, European Agriculture Ministers agreed a major reform of the Common Agricultural Policy (CAP). The aim of the reform is to simplify the way most support is given to farmers and to ‘decouple’ it from production – to ensure that in future, farmers’ decisions on what and how much they produce will be unaffected by the level of CAP subsidy that they receive. The reform was influenced by three factors:

- The imminent enlargement of the EU to embrace initially 8 new members (in May 2004), including many countries from central and eastern Europe with large numbers of farmers and relatively weak public administrative systems, who would have found it extremely difficult to cope with the complexities of the existing CAP subsidy system.
- Continuing criticism of CAP policies by European environmental and consumer interests, who believe that it encourages overproduction and thus threatens the environment and the quality and safety of food;
- The resumption of negotiations on a new World Trade round, involving the need for the EU to respond to pressure from other major international trading blocks to reduce the degree of protection afforded to its own agriculture. Other exporting countries like Australia and Brazil say that the CAP distorts international trade by giving EU producers an unfair advantage, which discriminates against the products of other, poorer countries and can result in the ‘dumping’ of low-cost exports on international markets when they are surplus to European demand, destabilising these markets and threatening the viability of production in other areas.

This latest reform is the third one in a sequence that has sought to address some of these issues. The first was in 1992, and the second in 2000 – the so-called ‘Agenda 2000’ reform. The reforms have been similar, in that they have all sought increasingly to break the link between policy support for farmers, and the types of product and levels of output that each farmer chooses to produce, so as to reduce the likelihood that support is encouraging overproduction and distorting markets. But this latest reform is arguably the most radical one.

Process

The new Regulations governing the reformed CAP are now in place, and mainly come into force from 1 January 2005. They set a framework for how the new systems

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will operate, but don't prescribe all the details. Some details are left for individual Member States to decide, based upon their own circumstances. Between now and 2005, each country must decide exactly how it is going to implement the new Regulations, and most are currently busy consulting and developing proposals. In the UK decisions on the detail of the reforms are being devolved to the four administrations in England, Wales, Scotland and Northern Ireland. In England, an initial consultation document on CAP reform was issued by the Department for the Environment, Food and Rural Affairs (DEFRA) early last Autumn, seeking responses by the end of October. A second consultation is expected in February, to examine some of the detailed options more thoroughly, and a final consultation will be held in the summer or early Autumn this year, setting out in draft the detailed legislation that will bring the new reforms into effect, in England.

2. Details of the Reform

To understand the importance of the reform you need to understand how support to farmers works now, and how it is to change after January 2005. Most farmers already know this, but this section attempts to explain it to any non-farming readers.

What happens now – a guide for the non-farmer

Today, all farmers in England who produce beef cattle, dairy cattle, sheep, or a range of the main arable crops (wheat, barley, oats, rye, maize, legumes – field peas and beans - oilseeds – rape and linseed – and potatoes for starch production), can receive support from the EU to help them to continue producing successfully. Support is given in relation to the specific products, through so-called 'regimes', which aim to stabilise the markets for each of the major products. Initially, CAP farm support entailed Ministers agreeing 'guaranteed prices' for these products and using public money to intervene in markets to ensure that prices didn't fall too far below these levels, each year. But this system proved costly, unpredictable and over-successful, in that it generated very large surpluses that were expensive to store and dispose of. So, since 1992, many of the main support systems for the regimes have been modified, and now operate as follows.

- For producers of beef and sheep, farmers claim 'direct payments' from the government, for each eligible animal kept on the farm, subject to certain criteria relating to their age and type – so 'premia' are paid on suckler cows, beef cattle and breeding ewes, each year. To claim, farmers must fill in forms stating how many eligible animals they hold and also demonstrating that they meet the minimum conditions for payment: some conditions relate to maximum and minimum stocking densities, so farmers also provide details of all the 'forage land' used to feed or graze stock on which claims are made.
- For farms with arable crops, direct payments are offered per hectare of each crop grown, and different rates are offered for different crop types. Each year, a farmer fills in a form detailing how many hectares of each crop have been grown and payments are calculated accordingly. Again, the payments are subject to a number of conditions. Most importantly, the land on which support can be paid (eligible area) must have been in crop production in 1991, and anyone growing a significant area of arable must 'set-aside' from production, each year, a specified percentage of their eligible land: recently this has been either 5 or 10%. On set-

aside land they must follow a set of management conditions to protect the environment and they receive a special set-aside premium, to compensate them for the land lying idle.

- In order to administer the beef, sheep and arable system together (termed the Integrated Administration and Control System, or IACS), farmers have to keep up to date detailed maps of all their 'IACS-eligible' crop and forage land, showing their land use choices, year on year, for whenever claims are made or checked. Incorrect or fraudulent claims can lead to significant penalties for claimants.
- For dairy farmers, the support regime offers no direct payments, but guarantees a 'minimum price' for milk and dairy products which supports the prices received by dairies when selling their output. However, to minimise surpluses the EU has also applied quotas to milk production since 1984. Today in the UK each dairy producer can only produce a specified quantity of milk, determined by his or her individual quota; if production goes above this level it cannot be sold at the guaranteed price and penalties may be levied. Farmers can buy and sell or lease quota, when they need to adjust their entitlements in line with changes in their production, but of course, this is not a free process.

So, the main CAP regimes - especially IACS - are fairly complex to administer. However, the system doesn't affect everyone, because some farms don't produce these particular outputs. In particular, support doesn't cover farms specialising in:

- Pigs and poultry
- Fruit and vegetables (other than starch potatoes and legume crops)
- Unusual types of grazing livestock - eg deer for venison, wild boar, goats (UK only) ostriches, etc.

What will happen from 2005

Beef, sheep and arable regimes – introduction of the new Single Farm Payment

This is the biggest single change. From 1 January, the separate support regimes for beef, sheep and arable crops will cease. Instead, each farm will be offered a support payment that is broadly based upon the average levels of annual support that they received under the 3 previous regimes, combined, in recent years. The payment will be made in relation to the amount of *IACS-eligible land* that they continue to manage.

The EU regulation introducing this new, so-called 'Single Farm Payment' (SFP), gives options for how the payment can be calculated. Either:

- It can be based upon the actual amount of money previously received by each farmer, in relation to the IACS-eligible land managed – the so-called '*historic basis*' for payment, which will mean that each farm will receive a different notional 'payment per hectare' on their land, depending on what it was used for, in the past; OR

- It can be based upon a *regionally-determined, average payment* per hectare for all land, or two separate payments for arable land and forage area, where payment rates are set so as to ensure that in each region, the total money paid out is the same as the overall level of support that this region received under the old regimes. Under this system, all farmers in each region get the same annual payment per hectare for eligible arable or forage land, but rates would vary between regions. In addition, countries that adopt this regional average payment system can decide, if they wish, to expand the definition of eligible land so that other kinds of farmland can be covered by the payment – for example, land currently used for non-IACS crops (eg fruit, potatoes and other vegetables, or farm woodlands). In this case the average payment rate would be lowered accordingly to ensure the same expenditure overall, in each region.

For farmers, a historic system would not mean a big change in how much money each individual gets from the government, whereas a regionalised average payment system will mean some farmers get less than they do now and others will get more: in effect, the more productive livestock farms (in terms of output per hectare) and the crop farms (whose current payments are generally higher than those for livestock farmers) will lose money to other farms with fewer stock per hectare or fewer hectares of crop land, or with land that was formerly not eligible for payment but which is newly classed as eligible under the new system, if this particular option is chosen.

DEFRA ministers have soon to decide which payment system to adopt, for the new SFP. In his speech to the Oxford farming conference, Agriculture Minister Lord Whitty indicated that they may favour a ‘hybrid’ system, such as has recently been agreed in Germany, where payments begin with a historic weighting but over time, this is gradually phased into a regionalised average payment system.

However, under either option, the new payment will not depend upon current production levels or decisions. You will get the same amount of money regardless of how many stock you keep or which crops you choose to grow, year on year, as long as you manage your eligible land according to a general set of conditions. This is a marked change from the current situation, where subsidy depends critically upon stocking and cropping patterns, year on year.

The general conditions for receiving the new payment involve three elements:

- So-called ‘*cross-compliance*’: ensuring management of land, crops and livestock is in line with EU environment, food safety and animal welfare legislation;
- Making sure farmland is kept in ‘good agricultural and environmental condition’, according to precise requirements to be determined by each Member State. In the

EU regulations, soil conservation is highlighted as a particularly important consideration for these conditions, as well as protecting most permanent pasture.

- For farms with eligible cropland, there will still be a compulsory set-aside requirement (see above for details) – the rate is likely to be around 5%, in 2005.

The result should be a simpler system to operate, for both farmers and government officials. However, because of these three conditions of payment, there will still be a need for claim forms to detail all eligible land and cropped and forage areas, at least.

Dairy – price cuts and start of direct payments

For dairy farms, the reform is more subtle. Quotas remain, but the EU will cut, in stages, the guaranteed prices for dairy products and introduce a new direct payment to farmers, as compensation. The payment can be made:

- in relation to the volume of milk that the farm is producing divided among the number of milking cows, to give a new ‘dairy cow premium’; OR
- as a payment based upon historic production levels which is added to the new Single Farm Payment system (which again, can be calculated on a historic or regional average basis for each farm) – ie the support will be rolled into the SFP.

Modulation – cutting SFP and transferring funds into rural development

Ministers have agreed that from 2005, the total sums involved in SFP support within each Member State should be gradually cut, in order to generate money that can be used to build up the Rural Development Programmes also funded by the CAP. Above a certain individual threshold, anyone receiving SFP in future will have their payments cut by 3% in the first year, 4% in the next and then 5% per year each year, from 2005-2012, to provide new funds which the EU will recycle into Member States’ Rural Development budgets. For every pound taken from the SFP budget in England, DEFRA will recoup a proportion of that pound, which it must then match with national funds, to offer more funding for schemes in the England Rural Development Programme (ERDP) – these include agri-environment and business development support of various kinds.

Other parts of the CAP

The reforms also make some changes to other parts of the current support system.

- Some new options for support can be offered under the Rural Development Programmes, to encourage quality production and help farmers meet new environmental or welfare standards, and to support farm planning. However, no new money will be available to finance these options until at least 2006 when the current ERDP will be relaunched, so it is unlikely that the government will act until then. After 2006 it is unclear which of these new options might be offered under ERDP – this will depend upon a separate consultation process during 2004-5, in which many of the current schemes might be changed.

- There is a new requirement that government makes a ‘farm advisory system’ available to all larger farms in receipt of the new Single Farm Payment, to help ensure that they are meeting regulatory requirements. The system must be voluntary for farmers and can be provided either at cost – ie as a commercial service – or involving some government subsidy.

It is important to note that *DEFRA still has to decide some crucial details of the reform* – most notably whether payments should be made on a historic or a regional average basis, and if the latter, whether other kinds of land should newly qualify for the payment. These decisions are being influenced by the consultation process described in part 1 of this paper, as well as developments in other EU countries and within the European Commission, which is currently busy drafting detailed ‘implementing regulations’ to support the main reform regulations.

Other details still to be decided by DEFRA include the options for dairy reform, and the precise requirements of ‘good agricultural and environmental condition’. Also, they must decide whether or not to apply another mechanism, called a ‘national envelope’ to topslice some of the SFP money from each contributing sector (beef, sheep arable and maybe dairy), and direct it into targeted schemes to benefit the environment or promote enhanced food quality.

Summary of changes in brief, from a farmer’s perspective:

- your future support level won’t be related to how many animals you keep or which crops you grow, year on year, but more on what you did in the past;
- payment will be linked to a specific area of land which has to be managed with some (new) basic environmental, safety and welfare conditions but beyond that, it doesn’t have to be actively ‘farmed’ to qualify for support;
- payment is likely to come in a lump sum, one or more times a year, and that amount will gradually get smaller due to modulation;
- the budget for ERDP schemes (agri-environment, rural enterprise, etc) will grow over time, giving more opportunities to join these schemes (although this growth is unlikely to go beyond demand, which is generally very high for these schemes).
- the paperwork involved in claiming SFP *should* be simpler;
- set-aside will still feature, for arable farmers.

3. Implications of the Reform

Because the future SFP will be paid as a single sum on all eligible land and won’t be affected by annual production decisions, it might provide a stimulus to farmers to think about changing their businesses, for example investing in new enterprises or improved equipment or facilities for the existing business. Some experts have said that many farmers would do best to stop producing altogether or, at least, to significantly reduce their scale of operations and simply live on the SFP income. On the other hand, there is no obligation on farms to change what they do now, and many people believe little will change, in the short term. Probably, much depends upon trends in markets and other factors beyond the influence of the CAP.

Before the reforms were finalised, and immediately afterwards, DEFRA commissioned economic modelling studies and other assessments to try to predict how they were likely to affect farming in England. At the same time, a variety of similar studies was carried out by different stakeholder groups, including the Royal Institute of Chartered Surveyors (RICS) and the National Farmers Union (NFU).

Some of the studies of reform impacts work by examining farm profitability changes if all market conditions remain unchanged – ie if the reforms were introduced tomorrow and farmers reacted immediately to the changes. In reality, this will not happen – any change will occur over a period of time, in which all the main markets will be changing, too, and this will influence what happens. Nevertheless, the study predictions can give an impression of how the changes will affect the relative attractiveness of different kinds of production and thus suggest broader scale changes.

In summary, the studies say the following (for more details, see DEFRA's website).

- Research by ADAS indicated that for most farms in the Less Favoured Areas (hills and uplands), decoupling will give an incentive to reduce stock numbers – particularly for suckler cow producers, but on stock farms in the lowlands, there is little incentive to change stock on smaller farms but an incentive to cut stock dramatically on larger farms and switch to arable, wherever the land is sufficiently productive. They conclude that decoupling will exert downward pressure on beef and sheep production in England but beef will be hit harder than sheep.
- Research by Cambridge University indicated that for arable farming, reforms may have little immediate impact on profitability and prices, but longer term they will make crops less profitable on much of the less productive arable land, so this land might not be cropped in future – perhaps moving into widespread set-aside or fallow. Also, wheat would become slightly more favoured by comparison to other crops, on the most productive land. Farm enlargement would also be encouraged.
- Research by Harper Adams and the Scottish Agricultural Colleges on whole farm impacts indicated that grassland is likely to be grazed less intensively but for a longer period each year, and silage will continue to replace hay, as forage.
- Research by GFA-RACE (Cirencester) and IEEP on the environmental impacts of reform suggested increased specialisation and concentration in some sectors, especially dairy and cereals, undergrazing in marginal areas, a reduction in suckler cow numbers and increase in high performance sheep enterprises in the hills, a decline in mixed farming and more monoculture cropping, reductions in farm workforce and more contract farming, and large-scale land fallow or industrial cropping in some arable areas.

Thus, the potential impacts upon farms, rural economies, environments and communities could be as follows.

For farming – with reduced business profits, but cushioned by the SFP, many businesses may start to think about restructuring. Pressure to cut costs will continue, so labour may be shed and families may need to think about working off the farm or finding new on-farm enterprises (novel crops, rental income, new farm-based business, adding value to produce, etc), to offset declining profits from their current

enterprises. For businesses already under financial pressure, the SFP may trigger them to stop serious farming altogether and simply claim the payments for looking after the land, but this could be too drastic a change for many to countenance.

For the environment – there seems a mix of possible negative and positive results. Moves towards reduced grazing pressures in some areas would be beneficial – especially on sensitive upland sites – but if valuable grassland is no longer grazed at all, that would be of concern. Any increase of wheat at the expense of other crops suggests less landscape and biodiversity interest in arable areas but it could mean less use of certain kinds of pesticide, which could be good for soils, water and some birds and animals. More concentration in dairy farming could be damaging for water quality, but the new ‘good agricultural and environmental condition’ requirements for SFP might trigger beneficial changes, depending upon how well they are adopted.

For rural economies, the effects are potentially interesting. Decoupling payments may give farmers more options to spend their money in new ways, which could be beneficial. On the other hand, the pressures for further farm structural change and likely reduced farm output could have negative effects upon rural businesses directly upstream or downstream of farming, in the food chain. The impacts upon rural tourism may be closely linked to the environmental impact of reform (see above).

For rural communities, the effect of the reform arguably depends less upon exactly what changes take place, and more upon how that process is managed, and how farmers and others are helped to cope with change. Without support, stress could increase in farm families, whereas with support it is possible that the changes could be seen as a positive opportunity. In the longer term, reform will further decrease the economic importance of farming’s role in rural areas, so its role in maintaining the environment and providing a valuable resource for rural communities will come more to the fore. As this happens, the key need may be for more mechanisms to build links between farming and non-farm interests in rural areas, to strengthen these roles.

Implications for Herefordshire

Farming in Herefordshire

Much of Herefordshire is given over to intensive arable cropping, particularly in the lowlands and south and, increasingly, extending onto the Herefordshire Plateau, an area traditionally associated with mixed farming. Accompanying cereal production, horticulture (traditionally apples and hops but now a much wider range of outputs) has been common and increasingly important in the lowlands, though usually in areas raised above the floodplains, and on the slopes of lower hills. Bush orchards have generally replaced the traditional tree orchards. Pasture remains common along the valley floors in the areas most prone to flooding. Among recent trends in lowland areas there has been some diversification into pig rearing and increasing conversion of meadows into arable. Potato cropping on valley land and low slopes has been a significant feature in recent years.

Dairy, beef and sheep continue to occupy a significant part of the upland regions of Herefordshire. Although permanent grassland is the largest land-use, it is more and more spatially differentiated across the county. In the north-west, where Welsh and English influences intermingle, pastoral husbandry is the dominant land-use though arable and conifer planting are also developing. In the south, arable expansion has been pronounced and has been accompanied by considerable woodland loss.

Possible impacts of CAP reform on Herefordshire farming

Decoupling and the Single Farm Payment (SFP) will, it is widely believed, lead to a significant extensification of production in Britain with an increase in fallow, reduced use of inputs and reduced grazing pressure. These are generally believed to yield positive environmental benefits but also to promote farm business restructuring and reductions in farm employment. Beyond this, the choice of SFP approach will be important.

According to DEFRA ³, a Standard Area payment would benefit LFA cattle and sheep, general cropping, horticulture, and small and medium dairy farms (particularly those which received no payments under IACS, assuming their land becomes newly eligible). However, it would also accelerate processes of restructuring ⁴ amongst cereal, mixed and medium-large lowland cattle and sheep farms, which would effectively lose support (with nearly 20% of all farms losing more than 20% of their current payments). So, given its mix of farm types, Herefordshire is likely to have both 'winners' and 'losers' as this system is gradually phased in. The growth of agri-environment policy through the new Entry Level Scheme (also starting in 2005) may also increase the number of environmental agreements in the county.

In general, reform is likely to have a greater immediate impact upon the dairy sector than the cereal sector, which has already gone through some recent restructuring. Current dairy restructuring trends are likely to speed up, leading to larger herd sizes and higher yields per hectare. This also suggests an increase in forage maize (already observable in Herefordshire) and concentration of dairy holdings, as smaller and less profitable farms sell up. But the pace of this change may be slower if England adopts area-based SFPs and could also be affected by any decision to use national envelopes.

4. Conclusions and next steps

There is a lot about these reforms that is still unclear, and we won't know all the details for some months yet. Nevertheless, we can help to influence the decision-making process and we can prepare to make the change as positive as possible by planning now, based on what we do know about what will happen.

In considering how interested groups and individuals in Herefordshire should react, a number of points would seem important.

³ DEFRA (2003) *Supplementary regulatory impact assessment on options for the implementation of the reform of the CAP arising from the agreement of the Council of Ministers of June 2003*. DEFRA.

⁴ GFA-RACE and IEEP (2003) *The potential environmental effects of the CAP reform agreement*. Draft final report to DEFRA.

- Making sure all local stakeholders know about what is happening, so that they can be sensitive to the challenges facing farming businesses and alive to the potential knock-on effects for their own concerns and interests.
- Keeping interested parties up to date with the consultation process, to give more people a chance to present evidence and feed information and views into DEFRA at appropriate points.
- Setting up systems to track actual changes as they occur, to see whether what has been predicted is actually happening and to pick up both positive and negative trends and thus be better able to deal with them as they develop.
- Establishing appropriate support mechanisms or structures/initiatives to pick up the opportunities/challenges created by the changes – at this stage, this may be more a case of identifying the potential for organisations to come together and work to develop these things in the next few years beyond 2005, than direct action straight away. Nevertheless, where discussion between different interests suggests new opportunities that would need further research and development before they could be put into effect, now is the appropriate time in which such research and development should be undertaken.
- Last but not least, using the opportunity of this conference to get a clearer view of the key issues for Herefordshire and the main perceptions and concerns of local people in rural areas in relation to the reform process, to guide future actions and initiatives.

Environment and Rural Development Committee

Enterprise and Culture Committee – Inquiry into Renewable Energy

Paper from the Convener

Background

1. At its meeting on 28 January 2004, the Committee agreed to appoint the Convener as reporter, to keep the Committee updated on the progress of this inquiry.
2. The purpose of this paper is to update members on the progress of the inquiry, and to suggest a number of key areas that members may wish to authorise the Convener to follow up during future evidence sessions.

Evidence taken by the Enterprise and Culture Committee

3. The remit of the Enterprise and Culture Committee's inquiry into renewable energy is attached for members' information at Annex A. Also attached at Annex B is a summary of the evidence given to the inquiry so far.
4. A number of issues that are relevant to the remit of this Committee have arisen during the course of the inquiry. It is anticipated that the Convener will attend the meeting of the Enterprise and Culture Committee when it takes evidence from the European Commission and the Deputy Minister for Enterprise and Lifelong Learning. This evidence session is scheduled to take place on March 30, and the Committee is expected to consider a draft report in late April or early May.
5. A number of relevant issues that the Committee may wish the Convener to raise during this evidence session are listed below. The list is not intended to be comprehensive and the suggested issues are not listed in any particular order. Members are invited to give their views on the priority areas that they wish the Convener to pursue at this meeting. Members are reminded that there may be some time constraints on the number of issues that the Convener will be able to pursue. It is also important that these issues fall within the current scope and remit of the inquiry being conducted by Enterprise and Culture Committee.

Issues that the Committee may wish to see raised in evidence

6. Local Issues
 - What opportunities should there be for local communities to be involved in renewable energy schemes?

- Is sufficient consultation taking place with local communities on proposed schemes?
- Do the current arrangements provide sufficient ability for local communities to derive economic benefits from renewable energy schemes?

7. Issues regarding the national grid

- Outwith the central belt, the national grid is not particularly strong, nor well-placed to deal with renewable energy sources that deliver input to the grid on an intermittent basis. How will the Executive ensure that grid management systems can accommodate renewable technologies?
- What work is being done to attempt to maximise the use of the grid for small scale embedded renewables, such as mini wind vanes and PVs, which potentially add base load energy and are likely to be compatible with urban areas?

8. Technology issues

- In addition to wind-farms, there are numerous other forms of renewable energy that are less well utilised or well-developed in Scotland, e.g. wave and tidal power, use of biomass and bio-fuels, and micro scale renewables which could be embedded in buildings. How should these alternative technologies be developed?
- Has sufficient consideration been given to maritime issues in developing off-shore technologies?

9. Other Environmental issues

- How will the implementation of strategic environmental assessments impact on the renewable energy sector?
- How are considerations of environmental justice being taken forward (e.g. for communities who have a high number of renewable energy schemes in their area)?
- How is the Executive addressing social justice by maximising the opportunities to link renewables with energy efficiency and tackling fuel poverty?
- What changes are planned to building standards to encourage developers to incorporate renewable technologies in building developments?
- How are energy conservation targets set, and are they achievable?
- How is the potential for 'green jobs' being developed?
- Should the development of renewable energy schemes be limited in conservation areas, and if so, how?

10. The Committee is invited to consider the issues listed above, and to agree the priority issues which the Convener may wish to raise in evidence with the Deputy Minister and the European Commission.

Sarah Boyack MSP
Convener

**REMIT FOR THE ENTERPRISE AND CULTURE COMMITTEE'S
RENEWABLE ENERGY INQUIRY**

'To inquire into the development of renewable energy in Scotland. Specifically, the Committee will wish to ask the following questions, which are intended to be illustrative rather than prescriptive:

- **Will the Executive targets be met, under current circumstances, and are they appropriate?**
 - how were they arrived at by the Executive?
 - what is the relationship with UK targets?
 - have assumptions been made about the contributions of different sectors?
 - what are the opportunities and implications for the economy in achieving the targets?
 - what are the implications if the Executive's targets are not met?

- **If not, why not? (What are the current barriers, and what action needs to be taken to ensure that the targets are met?)**
 - **global issues**
 - the Renewables Obligation (Scotland) and the UK energy legislative framework
 - the electricity market
 - the transmission network (inc. the Scottish national grid)

 - **local issues**
 - What opportunities are there/should there be for local community involvement in, and economic benefit from, renewable energy schemes?

 - **examination by sector**
 - onshore wind (inc. planning issues, community development)
 - offshore wind (inc. UK strategy, role for energy ITI?)
 - wave/tidal (inc. technology issues, job potential)
 - hydroelectric
 - biomass
 - other/longer-term (e.g. emerging technology, non-electricity)

- **Are there implications for the reliability of supply if the Executive's aspirational target is met?**

Evidence taken by the Enterprise and Culture Committee

The Committee has now taken oral evidence from the following organisations as part of its renewable energy inquiry:

- Director of the Institute for Energy Systems
- Scottish Enterprise
- Highlands and Islands Enterprise
- Five petitioners
- COSLA
- Argyll and Bute Council and Alienergy (Argyll Lomond and the Islands Energy Agency)
- Scottish Power and Scottish and Southern Energy
- Scottish Renewables Forum (officials)
- British Energy and British Nuclear Fuels Ltd (BNFL)
- Scottish Natural Heritage
- Scottish Environment Link
- British Energy
- Scottish Renewables Forum (representatives of research and development companies)
- Ofgem
- Department of Trade and Industry

Witnesses still due to give oral evidence over the coming weeks are:

- Ministry of Defence
- Civil Aviation Authority
- National Grid plc
- National Air Traffic Service
- Scottish Energy Environment Foundation
- Representatives of small and community renewable businesses
- Deputy Minister for Enterprise and Lifelong Learning.
- Officials from the European Commission

The Committee has also visited a windfarm in Campbeltown and the Vestas-Celtic turbine factory, and held an open meeting in Campbeltown which was attended by over 60 local people.

The Committee will also be conducting a number of case study visits, to Denmark, and throughout Scotland, to gain a greater understanding of the developing technologies in the renewable sector.

The deadline for submitting written submissions was 26 January. At the time of writing, approximately 150 written evidence submissions had been received. All submissions are available on-line on the Enterprise and Culture Committee home page.