

Sumpsi Viñas, José M.; García Azcarate, Tomás

**Book Part**

## Obstacles and constraints for a new CAP

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## Obstacles and Constraints for a New CAP<sup>3</sup>

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### **1 Introduction**

We have tried to order the discussion on obstacles and constraints for a new CAP in six points. Nevertheless, and before a detailed presentation of them, we would like to make some general remarks.

The discussion on agricultural policy is polluted by other agendas, private or public, such as the net-contribution of each Member States to the EU budget or the balance of competencies between different European institutions.

These concerns are relevant. But they should be addressed through specific and explicit measures, and not through the use or abuse of sectoral policies. We should be aware that this is not what was decided by the Fontainebleau summit in 1984.

We have learned some lessons from the previous reforms of the CAP, the MACSHARRY reform of 1992 and the Agenda 2000:

A reform has to be seen as a winning process by ALL contributors. This has been relatively easy to achieve in a context of possible increased expenditure. The transfer of support from consumers to taxpayers, more efficient from an economic point of view, has implied an increase in overall agricultural expenditure. If we take into account a drastic budget restriction (to the current level or even below), an agreement will be more difficult.

Reform proposals have to be balanced. The impact should not be concentrated on some regions. This is, for instance, the major political difficulty with European-level

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<sup>1</sup> Professor of Agricultural Economics, Universidad Politécnica de Madrid. The article reflects the individual opinion of the author and not necessarily the opinion of his organisation.

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modulation, the effect of which will be concentrated in the “new German *Länder*” (the former East Germany) and in East Anglia.

Even more, there should never be a rupture with the past but rather an evolution to a more desirable set of policies.

## **2 Obstacles and constraints coming from the new political-institutional scenario of the EU**

In addition to the slowing-down of the adaptive capacity of the Union (see point 7), the approval process will be each time more difficult due to *enlargement*. The Union will no longer be manageable in the same way.

This reinforces the debate on the “*new European governance*”. This debate is just starting, but different actors have different agendas: to increase regional influence, to decrease the margin of manoeuvre for central government, to decrease Brussels competencies, to develop European networks both horizontally and vertically, to increase the Committee of the Regions’ relevance or European Parliament responsibilities or Council competencies.

The current discussions around what is called the “German Proposal” or the “French position” are a good example of the complex mixture of targets and goals, condimented with public-relation aspects. Is it possible at one and the same time to decentralise the core of EU spending (agriculture and regional funds) and to promote a federal status? Is it possible to imagine a federal State with a budget below 0.5% of EU GDP?

## **3 Obstacles and constraints coming from lobby pressures**

Traditionally, the farmers’ unions were the most conservative lobbies on CAP reform. Traditionally, the Agricultural Ministers were conservatives. In order to obtain some reform agreement, it was necessary to promote “Jumbo Councils”, mixing farming and Foreign Affairs Ministers.

The Agenda 2000 represented a major change in this scenario. The Agricultural Ministers were more reform-oriented than the European Summit. Agricultural Conservatives entered into a joint venture with Finance Ministers in order to limit and delay a CAP reform.

Now, and this is a new element in the debate, other lobbies such as environmentalists, consumers, animal-welfare partisans and hunters are becoming increasingly relevant. The Council of Agricultural Ministers is no longer a farmers’ club but has become a more accurate representation of European society.

This change is the result of a double evolution, of society and of policy. On one hand, the economic and political influence of farmers is decreasing, even in rural communities. On the other, direct payments have made support to farmers more transparent and, therefore, have fed the debate on the legitimacy of agricultural spending.

These multiple actors open an interesting field for promoting reforms but also make the precise perception of the real expectations of European society more difficult.

Today’s situation is a good example of this confusion. It is said that:

- Farmers should be competitive in a more open economy.

- Farmers have to respect a minimum set of rules, as far as environment and animal welfare is concerned.
- Special rules have to apply on transport of live animals.
- But we cannot easily impose our own and internal rules on other countries (principle of extraterritoriality).
- Consumers have to understand that they have to pay a “correct” price for healthy food. A high standard of quality has to be guaranteed for food offered to consumers.
- But the farming industry has to collaborate with the macroeconomic target of keeping inflation under control.
- In addition, with enlargement a larger share of the population will spend a significant part of their income on food and will be highly sensitive to an increase in food prices.
- Agricultural expenditure has to be controlled or even to decrease.

Today the major obstacles do not come from lobbies but from the lack of political will to continue on the same track in the process of building Europe. The relevance of budget issues is the most spectacular demonstration of this identity crisis. When you do not know why you are paying, you always complain that you are paying too much.

#### **4 Obstacles coming from distributional effects of a new CAP**

One of the more difficult-to-justify aspects of the CAP is the distribution of the benefits and costs it generates. This can be looked at in many different ways: the distribution between commodities, between farms of different sizes, between producers, consumers and taxpayers and between Member States. The latter distribution is of greatest political significance. In fact, one of the major obstacles to reconverting current agricultural policy into a more integrated rural policy is the distributional effects among Member States (MS) provoked by reducing the first pillar and increasing the second. As a consequence of this sort of CAP reform, some countries would become winners whereas others would become losers, which would increase the difficulty of a Council agreement on CAP reform.

Up to now (MACSHARRY 1992, Agenda 2000), this redistribution issue was mitigated by the overall increase in EU agricultural expenditure. “Loser” Member States were losing parts of their shares in total expenditure, but the decided increase in direct payments represented an increase in agricultural expenditure in all Member States. The final Berlin discussion showed that this approach has found its own limits.

Certainly the full implementation of such a new CAP has the potential to alter greatly the distribution of support among MS. But this is not just an obstacle but also a benefit. It is a benefit because it is reasonable to expect that the EU’s largest spending policy should make a positive contribution to fulfilling the general objectives underlined by the Treaties in general, and the economic and social cohesion target in particular. If this cannot be done, it reflects either that the political institutions of the EU are not functioning as they should, or there is no real determination on the part of the Member States to achieve one of the most important objectives of the EU.

The main effects of reducing individual transfers, resulting from this sort of CAP reform, will be felt by the larger commercial farmers producing price-supported products and currently receiving large direct payments. Unless such farmers engage in the significant provision of environmental public goods and services, they will not

extract as much benefit from the new common agricultural and rural policy as under the current CAP. Such farmers are to be found in all Member States, but their relative weight varies greatly across them. In several Member States, they are influencing the position of some farmers' organisations against CAP reform in general and modulation in particular.

## **5 Obstacles and constraints coming from financial effects of a new CAP**

It is often argued that agricultural expenditure has to be capped in order to allow other EU policies to develop. As Delors has demonstrated with the regional funds, it is the lack of political will which limits the development of EU policies. There are budget margins in the current financial rules in order to allow such moves. Where is the political will?

Nevertheless, and as we have already underlined, in the future one of the most important constraints to the new CAP will be the EU budgetary constraint. The mid/long-term budgetary availability in real terms for CAP reform will stabilise or could even decrease. Given this budgetary constraint, the increase of the budget for the second pillar would need the reduction of the budget for the first pillar. This reduction could be achieved by:

- modulation;
- eco-conditionality;
- co-financing direct payments (first pillar);
- cutting direct payments.

The Agenda 2000 has already included the first two options to transfer EU funds within the agricultural budget from first pillar to second pillar: modulation and eco-conditionality. Concerning modulation, most MS have not applied it, nor do they appear to have any intention of doing so. The second option, eco-conditionality, is, in practice, very difficult to implement.

If Member States have an ambitious target for the Code of Good Practices, far more than what is foreseen in the current legislation, they are seriously limiting the impact of agro-environment support, which can only compensate farmers' activities in addition to good agricultural practices. This means that the farming community will lose public support, that farmers in some regions could suffer from market-competition distortion from other regions or from outside the Union, that protection of the environment would be seen by some farmers only as a constraint and not also as an opportunity.

Moreover, in the case of federal Member States, such as Spain or Germany, the regional governments also have a legal capacity to implement eco-conditionality, which makes it much more difficult.

The third option would allow to confront some of the most important EU concerns with:

- a greater responsibility of MS in the management of CAP direct payments,
- a reduction of EU agricultural budget share in total EU budget,
- a re-balancing of financial balance in some MS (net contributors).

Co-financing first pillar has some risks. The most important is re-nationalisation, as in this option the MS could claim some rules to allow national differences in applying first-pillar measures. Another risk is the relaxation of national contributions for all or some first-pillar measures by establishing a maximum amount of direct aid, a fixed EU contribution and an optional national contribution. Such an approach would imply another sort of re-nationalisation as finally the farmers could also receive different levels of direct aid across MS.

Co-financing first pillar would be unacceptable to poorer MS, especially to Accession Countries, but also to the MS receiving payments from the Cohesion Fund. In order to lessen this problem, it would be interesting to establish different rates of national co-financing according to the economic development level of Member States.

Co-financing will not be useful in the WTO context. Both co-financed or EU-financed amber and blue box are under discussion in this international context.

Therefore, in order to reduce the budget of the first pillar the most effective way would be cutting the CAP direct payments. Nevertheless, we can consider some different ways to reduce the CAP direct payments:

- Degressivity or linear reduction of direct payments. This option does not provoke distributional effects and is very easy to apply (English modulation).
- Progressive reduction of direct payments. This option provokes distributional effects and can be very complex to apply (French modulation).
- Reduction of arable-area payments in those EU regions where cereal yields are above the European average. This option would have positive effects on economic cohesion and would be very easy to apply but difficult to agree in the Council (see last paragraph of point 6)

Moving EU agricultural budget from first pillar to second pillar would reduce the total amount of EU budget allocated to the CAP by increasing the co-financing of agricultural expenditure on behalf of the Member States (MS). However, this change would work against countries that are in a weaker economic position, which in turn would act against the principle of cohesion. These countries would oppose such change, unless the level of Community co-financing of the second pillar were very high (80–90%) or new flexibility were introduced in the national co-financing, allowing, for instance, an increased share of private financing.

## **6 Obstacles and constraints coming from higher transaction costs of the new CAP**

One of the most important obstacles to moving the current CAP towards a more integrated rural policy (moving from first pillar to second pillar) is the higher transaction costs of the new CAP.

The two key elements of the new CAP are agro-environmental payments and rural-development incentives, both included in the new Rural Development Regulation (second pillar). Concerning the first element, to strictly establish public payments for the provision of landscapes, environmental and cultural goods and services, it would be necessary to fulfil two conditions: first, to pay separately for each public service or good provided by farmers according to its value (which gives rise to very complex problems of valuing environmental goods and services), and, second, to verify that farmers have really provided the specified public goods and services for which they are going to

receive the corresponding payments. Both questions need a lot of foregoing studies, designing, bargaining, monitoring and enforcement costs. Research results show that the transaction costs of agro-environmental programmes vary between 5% (some general and light agro-environmental programmes and 30% (some ESA schemes). Concerning the transaction-costs constraint, the question is: who has to pay transaction costs? At present these costs are paid by the Member States, but this adds further financial problems to the MS when applying agro-environmental programmes

But there is not just a financial problem. Most of the MS' agricultural administrations are not well prepared to apply these kinds of programmes on a large scale. The organisation, structure and human resources of the agricultural administrations should be significantly adjusted to adapt them to the new CAP requirements (not only in agro-environmental programmes, but also applying eco-conditionality and new environmental less favoured areas (LFA) scheme). In many countries we have identified a lack of co-ordination between agricultural and environmental administration in applying agro-environmental measures. In other words, it is not just the farmers who have problems adapting to the new CAP, but also the officials and administrations are failing to adjust.

Concerning rural-development incentives, the problem is the capability and initiative of rural actors to generate projects and investments for on-farm and off-farm activities (diversification). So far the experience of the EU LEADER initiative shows that a lot of work and capacity building is necessary to change the conservative attitudes of rural people and encourage them to undertake new activities and rural affairs.

Moreover, the evaluation of the LEADER initiative shows that, in spite of intensive technical work and meetings with rural people carried out by the Local Action Groups, very few projects have been undertaken.

We still see difficulties to implement the multifunctionality in a sound way. The concept of multifunctionality raises some critical questions: To what extent does society demand non-food agricultural functions? What amount should be paid for non-food agricultural functions and in what way?

Regarding the first question, the way of knowing whether society really wants these public goods and services is by determining the willingness to pay for them. Studies carried out so far have produced a wide range of results depending on the country and public goods or services provided by farming. In the case of Spain, the conclusions of several studies on the provision of certain public goods and services (natural values, biodiversity, landscape) by farming show that the willingness to pay is minimal. These results suggest that the demand of Spanish society for non-food agricultural functions is very low.

Regarding the question how to pay for non-food agricultural functions, there are two answers based on two different methods of applying the concept of multifunctionality. The first consists in paying for all activities as a whole by means of CAP direct payments (first pillar). This way of operating is not very correct and really only attempts to justify the current amount, or even higher amounts, of CAP direct payments. The implicit reasoning is as follows: without CAP direct payments there would be no agriculture and without agriculture there would be no maintenance of the landscape, nor conservation of the rural environment, etc. The main problem is that this method of applying the concept of multifunctionality does not ensure that farmers provide the public goods and services that constitute the non-food functions of agriculture.

The second method of applying the principle of multifunctionality consists in paying for each function separately once it has been verified that the function in question has indeed been carried out. By treating each activity separately, it is possible to tackle the question of payment in a more correct way. Thus, the food function of agriculture is rewarded by the market and therefore, at least from a theoretical point of view, does not require public funding. On the other hand, non-food functions of agriculture as provision of environmental public goods or maintenance of marginal rural areas are not rewarded by the market and thus require public funding. Nevertheless, private initiative should participate in co-financing payments to farmers whenever possible (environmental goods or services in which it is possible to apply the exclusion principle, for example entrance fees for visitors to a National Park). Nevertheless, fixing the level of these payments and checking that provision of environmental goods has really been delivered implies high transaction costs.

In general terms we can say the first method of implementation is defended by farmers' organisations and the national and regional agrarian administrations, whereas the second one is defended by environmental organisations, rural development networks (LEADER programmes) and some groups of academics. The first method implies consolidating the first pillar of the CAP, whereas the second method leads to reducing the budget of the first pillar and increasing the budget allocated to the second pillar. This explains why many MS are rejecting this second way to implement multifunctionality as the first pillar is fully financed by Brussels, whereas the second pillar is only partly financed by Brussels.

The shift towards area payments (by the 1992 Reform and reinforced by the Agenda 2000) was the first step towards a more territorial approach to rural policy, instead of a purely commodity- and production-based approach. Farmers must receive public support for what they do on the land, not for the commodities they produce. But decoupling needs to be taken further, removing the current massive bias in favour of intensive, high-yielding systems. In that sense, the Spanish Ministry of Agriculture (MAPA) is preparing a proposal on arable-area payments based on a common payment for all of the EU, and thus independent of regional yield of cereals. This change from the current differentiated area payments (partly decoupled) to common area payments (fully decoupled) would contribute to the social cohesion and extensification of farming, which is environmentally beneficial. But such a proposal will be difficult to accept by the MS with the highest yields of cereals (e.g. France) due to the negative distributional effects (losers). A more realistic option would be to reduce the current differences in the arable-area payments across EU countries/regions.

## **7 Obstacles and constraints coming from the imbalance between EU and MS rules (principle of subsidiarity)**

Changes are needed at all levels. Many of the current problems lie in the design of EU regulations, but national and regional implementation also plays a significant role. For example, under existing arable regulations it is possible for the Member States to establish national rules for set-aside. Equally, the afforestation of farmland could be implemented in a far more targeted and environmentally-sensitive manner under the existing EU regulation. The Agenda 2000 has introduced eco-conditionality, which is applied in a different way by Member States.

However, an excess or abuse of the principle of subsidiarity leads to a lack of "environmental cohesion" across the EU, with some Member States making greater



efforts than others to address environmental issues. EU regulations should give clearer guidance and require more specific commitments to prevent this “two-speed” situation. For example, applying eco-conditionality to all support regimes should be obligatory, and a clear guideline and timetable for implementation, monitoring and revision of measures should be established at EU level. Targeting of afforestation programmes to prevent negative impacts on habitats and to deliver specific environmental benefits should also be obligatory. The funding for the CAP is common to all, so the rules should ensure that environmental integration is equal as far as possible across all countries.

In some cases the abuse of the principle of subsidiarity can provoke a significant distortion of competition among Member States. For instance, the way in which the Berlin Summit passed the eco-conditionality is a clear example. The farmers from countries applying eco-conditionality in a stricter way will be in a worse position to compete than farmers from countries applying eco-conditionality with a lighter touch.

In other cases the abuse of the principle of subsidiarity leads to CAP re-nationalisation. For instance, the way in which the Berlin Summit adopted modulation is an example of this perverse effect (re-nationalisation). This sort of abuse of the principle of subsidiarity normally happens when the Council is unable to reach an agreement on some measure (in this case modulation).

The ideal scenario to balance common and national rules for a new CAP could be:

- Agreement between Member States (including accession countries) on the need for a new direction for EU rural policies, based on the principles of sustainability. At the moment there is no agreement (the last attempt at Cork failed). As a consequence, reforms are hopelessly piecemeal and there is always resistance.
- Agreement on a broad strategy of reform over 10–15 years, to be applied to all regimes of the CAP, involving removal of mechanisms which promote and/or maintain intensive farming systems and which conflict with the aims of agro-environment programmes and/or environmental legislation; re-balancing of support in favour of low-intensity production; shift of financial resources towards agro-environment and sustainable rural development.
- At Member State and regional levels, comprehensive review of the environmental effects and tendencies of agricultural land/resource use, leading to strategies with quantified targets for addressing issues. Cross-compliance, agro-environment payments and rural-development aids should be implemented with the aim of delivering these specific, quantified targets. Implementation of mainstream CAP measures would be adjusted to prevent conflicts with environmental objectives and measures.