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Greening agricultural payments in the EU's Common Agricultural Policy

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Abstract. Environmental objectives have become increasingly integrated into the EU's Common Agricultural Policy (CAP) since the mid-1980s. Integration has been pursued through the attachment of environmental conditions to the receipt of direct payments in Pillar 1 (cross compliance) and the use of voluntary agri-environment measures in Pillar 2. In formulating its proposals for the revision of the CAP post-2013, the Commission opted to pursue further integration largely through Pillar 1 through the introduction of a 'green' payment for farmers following a specified set of mandatory farm practices. The legislative process was not concluded in February 2013, but enough is known of the positions of the Council and the European Parliament to indicate that the level of greening ambition in this CAP reform will be very limited. Some explanations for the apparent failure to significantly reshape the CAP to tackle the problems faced by the natural environment are reviewed. It is suggested that, far from being complementary, cross compliance and voluntary agri-environment measures are competing approaches to further greening of the CAP. Advocates of a greater focus on environmental objectives need to choose between these approaches.

Keywords. CAP post-2013, greening, cross compliance, Pillar 1

JEL codes. Q01, Q18, Q24

1. Introduction

Agriculture and forestry have a key role in producing environmental public goods such as landscapes, farmland biodiversity, and greater resilience to natural disasters such as flooding, drought and fire. However, many farming practices also put pressure on the environment, leading to soil erosion, water shortages and pollution, and loss of wildlife habitats and biodiversity. Agriculture is also required to contribute to the EU's climate and energy agenda by reducing GHG emissions, improving energy efficiency, increasing biomass and renewable energy production, and protecting and sequestering carbon in soils. At the same time, agricultural production conditions will be increasingly affected by ongoing climate change. Helping to mitigate and adapt to climate change has become a major new chal-

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lenge for the agricultural sector. Managing scarce resources more effectively and increasing resource efficiency in agriculture in terms of external chemical inputs, water and energy use, land use and waste generation is also one of the goals under the flagship initiative *A resource-efficient Europe* under the Europe 2020 strategy (CEC, 2011a).

There has been progress in limiting agriculture's negative impacts on the environment as well as encouraging more environmentally-friendly agricultural practices on a proportion of European farmland (EEA, 2010). Emissions of nitrogen and phosphorous into waterways as well as greenhouse gases have been falling. However, successive investigations of the state of the European environment show that we are not yet in a sustainable position. The EU has set ambitious targets for further environmental improvement in connection with water, soils, air, climate and biodiversity (CEC, 2011c, Annex 2A; EEA, 2010). The improvements that have taken place occurred during a period in which growth in EU agricultural output marked time. Now, the market context for agricultural production has changed. Projections of global food demand and prices suggest there will be strong incentives to increase production in the coming decade (OECD/FAO, 2012). In the context of Europe's ongoing economic crisis, policy-makers in many EU countries are targeting increased food production and agri-food exports as a potential growth sector to help lead economic recovery. At the same time, biofuel and renewable energy targets add further to the demand for agricultural resources within the EU, increasing the competition for land with nature (Burrell, 2010; DEIAGRA, 2008).

This is the context in which the European Commission published its proposals for new regulations for the EU's Common Agricultural Policy (CAP) in October 2011 (CEC, 2011c). Sustainable management of natural resources and climate action is one of the three objectives of the CAP post-2013 (CEC, 2010). This objective is addressed in the Commission's proposal through a mandatory 'green' component of direct payments supporting environmental measures applicable across the whole of the EU territory; through changes in cross compliance; and through more strategic targeting in Pillar 2, with the environment and climate change as guiding considerations. The Commission proposed to allocate 30% of each country's national ceiling for direct payments as a green payment to farmers who would be required to follow a number of 'agricultural practices beneficial for the climate and the environment'. The requirements include ecological focus areas (EFAs), crop diversification and the maintenance of existing areas of permanent grassland at farm level. An important consideration was that greening should not threaten the viability of the farming sector nor unduly complicate the management of the policy (CEC, 2011c, Annex 2, p. 6). The Commission's stated goal was to improve the balance between different policy objectives through more targeted measures which would imply greater spending efficiency and greater focus on the EU value added (CEC, 2010). Both the Council (Council of the European Union, 2011) and the European Parliament (European Parliament, 2011) initially supported the further greening of the CAP towards 2020.

This paper assesses the Commission's proposal in the light of the history of efforts to integrate environmental objectives into the CAP. There have been essentially two approaches (OECD, 2011).² One approach has been to add the observance of environmen-

² The environmental impact of agriculture has also been addressed through environmental legislation, see Jack (2009).

tal standards and practices as a condition for eligibility to receive direct payments in Pillar 1 of the CAP. The other approach has been to remunerate farmers who voluntarily enrol in agri-environment measures (AEMs) for the extra costs involved in managing their land to produce additional environmental public goods in Pillar 2 of the CAP.³ While these two approaches have proceeded in parallel, expenditure on Pillar 1 direct payments remains far more significant than expenditure on environmental measures in Pillar 2.

Nonetheless, there appeared to be a logic in the CAP reform process whereby resources would be gradually transferred from direct payments in Pillar 1 to the more targeted measures in Pillar 2. Moving from broad-brush, undifferentiated policies which provide support to all farmers and all land indiscriminately to more targeted measures was the policy approach recommended by OECD Agriculture Ministers in their 1998 Communique and spelled out in the OECD report *A Positive Reform Agenda* (OECD, 2002). The rationale for targeting is that it leads to reduced transfers, greater policy efficiency with fewer leakages to unintended beneficiaries, and reduced distortions, albeit with the downside of higher transaction costs. Following the OECD advice would mean gradually reducing the importance of undifferentiated support in Pillar 1 of the CAP but increasing targeted payments through AEMs in Pillar 2 where there was evidence of under-supply of environmental public goods. This had been the direction of CAP reform between 1992 and 2008, even if the extent and pace of the shift in CAP funds left advocates of more radical reform dissatisfied (Buckwell, 1997).

However, this was not the approach taken by the Commission in its proposals for further greening of the CAP post-2013. Instead, the proposals envisage adding further conditions to the receipt of direct payments in Pillar 1. The Commission argued that greening Pillar 1 payments was the more appropriate choice because the voluntary approach using AEMs in Pillar 2 was unlikely to cover a significant part of the Community land area where the environmental pressures due to agriculture were greatest. There was also increasing resistance to a further transfer of funds to Pillar 2 both from farm organisations (representing the main beneficiaries of Pillar 1 payments) and Member States (which are required to finance the non-co-financed share of Pillar 2 payments).

In February 2013, the Commission's proposals are still in the legislative process and the ultimate outcome is not known. However, the reaction to the proposals in the Agricultural Council, in the European Parliament's Agriculture Committee (COMAGRI) and among Member States and interest groups was generally critical. Environmental groups criticised them for not being ambitious enough. Farmers' groups criticised them for imposing higher costs and taking land out of production when the global need is to produce more food. National administrations were unhappy because of the greater complexity they added in the administration of direct payments. It looks like greening will survive as a concept, but with very limited impact and limited environmental significance – an outcome described by environmental groups as 'green-washing' (Birdlife and others 2011).

In this paper, we explore the Commission's rationale for greening Pillar 1 payments, the implications of this approach and the political reactions in the light of previous efforts

³ The two Pillars of the CAP were introduced in the 1999 Agenda 2000 CAP reform. Pillar 1 funds market price and income support on an annual basis and is fully financed from the EU budget. Pillar 2 funds one-off and multi-annual rural development measures on a programmed basis, and is co-financed by the EU budget with Member States.

to green the CAP. Section 2 describes the gradual integration of environmental instruments into the CAP, focusing particularly on Pillar 1.⁴ Section 3 briefly evaluates the experience to date with the different CAP measures to target environmental objectives. Section 4 describes the Commission's recent proposals for the green payment in Pillar 1 and the reactions to this. Section 5 concludes with some reflections on the reasons for the likely legislative outcome and its implications for those seeking to further green the CAP to better meet the major environmental challenges facing agriculture in the coming decade.

2. Adapting direct payments to environmental objectives

The process of integrating environmental objectives into the CAP has been slow and arduous stretching back over the past 25 years. The high levels of market price support that characterised the CAP in the 1970s and 1980s were an important contributory factor to the process of intensification which has been the main cause of environmental damage in agriculture. The gradual reduction of price support and its replacement, first, by coupled payments and, subsequently, by decoupled payments was expected to contribute to alleviating some of these environmental pressures. This reform of price and markets policy was accompanied by specific environmental initiatives within the CAP. Within Pillar 1, the introduction of direct payments allowed conditions to be attached to the receipt of aid with the aim of promoting environmental objectives. At the same time, Pillar 2 has funded agri-environment measures which have remunerated farmers for practices which provide additional environmental benefits. This section briefly reviews the main milestones in integrating environmental objectives into the CAP to date (see Buller, 2002 for an earlier review).

Attempts were made to limit budget expenditure on EU agricultural policy from the early 1980s with the introduction of milk quotas, followed by a series of budget stabiliser mechanisms in the second half of the 1980s. These measures failed to address the fundamental disequilibria in agricultural markets. The reform process began with the MacSharry (1992) and Agenda 2000 (1999) reforms which compensated farmers for reductions in guaranteed intervention prices through granting coupled direct payments limited to predetermined quantities (hectares in the case of major crops, animal numbers in the case of livestock). The Agenda 2000 reform formalised the distinction between market price and income support policies (financed through Pillar 1) and rural development policies (financed through Pillar 2). The Mid-Term Review (MTR) (2003) and Health Check (2008) reforms transformed the majority of direct payments into decoupled payments. Reforms to a number of commodity regimes (sugar, wine, tobacco, cotton, rice, olive oil) during this period also lowered support prices and provided compensation to farmers in the form of increased direct payments. Following the implementation of the Health Check reforms from 2010, guaranteed support prices now operate at safety net levels and support to farming takes the form of largely decoupled payments through Pillar 1 and more targeted interventions through Pillar 2.

At the same time, the negative environmental costs of growth both in the wider economy and in agriculture were increasingly recognised. The first recognition of environmen-

⁴ A companion article reviews the history of agri-environment measures in Pillar 2 (Dwyer, 2013).

tal issues in the CAP was the introduction of the measure on mountain and hill farming in certain Less Favoured Areas (LFAs) in 1975 (Directive 75/268/EC). The objective of this measure was to ensure the continuation of agricultural production thereby maintaining a minimum population level and conserving the countryside. It addressed a very specific need to avert the depopulation of marginal farming areas but otherwise did not represent a break-through in terms of integrating environmental objectives into the CAP.

The Commission first drew attention to the need for agricultural policy to take more account of environmental issues, both as regards the control of harmful practices, and the promotion of practices friendly to the environment, in its Green Paper on perspectives for the CAP in 1985 (CEC, 1985). The paper recognised that the changes in farming practices in previous decades which had been important in increasing agricultural output had also contributed to the loss of biodiversity, the destruction of valuable ecosystems such as wetlands, and had increased risks of ground and surface water pollution. It identified the importance of setting the environmental reference level or baseline. Where the negative consequences of agricultural production justified extending regulatory controls designed to avoid deterioration of the environment, the 'polluter pays' principle should apply, and it would not be normal for farmers to expect to be compensated by the public authorities for the introduction of such rules. At the same time, the paper recognised that 'at least as important as the 'passive' protection of the environment is a policy designed to promote farming practices which conserve the rural environment and protect specific sites' (p. 51). In these cases where agriculture contributes to the conservation of the rural environment and thus produces a public good, society should provide the financial resources to permit farmers to fulfil this task. The paper noted that an added attraction of promoting such practices was that generally they were less intensive (and thereby less productive) and could help to contain the unwanted growth of agricultural production.

In the same year, the first agri-environment measure was introduced with article 19 of Regulation (EEC) 797/85 which allowed Member States to make payments to farmers who followed practices compatible with the environment in environmentally sensitive areas. However, only two countries, Germany and the UK, made use of this voluntary scheme (CEC, 1988). The Commission further spelled out its thinking in a 1988 Communication which put emphasis particularly on the problems caused by large-scale intensive livestock rearing and intensive crop production in zones at risk of pollution of surface and ground waters by nitrates ('vulnerable zones') (CEC, 1998), prefiguring the introduction of the Nitrates Directive in 1991. Also in 1988, a five-year voluntary set aside scheme was introduced as a mechanism to control surpluses in arable production (Regulation (EEC) 1272/88).

These ideas formed part of the background to the 1992 MacSharry CAP reform (CEC, 1991). The main thrust of this reform was to reduce the level of guaranteed prices for arable crops and livestock, while compensating farmers through coupled direct payments (area aids in the case of arable crops, headage payments in the case of livestock). To control the increase in budget costs, maximum areas for arable aid and ceilings for the numbers of animals supported by headage payments were set for each country. Set aside was made compulsory (for larger farms) as a condition to apply for compensatory payments. The reform included specific instruments ('accompanying measures') to encourage less intensive production, both to reduce market surpluses and to alleviate environmen-

tal pressures. These included an early retirement scheme, an afforestation scheme and an agri-environment scheme which was mandatory for Member States to introduce. Member States were obliged to apply 'appropriate environmental conditions' to the management of compulsory set aside in arable cropping, and were allowed to introduce environmental conditions on the direct payments offered as headage subsidies for beef cattle and sheep. However, the UK was one of the few to apply conditions to livestock subsidies (Alliance Environment, 2007).

The coming into force of the Single European Act (1987) added a title on the environment to the European treaties and, for the first time, gave a legal basis for EU environmental policies. The growth in environmental awareness led to the introduction of a raft of environmental legislation affecting agricultural practices. Among the more important were the Nitrates Directive (1991), the Pesticides Regulation (1991), the Habitats Directive (1992) and the Water Framework Directive (2000). Following the Rio Summit on Sustainable Development in 1992, the Amsterdam Treaty (1997) made sustainable development one of the Community's tasks and clarified the basis for environmental policy. The Cardiff process, which required the various formations of the EU Council of Ministers to develop comprehensive strategies to integrate environmental concerns within their respective areas of activity, began in 1998. The Agricultural Council's response was embodied in the Agenda 2000 reform (CEC, 1999), which thus can lay claim to being the real start to the process of integrating environmental objectives into agricultural policy.

Under the 'horizontal measures' regulation establishing common rules for direct support schemes under the CAP, Member States were required from 1 January 2000 to apply environmental measures they considered appropriate in view of the land used and the production concerned using one of three options (Regulation (EC) 1259/1999). First, implementation of appropriate agri-environment measures applied under rural development programmes could be sufficient. Second, Member States could make direct payments conditional on observance of generally applicable mandatory environmental requirements. Third, Member States could attach specific environmental conditions to the grant of payments under a market regime where the environmental situation requires additional efforts. Member States could use the proceeds from withholding payments in cases of non-compliance with environmental measures or from reducing payments to larger farms (modulation) to fund increased expenditure on environmental measures in Pillar 2. In practice, Member States were slow to use the new opportunities. Few countries introduced new environmental standards through cross compliance and only two Member States chose significantly to expand expenditure on agri-environment and other accompanying measures through the use of modulation (Baldock, Dwyer, and Sumpster, 2002).

Separately, under the rural development regulation (Regulation (EC) 1257/1999), farmers in receipt of the less favoured areas allowance and participating in AEMs were required to observe 'usual good farming practice', while those granted one-off aids (investment, young farmers, processing and marketing) were required to observe 'minimum standards regarding the environment'. Payments of compensatory allowances under the LFA directive were changed to an area basis to reduce the tendency to overstock resulting from the headage payment system. Usual good farming practice was defined as the standard of farming which a reasonable farmer would follow in the region concerned (Regulation (EC) 1750/1999). Member States were required to set out verifiable standards in their

rural development plans which, in any case, should entail compliance with general mandatory environmental requirements. These requirements for Pillar 2 payments were the precursor for cross compliance in Pillar 1 in the MTR reform in 2003.

With the implementation of the MacSharry and Agenda 2000 reforms, EU farm support was characterised by a mixture of market price support and production-limited direct payments. This regime was threatened by the opening of agricultural trade liberalisation negotiations in 1999 in the WTO following the completion of the Uruguay Round Agreement on Agriculture. The EU along with a number of other countries developed the concept of multifunctionality to try to defend these payments in the forthcoming negotiations, building on the commitment (in Article 20(c) of the Agreement) that in negotiating the continuation of the agricultural policy reform process 'non-trade concerns' would be taken into account (Norwegian Ministry of Agriculture, 2000). Multifunctionality asserts that agricultural production produces a range of valued outputs including not only food but also environmental protection, landscape preservation, rural vitality and other public goods. Importantly, these multifunctional outputs are jointly produced so that a decline in production would also lead to a reduction in these accompanying services. To maintain the public goods provided by agriculture it was thus necessary to continue to be able to use coupled payments.

The multifunctionality concept gave rise to a significant research agenda, not least at the OECD (OECD, 2001, 2003) which identified the degree of jointness in production as a key determinant in policy choice. Jointness was found to vary significantly depending on which non-commodity output was in question. It was rarely or never found to exist in fixed proportions, but to vary by farm, region, or production system. With the decoupling of direct payments in the MTR the EU's payments moved into the green box in WTO terminology and were no longer threatened by reduction commitments. As a result, the EU lost interest in promoting multifunctionality although it still survives in the arguments for coupled payments for suckler cow and sheep production in marginal farming areas to prevent land abandonment.

While the MTR is known principally for the decoupling of direct payments, it also strengthened the integration of environmental objectives into the CAP (Regulation (EC) 1782/2003). Cross compliance which was introduced as a voluntary option for member states in the Agenda 2000 reform became mandatory with the 2003 reform. As of January 2005, for farmers to receive the Single Farm Payment, they had to comply with 19 Statutory Management Requirements (SMRs) – five of which are environmental – and with a number of standards to ensure the 'good agricultural and environmental condition' (GAEC) of agricultural land. The SMRs are based on pre-existing EU directives and regulations, while GAEC was a new requirement and consisted of 11 standards relating to soil erosion, soil organic matter, soil structure and a minimum level of maintenance of the land. This approach was extended from January 2007 with respect to the whole holding to beneficiaries receiving aid with regard to eight measures under 'Axis 2' of the second pillar of the CAP (art. 51 of Regulation (EC) 1698/2005) (Alliance Environment, 2007). The reform also established the obligation to maintain the ratio of permanent pasture to the total agricultural area at either the national or regional level in view of its positive environmental effect. Compulsory set aside was continued, and the environmental benefits connected with the measure were highlighted. A new Article 69 was introduced which allowed Member States to retain up to 10% of the previously coupled payments in spe-

cific sectors (arable crops, beef and sheep) to support specific types of farming which are important for the environment or for improving the quality and marketing of agricultural products. Also important was the transfer of funds from the first to the second pillar of the CAP through a progressive reduction of direct payments to be used for the funding of rural development measures (modulation). Furthermore, it became compulsory for Member States to allocate 25% of their Pillar 2 funding in the 2007-2013 programming period to Axis 2 measures covering land management and agri-environment measures.

The Health Check agreement in 2008 was primarily concerned with completing the MTR reforms by moving to decouple most of the remaining coupled payments, agreeing the abolition of milk quotas, as well as transferring additional funds from Pillar 1 to Pillar 2 through modulation (Regulation (EC) 73/2009). Coupled payments at the current level or below were only permitted for the suckler cow and sheepmeat and goatmeat sectors where maintaining a minimum level of agricultural production may be necessary for the agricultural economies in certain regions and, in particular, where farmers cannot have recourse to other economic alternatives. The possibility to make payments to specific sectors up to 10% of direct payment national ceilings was continued, but the menu of options was expanded under the now-relabelled Article 68. Uses can now include protecting the environment, improving the quality and marketing of products (as previously permitted under Article 69) or for animal welfare support; payments for disadvantages faced by specific sectors (dairy, beef, sheep and goats, and rice) in economically vulnerable or environmentally sensitive areas as well as for economically vulnerable types of farming; top-ups to existing entitlements in areas where land abandonment is a threat; support for risk assurance in the form of contributions to crop insurance premia; and contributions to mutual funds for animal and plant diseases. Schemes to protect the environment should be designed in the same way as AEMs in Pillar 2; they must build on the cross compliance baseline and the payment can only cover the additional costs actually incurred and income foregone. This particular measure clearly blurs the supposedly distinctive characteristics of measures funded by Pillar 1 and Pillar 2 as it allows 100% EU financing for multi-annual environmental measures undertaken voluntarily by farmers. From a slow start, some Member States have started to use Article 68 for environmental objectives, including schemes for supporting permanent grassland under low-intensity use (e.g. in Denmark), and for local high nature value farming support schemes (in the Burren, Ireland), while France has moved its *prime à l'herbe* grassland support scheme out of Pillar 2 and is now funding it under Article 68 of Pillar 1.

Cross compliance standards were adjusted and simplified in the Health Check. Two new issues were added to GAEC standards in relation to the 'protection and management of water' and to 'protect water against pollution and run-off and manage the use of water', with associated new related standards. A more contentious element was the division of GAEC standards into those that are mandatory and those that are optional. This was seen by some environmental organisations as weakening the environmental baseline as well as opening up the possibility of an unequal mandatory baseline across Europe (IEEP, 2008b). Also significant was the abolition of compulsory set aside from 2009 (after agreement to set the set aside rate at 0% in 2008) in response to tight world market supplies. The loss of the environmental benefits of set aside (in place for arable farmers since 1994) was a significant negative outcome of the Health Check reform. An optional standard to provide for the establishment

and/or retention of habitats was introduced specifically to offset the loss of environmental benefits from the abolition of set aside. A potentially important limitation on the use of farming standards by Member States was the addition of a prohibition that *'Member States shall not define minimum requirements which are not foreseen in that framework'*.

The Commission had identified four new 'challenges' – climate change, renewable energies, water management and biodiversity, later extended to include innovation in these environmental areas and accompanying measures for dairy – which it wanted to address in Pillar 2. It proposed to further modulate resources from Pillar 1 to finance additional activities to address these challenges. The modulation elements of the Commission's proposal were among the more contentious and were significantly weakened in the final agreement. As an additional inducement, the co-financing rate for the modulated funds was reduced to 25% and to as low as 10% in convergence regions. Member States were required to amend their rural development programmes to show how they planned to use these new resources to address these challenges (IEEP, 2008b).

3. Assessment of CAP environmental measures

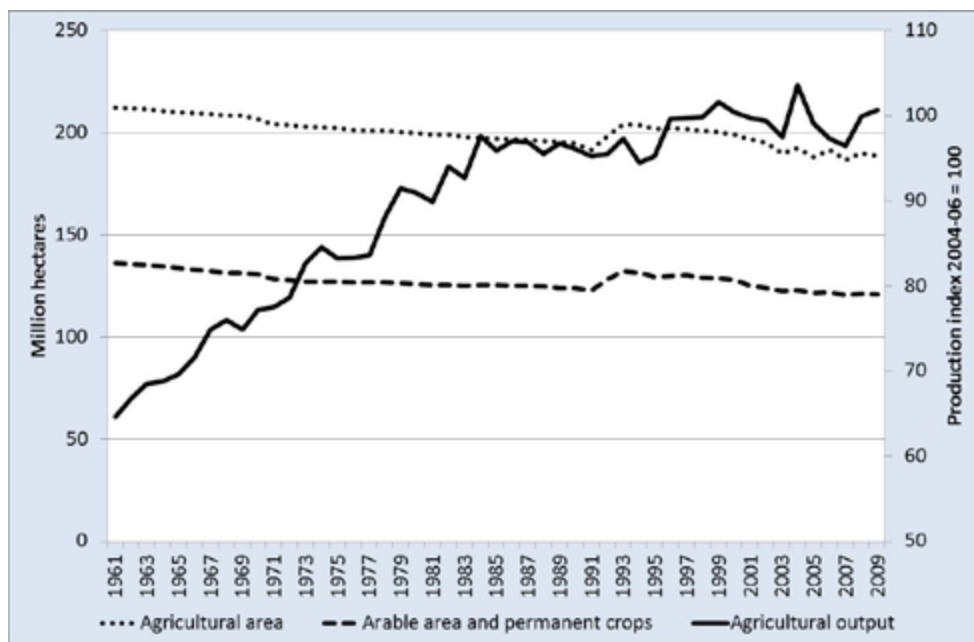
This section briefly evaluates the experiences to date with the different CAP instruments to target environmental objectives. The other major influence on the environmental impact of agricultural production is the body of environmental legislation introduced since the 1990s, but we do not discuss this further in this paper.

Decoupling

The move from market price support to direct payments was itself an important contribution to reversing some of the pressures for intensification and environmental damage attributed to the early CAP. Support to EU agriculture declined from 39% of farm receipts in the mid-1980s to 34% in 2002–2004, and to 20% in 2009–2011 (as measured by the OECD Producer Support Estimate). More important, almost all (98%) of this support in EU15 was output and input linked in the mid-1980s, falling to 70% in 2002–2004 and 52% in 2009–2011 (OECD, 2013). While it is important to avoid attributing causation to correlation, it is striking how the upward increase in EU agricultural output came to a halt at the same time as the implementation of the MacSharry reform and has stagnated since that time (Figure 1). As agricultural productivity has continued to increase during this period, this implies reduced use of inputs and not only land.

Decoupling leads to less intensive production because it reduces the effective market price received by producers. A profit-maximising producer would use inputs, such as fertilisers or chemicals, up to the point where the expected marginal return from using an additional unit of input equals its marginal cost. Lowering the effective market price lowers the expected marginal return, and thus reduces the optimal input usage. Overall production was expected to fall as a result of decoupling (relative to the counterfactual) and to be produced under more extensive (less input-intensive) conditions.

Although the theoretical conclusion is clear, empirical evidence to support a causal link between decoupling and lower input use is harder to find. Ex-post studies examine the

Figure 1. EU-27 production and land use changes, 1961-2009

Source: FAOSTAT

Note: The figures are for the 27 current Member States over the whole period. The trend is influenced by the fall in agricultural output in the new Member States following their transition to market economies after 1989 but as their share of EU27 output is only around 15% the trend also accurately reflects the evolution in the old Member States

trend in input use pre-and post decoupling. For example, LMC International (2005), using FADN farm survey data, found that fertiliser use had declined in a number of countries following the MacSharry reform (which decoupled arable payments from yield), but there were several exceptions to this finding. They concluded that the FADN data were broadly consistent with the hypothesis that there has been a general reduction in the intensity of cereal farming, but the evidence was neither clear-cut nor particularly strong. One reason is that decoupling also encouraged a reshuffling in the portfolio of crops grown and different crops have different input requirements. In Italy, for example, Vollaro (2010) found that the expansion of profitable crops like vegetables, flowers and vineyards, along with the receipt of the single payment, increased expenditure on fertilizers and crop protection inputs. Other studies using simulation modelling methodologies have found that decoupling reduced the incentive for intensification and use of inputs but that impacts on pollution risk are fairly insignificant (Brady, 2011). This is because pollution is influenced primarily by crop-specific characteristics given the geophysical characteristics of a region, and the balance between crop and livestock output, rather than the level of production per se.

The environmental impact of direct payments can be strengthened by attaching conditions for eligibility (cross compliance rules are discussed in the next section). In the case

of coupled payments, setting maximum areas or maximum numbers of animals for aid as under the MacSharry reform limits the scope for intensification. Stocking rate restrictions were another mechanism used to discourage intensification. For the basic beef premium introduced in the MacSharry reform, payments were only made on animals up to 2 Live-stock Units (LU)/ha. For the additional extensification premium, a maximum level of 1.4 LU/ha was established, calculated on the basis of the total number of adult bovine animals and sheep and goats.

Set aside originally introduced for supply control purposes had important environmental benefits especially where land was left fallow (the obligation could also be fulfilled by cultivating non-food crops on set aside land). The scheme was obligatory for larger (commercial) arable crop producers. Set aside could be either rotational or non-rotational, with different environmental benefits. Farmers could volunteer to set aside a larger share of their land than that stipulated in the regulations. The proportion of the arable crop area that commercial producers had to put into set aside varied from year to year, between 5% and 17.5%, and was reduced to 0% for the 2008 harvest before the scheme was abolished in the following year. Over the 2000-2006 period, set aside land covered on average around 6 million ha (around 4 million ha being compulsory set aside), mainly concentrated in the EU-15 and representing around 8% of total arable land. Around 800-900,000 ha of set aside land was cultivated with non-food crops (Areté Consulting, 2008).

Re-introducing fallow land into arable rotations delivered a range of environmental benefits (IEEP, 2008a). The benefits depended on a variety of factors, such as the specific environmental and climatic conditions of the areas concerned by the measure, the type of set aside (fallow, rotational, seeded etc.), the features of the green cover on set aside land, and the land management practices applied but were generally assessed as positive, particularly for water consumption, nitrogen losses, biodiversity, GHG emissions and energy consumption (Areté Consulting 2008). However, where set aside land was used for the cultivation of energy crops, its environmental impacts generally are not dissimilar to those of the main alternative conventional agricultural systems.

The main environmental threat foreseen from decoupling was that it could lead to the abandonment of farming in marginal farming areas where the environmental services depend on farming activities taking place. In the CAP itself, the first compensatory allowances for less favoured areas (LFAs) were introduced in 1975 to ensure the continuation of farming in areas where natural handicaps caused lower agricultural productivity and farming was becoming vulnerable. In marginal agricultural regions, decoupling risks having a negative impact on biodiversity and landscape mosaic because of the homogenisation of land use that results from land being taken out of production. Model simulations show that voluntary AEMs and national support can act to buffer the full potential impacts of decoupling on landscape values in these regions. Also the GAEC standards to maintain a minimum level of farming activity help to mitigate the expected effects of the reform (Brady *et al.*, 2009).

Respect for environmental standards and cross compliance

It is only when farmers are in receipt of direct payments that requiring them to observe particular management practices beneficial to the environment through cross

compliance becomes possible; market price support benefits all producers regardless of their production practices. The steady evolution of environmental conditionality, from voluntary to mandatory, and from Pillar 2 to Pillar 1, was described in the previous section. The standards are derived either from EU legislation (SMRs) or form part of a Member State's definition of good agricultural and environmental condition (GAEC). Furthermore, Member States have to ensure that the ratio between arable and grassland does not decrease more than 10% to the detriment of grassland at regional level, compared to the year 2003 (new Member States have a different base year). The current GAEC framework following the Health Check which distinguished between compulsory and optional standards is set out in Table 1.

Table 1. EU Framework of issues and standards for Good Agricultural and Environmental Condition

Issue	Compulsory standards	Optional standards
Soil erosion: Protect soil through appropriate measures	- Minimum soil cover	- Retain terraces
	- Minimum land management reflecting site-specific conditions	
Soil organic matter: Maintain soil organic matter levels through appropriate practices	- Arable stubble management	- Standards for crop rotations
Soil structure: Maintain soil structure through appropriate measures		- Appropriate machinery use
Minimum level of maintenance: Ensure a minimum level of maintenance and avoid the deterioration of habitats	- Retention of landscape features, including, where appropriate, <i>hedges, ponds, ditches trees in line, in group or isolated and field margins</i>	- Minimum livestock stocking rates or/and appropriate regimes
		- <i>Establishment and/or retention of habitats</i>
	- Avoiding the encroachment of unwanted vegetation on agricultural land	- Prohibition of the grubbing up of olive trees
	- Protection of permanent pastures	- Maintenance of olive groves and vines in good vegetative condition
Protection and management of water: Protect water against pollution and run-off, and manage the use of water	- <i>Establishment of buffer strips along water courses (implemented by 2012)</i>	
	- <i>Where use of water for irrigation is subject to authorisation, compliance with authorisation procedures</i>	

Note: Standards shown in *italics* were added in 2009

Source: Annex III of Regulation (EC) 73/2009

The EU regulation on cross compliance leaves many details of design and implementation to the discretion of individual Member States and its regions. EU legislation, e.g. the Nitrates Directive, does not apply directly to individual farmers but rather to the Member State. Farm-specific requirements have to be transposed into national legislation by the Member States which thus determine what specific management requirements will apply to farmers. Farmers' obligations to ensure GAEC are often based on or adapted from previously existing standards of 'good farming practice'. National GAEC standards may have previously been implemented in national legislation (often for specific areas such as protected areas or nitrate vulnerable zones) or may have been non-statutory (e.g. promoted by the advisory services). As for SMRs, there are differences in how Member States have interpreted and implemented the GAEC standards (Alliance Environment, 2007). Member States are also required to establish an inspection and enforcement system, with reduction or withdrawal of direct payments for those farmers who do not comply with the SMR and GAEC standards.

Pillar 2 agri-environment measures

AEMs in Pillar 2 have the dual role of 'supporting the sustainable development of rural areas and in responding to society's increasing demand for environmental services' (Regulation (EC) 1698/2005). AEMs are designed and implemented by Member States or regions as part of their rural development programmes (RDPs). It is currently the only measure that all Member States/regions must include in their RDPs. The measure functions by supporting voluntary commitments (beyond a baseline set by cross compliance) undertaken for a period of five years or longer by farmers and other land managers who enter a management agreement that requires specific environmentally-friendly standards to be met. Commitments can cover the following activities: organic farming, integrated production, other extensification of farming systems (i.e. fertilisers and pesticides reduction, extensification of livestock); diversification of crop rotations; reduction of irrigation; action to conserve soil; management of landscape and pastures; actions to maintain habitats favourable for biodiversity; genetic resources; and other targeted actions which for example include the use of integrated environmental planning. To ensure WTO compatibility payments are based on costs incurred and income foregone, with the possibility of paying for transaction costs in addition. Other environmental measures in Pillar 2 include payments related to Natura 2000 areas, the Water Framework Directive, Natural Handicap Areas, forests and environmental investments. Also measures that support training and the diffusion of knowledge and information, as well as support to the setting-up and use of advisory services, play an important role in improving knowledge of farmers and foresters on environmental matters and in the uptake of more environment-friendly management practices.

In 2009, the agricultural area under AEMs amounted to nearly 38.5 million ha and represented 20.9% of the UAA in the EU-27 (DG AGRI, 2011). Use of AEMs varies widely between Member States. This share was significantly higher in the EU-15 (25.2% or 33.5 million ha) than in the EU-12 (9.7% or 5 million ha). Some countries (Luxembourg, Finland, Sweden and Austria) had more than two-thirds of their UAA enrolled in agri-environmental commitments, but in 8 other countries (Portugal, Cyprus, Malta, Romania,

Lithuania, the Netherlands, Poland, Bulgaria) this share was below 10%. Within countries, schemes tend to be more attractive to farmers who are already farming in a less-intensive way, and it has been difficult to attract more intensive farmers and farmers in more intensively-farmed regions to participate. Enrolment also fluctuates in response to the rhythms of programming and budget cycles.

AEM design and therefore effectiveness in terms of delivery varies widely. Design is partly a trade-off between environmental effectiveness and administrative complexity and cost. Effectiveness is also influenced by the relative importance of farm income versus environmental objectives in the design of the scheme. The degree to which these measures have led to an improvement in the environmental performance of agriculture is a matter of continued debate. The environmental impacts of Pillar 2 measures are monitored through mid-term and *ex post* evaluations of past and current RDPs and data on indicators within the Common Monitoring and Evaluation Framework. However, the level of detail of the evidence provided varies considerably between Member States, making EU wide assessments problematic (ECA, 2011; OECD, 2011). One recent literature review concluded that they have had mixed success depending on the schemes and indicators under investigation (Uthes *et al.*, 2011). There is some evidence that AEMs reverse negative trends in bird monitoring data, particularly in diversified, small-scale landscapes. Studies in intensively farmed regions usually reported less successful results and concluded that much more and different conservation efforts are needed. A recent review of AEM implementation by the European Court of Auditors drew attention to the need for more monitoring and recommended for the next programming period that AEM expenditure should be more precisely targeted; that there should be a clear distinction between simple and more demanding agri-environment sub-measures; and that Member States should be more pro-active in managing agri-environment payments (ECA, 2011).

Conclusions on Pillar 1 payments and environmental objectives

The EU has followed two approaches to integrating environmental objectives into the CAP. The first, within Pillar 1, is to add respect for environmental standards as a condition to receive direct payments and to couple some payments to specific types of farming which are important for protection and enhancement of the environment. The second, within Pillar 2, is to remunerate farmers who voluntarily agree to implement practices beneficial for the environment beyond the baseline level. However, the relative funding levels for these two approaches is very different and, despite a widespread perception, there has been no shift to a greater emphasis on AEMs within Pillar 2 over time (Table 2).

Comparisons are made difficult because direct payments are annual payments where changes from year to year reflect policy decisions, mainly the decision to phase in direct payments to the new Member States after their accession in 2004 and 2007 respectively. Pillar 2 payments show a different rhythm as they are linked to programming periods and payments reflect issues to do with policy implementation as much as policy change. Payments made fell in 2007, the first year of the new programming period, because of the time taken for approval of new programmes and to enter into contracts with farmers and others to spend the money. Within Pillar 2, AEMs are less affected by this disruption because pay-

Table 2. Relative importance of expenditure on direct payments in Pillar 1 and environmental payments in Pillar 2, € million and percent

Chapter	2000-06 average	2007	2008	2009	2010	2011	2007-11 average
€ million							
Direct aids	29,861.3	37,045.8	37,568.6	39,113.9	39,675.7	40,178.0	38,716.4
Total Pillar 2	4,705.6	2,517.4	6,064.5	8,204.3	10,677.0	12,175.0	7,927.6
Axis 2 measures	3,456.3	2,054.3	4,546.5	4,740.7	5,437.2	5,834.5	4,522.6
AEMs in Axis 2	2,053.9	1,204.0	2,312.0	2,547.5	2,897.4	3,077.0	2,407.6
Share Pillar 2 (1)	13.6%	6.4%	13.9%	17.3%	21.2%	23.3%	17.0%
Share Axis 2 (1)	10.4%	5.3%	10.8%	10.8%	12.1%	12.7%	10.5%
Share AEMs (1)	6.4%	3.1%	5.8%	6.1%	6.8%	7.1%	5.9%
Share Axis 2 (2)	73.5%	81.6%	75.0%	57.8%	50.9%	47.9%	57.0%
Share AEMs (2)	43.6%	47.8%	38.1%	31.1%	27.1%	25.3%	30.4%

Notes: Two measures of agri-environment expenditure are shown in this table. AEM expenditure refers only to expenditure on agri-environment measures, while all Axis 2 measures include natural handicap payments to farmers in disadvantaged areas, Natura 2000 payments, and afforestation payments as well as AEM payments. Annual expenditure is from Q4 of the previous year to Q3 of the year shown. It represents payment claims declared by Member States. The 2000-2006 figures may not be fully comparable due to methodological differences between the two programming periods. Shares labelled (1) are the ratio of the chapter heading to the sum of direct payments and the chapter heading. Shares labelled (2) are the ratio of the chapter heading to total Pillar 2 expenditure.

Sources: 2000-2006 figures DG Agriculture *Rural Development in the European Union 2007*; 2007-2011 figures are from DG Agriculture Financial Reports for the EAGF and the EAFRD for the respective years.

ments continue to be made to farmers who enrolled in AEMs in the previous period and because AEMs are among the first RDP measures that are implemented at the beginning of a programming period. Thus, we observe the relative importance of Pillar 2 expenditure increasing over time, but within Pillar 2 the relative importance of AEM expenditure is decreasing year on year in the current programming period. With two years to go, the 2007-2011 annual averages may provide a reasonable guide to the final outcome.

Within the rural development budget, there is a strong environmental focus. According to the RDPs submitted by Member States, 45% of the EAFRD funding for the 2007-2013 period (some €43 billion) has been allocated to Axis 2 measures ('improving the environment and the countryside'). Around half of this funding, €22 billion, will be spent on agri-environment measures; €472 million will be spent on Natura 2000 measures on farm land; and €111 million on Natura 2000 measures on forestry land (CEC, 2011c, Annex 2). Actual expenditure figures show that, if anything, Axis 2 measures have been even more important to date and that AEM expenditure has maintained its projected share of around 50% (Table 2). However, the relative importance of Pillar 1 and Axis 2 payments has not changed in the current programming period. Indeed, based on expenditure figures to date, the share of AEM expenditures has declined compared to the previous programming period both with respect to Pillar 1 and Pillar 2 payments, even if the absolute amounts, in nominal terms, show an increase.

The continued importance of Pillar 1 payments in delivering environmental benefits shows how entrenched is the support for these payments – this was evident in the watering-down of the Commission's modulation proposals in the 2008 Health Check (IEEP 2008b). This is mainly because of the importance of direct payments in providing income support to EU farmers. But an influential secondary narrative defends direct payments as the basis for the delivery of public goods through agriculture.⁵ Lumbroso and Garvey (2013) point to the paradox that, from a strong argument for radical reform, the public goods argument has become a legitimisation tool for existing measures and a by-product of income support. Indeed, it is only because it is linked to direct payments that cross compliance retains its effectiveness. At the same time, the new legitimacy conferred by cross compliance hampers the reallocation of funds in favour of more targeted rural development measures. We return to this paradox in the conclusion.

This narrative also sheds light on what is considered to be the appropriate environmental reference level. Even if cross compliance is the baseline for Pillar 2 voluntary AEMs, the argument that direct payments in part compensate farmers for the high environmental standards required by cross compliance indicates that, in practice, the environmental reference level is lower, potentially as low as the SMRs which are the legal mandatory EU requirements. In practice, in some countries, some GAEC standards would also be backed by national legislation which raises the environmental reference threshold. This point is overlooked by proponents of more radical CAP reform. Not only would more radical reform imply the gradual elimination of most untargeted Pillar 1 direct payments in favour of AEMs in Pillar 2, but it would also require securing the environmental benefits currently due to GAEC standards. Whether this would be done by transferring the GAEC standards to broad-based entry-level AEMs (implying that society continues to bear the costs of meeting these standards) or by transforming the GAEC standards into legislation (thus placing the onus of meeting the standards on farmers) will reflect society's view of the appropriate allocation of property rights in the environment, taking into account the impact on agriculture's competitiveness.

4. Commission's post-2013 greening proposals

Promoting sustainable management of natural resources and climate action is one of the three stated objectives of the CAP post-2013. In pursuing this objective, the Commis-

⁵ According to the Commission: *'Decoupled direct payments provide today basic income support and support for basic public goods desired by European society.'* (CEC 2010, 4). This is further developed in the impact assessment as follows: *'Without basic income support, the less competitive farmers who very often manage marginal land and land in remote areas in an extensive manner, thereby helping to maintain areas of high natural value, may cease their agriculture activity because they no longer make a sustainable income; moreover, GAEC that are part of the baseline for agri-environment measures no longer apply to land that does not receive direct payments.'* (CEC 2011a, Annex 2). According to COPA-COGECA: *'Direct payments under pillar 1 enable EU farmers to provide a series of public benefits as a result of their farming activity which are valued by society but are not currently rewarded by the market and, in many cases, will never be.'* (Copa Cogeca, 2010, p 13). The Agricultural Council underlined: *'that direct income support to EU farmers currently contributes to ensuring a fair standard of living for the agricultural community; it also enhances the provision of public goods and services by farmers for which the market does not pay, and BROADLY AGREES that this support has proven its worth and will remain an essential element in the CAP towards 2020, notably in the context of the additional costs producers face in meeting the EU's high environmental and animal welfare standards.'* (Council of the European Union 2011).

sion had the choice to emphasise either greening Pillar 1 (by raising the cross compliance threshold or otherwise adding environmental conditions to part or all of direct payments) or to further modulate funds from Pillar 1 to Pillar 2 with a view to expanding the scale of AEMs. The policy advice to the Commission, from the OECD and other sources, would be to favour the transfer of funds to more targeted measures in Pillar 2. In fact, the Commission chose a variant of the former approach in proposing a 'green' payment in Pillar 1 to farmers following a mandatory set of farm practices contributing to the environment. However, it now looks as if the legislature (Council and Parliament) will water down this proposal to such an extent that the additional benefits for the environment will be very minimal. In this section, the Commission's proposal is described and the reactions to it are examined with a view to understanding the reasons for the apparent failure of the Commission's strategy.

The Commission began its reflections of the CAP post-2013 in its November 2010 Communication which outlined three potential directions for the CAP which it called the adjustment, integration and refocus scenarios, respectively (CEC, 2010). This Communication contained for the first time the proposal to introduce a top-up payment in Pillar 1 as part of a greening strategy. Specifically, the Communication proposed:

Enhancement of environmental performance of the CAP through a *mandatory 'greening' component of direct payments* by supporting environmental measures applicable across the whole of the EU territory. Priority should be given to actions addressing both climate and environment policy goals. These could take the form of simple, generalised, non-contractual and annual environmental actions that go beyond cross compliance and are linked to agriculture (e.g. permanent pasture, green cover, crop rotation and ecological set aside). In addition, the possibility of including the requirements of current NATURA 2000 areas and enhancing certain elements of GAEC standards should be analysed. (italics added)

The Communication attributed the idea of restructuring Pillar 1 payments to the European Parliament. However, the Parliament's resolution in July 2010 (based on the Lyon report) called for the vast bulk of agricultural land to be covered by agri-environment measures and for additional incentives for improved environmental management to be delivered through an enlarged Pillar 2 budget (European Parliament, 2010). It mentions the idea of a top-up payment in Pillar 1 but in the context of multi-annual contracts linked to carbon reduction/sequestration and biomass products.⁶ In its resolution responding to the Communication (based on the Dess report), the Parliament accepted that 'natural resource protection should be more closely linked to the granting of direct payments and calls, therefore, for the introduction, through a greening component, of an EU-wide incentivisation scheme with the objective of ensuring farm sustainability and long-term food security through effective management of scarce resources (water, energy, soil) while reducing production costs in the long term by reducing input use' (European Parliament, 2011).

⁶ The resolution reads (paragraph 71): 'Believes that an EU-funded top-up payment should be made available to farmers through simple multiannual contracts rewarding them for reducing their carbon emissions per unit of production and/or increasing their sequestration of carbon in the soil through sustainable production methods and through the production of biomass that can be used in the production of long-lasting agro-materials;' (European Parliament, 2010).

It specified that 'further greening should be pursued across Member States by means of a priority catalogue of area-based and/or farm-level measures that are 100% EU-financed; considers that any recipient of these particular payments must implement a certain number of greening measures, which should build on existing structures, chosen from a national or a regional list established by the Member State on the basis of a broader EU list, which is applicable to all types of farming; considers that examples of such measures could include: support for low carbon emissions and measures to limit or capture GHG emissions; support for low energy consumption and energy efficiency; buffer strips, field margins, presence of hedges, etc.; permanent pastures; precision farming techniques; crop rotation and crop diversity; feed efficiency plans'. These ideas prefigure the flexibility options put forward in the debate on the Commission's legislative proposals following their publication.

The Commission's intentions were elaborated in its proposal for the next Multi-annual Financial Framework in July 2011 which called for 30% of direct support to be made conditional on 'greening' to ensure that the CAP helps the EU to deliver on its environmental and climate action objectives, beyond the cross compliance requirements of current legislation (CEC, 2011d). In its legal proposals presented to the European Council and the European Parliament setting out proposed changes to the Common Agricultural Policy (CAP) for the post-2013 period on 12 October 2011, the greening requirements were specified to include ecological focus areas (EFAs), crop diversification and the maintenance of existing areas of permanent pasture at farm level. Participants in the proposed small farmers' scheme are exempt and organic farmers would automatically receive the greening payment (CEC 2011c).

Other greening elements included in the draft regulations include changes to GAEC standards, a revamping of Pillar 2 AEMs and a more important role for the Farm Advisory Service in facilitating innovations to deliver climate change and environmental objectives. The changes to the GAEC standards were driven in part by a simplification agenda and results in a new framework arranged into four thematic areas and nine issues (CEC, 2011e, Annex II). Certain articles from the Birds and Habitats Directives were removed from the SMR requirements. Member States are required to develop new GAEC standards for maintaining soil organic matter and protecting wetland and carbon rich soils. The compulsory GAEC on '*avoiding the encroachment of unwanted vegetation on agricultural land*' has been removed. Although this was seen as a way of avoiding the abandonment of agricultural land, it was also criticised as driving the removal of habitat in several Member States. The optional GAEC standards for '*appropriate machinery use to maintain soil structure*', minimum livestock stocking rates and/or appropriate regimes and '*establishment and/or retention of habitats*' have also been removed. Requirements related to the Water Framework Directive and Sustainable Use of Pesticides Directive would become part of cross compliance once implemented by all Member States. Participants in the small farm scheme would be exempted from cross compliance requirements. The restriction that Member States shall not define minimum standards which are not established in the relevant Annex is continued. Despite the potential significance of some of these changes for environmental management, the real novelty of the Commission's proposals was its attempt to define and fund mandatory green standards applicable across the EU which could be administered as a Pillar 1 direct payment.

In its impact assessment of the proposals in the 2010 Communication, the Commission asked the question whether it would not be simpler to use part of Pillar I funding for complying with environmental measures within rural development policy instead? *'Seen from the perspective of providing choice for the farmers, it would seem preferable to envisage measures with payment levels differentiated by measures according to cost incurred and income forgone, as well as to give more discretion to Member States for their design so as to tailor them as much as possible to specific situations'* (CEC, 2011c, Annex 2, p. 14).

Its objection to this approach was that it would give too much discretion to Member States and farmers. Even in a best case scenario, it would not link the greening requirements to Pillar I payments and it would not cover the entire EU territory. This would be partly because of insufficient budget resources (comparing existing premia in AEMs with the future payment levels for the greening component) as well as the varied uptake of agri-environment across Member States. The Commission saw particular problems for climate change objectives as it would leave open the possibility for only a part of the farm to adopt climate friendly practices while the rest of the farm continues to be operated with potentially detrimental methods undermining the global result.

The Commission also considered and rejected the option to include the greening requirements as part of GAEC standards. *'To make the greening effective, the measures in the greening component should be compulsory for the farmer, the discretion left to the Member State limited, and sanctions effective. If greening is effectively a requirement in the direct payments system, then wouldn't it be simpler to work instead on enhancing cross compliance?'* (CEC, 2011c, Annex 2, p. 13).

It responded to this question as follows: *'Although this line of reasoning is put forth arguably on simplification grounds, it hides the complexities inherent in Member States defining and administering GAEC tailored to regional specificities. As the experience with the optional GAEC on crop rotation has shown, this approach would not necessarily ensure that the entire EU territory is effectively greened. At the same time, it would meet with considerable resistance from farmers as it would be framed as a requirement rather than an incentive, and arguably do away with the political visibility of greening direct payments that is one of the main drivers of this reform'* (CEC, 2011c, Annex 2, p. 13).

These passages point to the concerns the Commission had when formulating its greening proposal. It wanted a universal set of measures which would apply to all farms, it wanted to avoid giving Member States discretion, it wanted farmers to see this as an incentive rather than an imposition, but most particularly, it wanted greening to be associated with Pillar 1 payments in order to promote their legitimacy and to provide an additional justification for maintaining the Pillar 1 budget of the CAP.

The Commission's proposals gave rise to a lively and mostly critical debate (Hart and Little, 2012; House of Commons, 2012; Matthews, 2012, 2013). In February 2013, the legislative process has not yet been concluded. But enough is known of the positions of the main players to suggest that the outcome will be much less ambitious than what the Commission proposed, which itself was strongly criticised by environmental NGOs as an inadequate response to the stressed state of Europe's natural environment (Birdlife *et al.*, 2011). The following resumé of the state of play is based on the European Council conclusions on the next MFF at its February 2013 meeting (European Council, 2013); the summary by the Cyprus Presidency of the discussions in the Agricultural Council in December 2012

(Council of the European Union, 2012), and the amendments to the Commission's legislative proposals adopted by COMAGRI in January 2013 (European Parliament, 2013). Virtually all the amendments to the legislative drafts indicate a considerable weakening of the Commission's proposals.

1. The conditions attached to the three greening measures proposed by the Commission (crop diversification, ecological focus areas, maintaining permanent pasture) will be relaxed or eliminated, for example, by raising the minimum farm size threshold where the measures apply or extending the types of land uses that count towards EFAs. For example, the European Council particularly specified that "The requirement to have an ecological focus area (EFA) on each agricultural holding will be implemented in ways that do not require the land in question to be taken out of production and that avoids unjustified losses in the income of farmers" (European Council, 2013, p. 27).
2. Greening will effectively be made voluntary by limiting the penalty for non-compliance to the loss of the green payment excluding the possibility of also reducing the basic payment as proposed by the Commission. This is despite the Commission's insistence that mandatory participation in the green payment is essential if the measures are to be effective.
3. Additional 'equivalent' greening measures will be introduced in the name of flexibility. Although flexibility in the implementation of environmental measures is often positive, it leaves open the possibility that the equivalent measures selected may have even less impact on the environment than what was proposed by the Commission.
4. Farmers will be permitted to qualify for the green payment in Pillar 1 provided they show they are already managing land in an environmentally-responsible way ('green by definition'), for example, through enrolment in a Pillar 2 AEM or in an environmental certification scheme. The problem with these exceptions is that there is clearly no environmental additionality. There is also the risk that farmers might be paid twice ('double funding') for the same practices both in Pillar 1 and Pillar 2.
5. It is probable that the Commission's proposals on GAEC standards will be weakened. The elimination of the inclusion of the Water Framework Directive and the Sustainable Use of Pesticide Directive as part of cross compliance once the obligations relevant to farmers have been identified has been recommended by COMAGRI and is likely to be supported in Council.
6. There will be less money for AEMs in the rural development pillar. Not only has the funding for the Pillar 2 budget been reduced in the European Council's conclusions on the next MFF, but flexibility will be given to Member States to shift a proportion of their Pillar 2 budgets to Pillar 1 which could further reduce the funds available for rural development. Rural development programmes are given new tasks, notably income stabilisation and risk management, which could potentially crowd out spending on AEMs. The Commission had proposed that Member States should maintain a minimum spend (25%) of their Pillar 2 budgets on agri-environment and climate measures but only in the preamble to the draft rural development regulation and not in the regulation itself. Here there is a difference between the two legislative bodies, with the Council favouring the Commission's proposal while COMAGRI has proposed to make this a mandatory requirement in the regulation.

It must be stressed again that these are predictions based on negotiations in progress in the two legislative bodies and the final outcome could be different. However, the Commission's proposals look likely to be seriously emasculated when they eventually emerge from the legislative process. Certainly, neither of the two institutions is pushing for a more ambitious greening agenda. We conclude that the additional environmental benefits likely to materialise as a result of adopting the new regulations for the CAP post-2013 will be very minimal, certainly in the context of the budget resources justified by this objective.

5. Final reflections on greening the CAP through Pillar 1

The integration of environmental objectives into the CAP has until now progressed along two tracks: attaching environmental conditions to Pillar 1 payments and supporting voluntary agri-environment measures in Pillar 2. Looking at the history of CAP reform, the Commission might have proposed a redistribution of CAP resources in favour of Pillar 2 and voluntary AEMs. Such a shift would also be in line with OECD recommendations to favour targeted and transparent measures as part of agricultural policy reform. The Commission's proposals for the CAP post-2013 instead proposed to designate 30% of each country's direct payments national ceiling as a 'green' payment conditional on following a set of practices beneficial for climate and the environment. However, we concluded that the eventual legislative outcome is unlikely to lead to major environmental improvements. In this concluding section, we reflect on this apparent failure of the Commission's greening strategy and the reasons for it. A mixture of strategic, technical and political economy factors appear to have played a role.

First, farm organisations, as the main beneficiaries of direct payments under Pillar 1, are naturally its strongest defenders. Direct payments represented on average 29% of agricultural income in the EU in the period 2007-2009 (with total subsidies coming close to 40% of agricultural income) (DG AGRI, 2012). Greening would add to the costs of production although the Commission's calculations suggested that the overall impact would be slight (CEC, 2011c, Annex 2D). It projected an average decrease in overall farm income per worker of between 1.4% and 3.2%. Livestock farms would be more adversely affected because of higher feed costs, while arable farms might even expect to gain because the higher market margin (due the higher market prices caused by the slight reduction in supply) would be sufficient to outweigh the costs of greening. This calculation assumes that farmers would continue to receive the same level of direct payments even in the absence of greening. If greening were the *quid pro quo* for preventing a cut in the direct payments envelope by anything more than 1-3% income reduction calculated above as the cost of greening, then arguably farmers are better off under the Commission's proposals.

Second, the Commission's attempt to establish this *quid pro quo* and to link greening to the size of the CAP budget was never credible. It put forward the green payment in Pillar 1 as a way to enhance the legitimacy of direct payments and to defend its proposal to maintain a constant CAP budget in nominal terms in the next MFF. The promise to green the CAP may have been necessary to gain the support of the College of Commissioners to propose the continuation of CAP funding in the Commission's MFF proposal. The difficulty was that, once the proposal was made, there was no credible threat to reduce direct payments if ambitious greening measures were not adopted. The two legislative bod-

ies worked on the assumption that the budget allocation was exogenous (not necessarily given but not something which would be influenced up or down by decisions taken on greening). There was thus no counterweight to the incentives for agricultural ministers to minimise the additional ‘burdens’ that greening imposes on farmers. While the European Council conclusions on the next MFF endorsed the Commission’s proposal to use 30% of direct payment ceilings for the green payment, this was not linked to any specific level of greening ambition; indeed, the European Council called for ‘a clearly defined flexibility for the Member States relating to the choice of equivalent greening measures.’ By proposing greening as a way of legitimising the existing flow of untargeted Pillar 1 payments to farmers, the Commission framed the issue in a way that it was bound to lose.

Third, the farm organisations had a new card which they played to maximum advantage, namely, food security. During the ‘reform period’ 1992 to 2008, agricultural policy reform and the integration of environmental objectives into agricultural policy were mutually supportive. Decoupling discouraged the use of off-farm inputs, while encouraging more extensive agricultural production helped to limit the budgetary cost of over-production during this period when EU market prices were still above world market levels. But since the 2007-2008 price spike and the growing realisation of the fragility of global food supplies, more emphasis is now put on the necessity for Europe to contribute to increased food production in the name of ‘food security’. This argument is used particularly against the proposal to designate 7% of arable land as EFAs (which, given the existence of trees, hedgerows, field margins and awkward corners on many farms which count towards EFAs implies leaving around 3-4% of cultivated land fallow). It explains the European Council’s decision that EFAs should be implemented in ways that do not require land to be taken out of production. Yet only a few years ago arable farmers had to set aside up to 10-15% of their arable land in order to be eligible for direct payments. The change in the market environment explains the different perceptions of the burden of fallowing land in the two situations.

Fourth, Member State governments were unenthusiastic about the Commission’s proposal. They have no appetite to pursue further greening through Pillar 2 because of the requirement to co-finance this expenditure. But they are concerned about greening in Pillar 1 because of the additional administrative complexity it implies, which flies in the face of the continuing demand from Member States for simplification. Member States have therefore pushed hard for flexibility and the recognition of alternative practices as being equivalent to the Commission’s greening proposals. They have also supported extending automatic eligibility for the green payment (‘green by definition’) to other groups of farmers, e.g. those enrolled in AEMs, for the same reason. In this way, Member State interests have also contributed to the hollowing-out of the Commission’s greening proposal.

Fifth, although the European Parliament was broadly in favour of some further greening of the CAP, its preferred approach was to advocate further reliance on voluntary AEMs in Pillar 2. It never embraced the Commission’s idea of a mandatory green payment in Pillar 1 in return for higher environmental standards (a form of super cross compliance). Instead, it has sought to effectively connect Pillar 2-type AEM measures to the Commission’s Pillar 1 green payment through offering a wider ‘menu’ approach to the practices which would determine eligibility for the payment. While many of these individual measures are worthy and desirable, it is hard to see how they belong to the broad-

brush payments in Pillar 1. By pursuing this approach instead of a more principled position of transferring funds to Pillar 2, the Parliament has also helped to undermine the Commission's proposal.

Sixth, a lack of confidence in the environmental effectiveness of the measures proposed made them difficult to defend. Requiring every farmer throughout the EU to follow exactly the same management prescriptions, regardless of the ecological context, environmental pressures, or opportunity costs, is a highly inefficient policy approach. Environmental NGOs pointed out that requiring individual farms to maintain existing levels of permanent pasture would not necessarily help to protect species-rich semi-extensive grasslands and grasslands of high nature value. Crop diversification was seen as a second-best alternative to crop rotation. While the environmental potential of ecological focus areas was more widely recognised, particularly for biodiversity, questions were raised as to whether science supports setting aside individual parts of every farm regardless of its conservation value, or whether a more targeted approach might not be more effective (Godfray 2012). The absence of management prescriptions also reduces their likely environmental value. As the European Court of Auditors pointed out: *'... the regulation does not specify the concrete objectives, which should be achieved by the farming community in that domain, nor does it explain the impact which is expected from implementing such measures. The absence of such justification raises the questions as to the claimed aim that the policy is results oriented'* (ECA, 2012, p. 40).

The apparent failure of the Commission's greening strategy points to a more fundamental dilemma for those seeking to orient the CAP more towards environmental objectives. During past reforms of the CAP, greening Pillar 1 payments through cross compliance and promoting voluntary AEMs in Pillar 2 were seen as complementary strategies to green the CAP. In fact, it appears they are increasingly competitive, at least as long as Pillar 1 payments are primarily intended as income support. Increasing the budget for voluntary AEMs in Pillar 2 can only occur by transferring resources from Pillar 1. But the effectiveness of cross compliance in Pillar 1 depends on the level of direct payments. Strengthening voluntary AEMs in Pillar 2 can only occur at the expense of weakening the sanctions for cross compliance in Pillar 1, and vice versa. In future, those seeking to orient the CAP more towards environmental objectives may need to choose between one approach or the other.

Targeted agri-environment payments linked to the provision of identifiable and specified environmental public goods are a cost-effective way to achieve environmental benefits. However, if further greening of the CAP were pursued through targeted AEMs in Pillar 2, there is a risk that the environmental benefits achieved through cross compliance could be lost. These are mainly the GAEC standards which go beyond the environmental baseline set by legislation and incorporated in Statutory Management Requirements. Currently, GAEC standards do not apply to farmers who opt out of or otherwise do not receive direct payments. It seems necessary that, to be effective, legal force should be given to these codes of good farming practice.

This suggests a need to revisit where European society wants to draw the 'environmental baseline' or reference level which distinguishes between those obligations which farmers are expected to carry as part of the normal practice of farming ('polluter pays principle') and those obligations which society accepts go beyond normal good farming

practice and where farmers should be remunerated for the additional costs and income foregone in achieving them ('provider gets principle'). It is often assumed that this is currently given by cross compliance (both statutory management requirements and GAEC standards). However, the strong political support for the view that direct payments are, in part, a recognition of the costs that society asks farmers to bear through cross compliance implicitly undermines the 'polluter pays principle'. If farmers who do not receive direct payments are not expected to observe the cross compliance standards, then these do not form the environmental baseline. Whether or not this should be the case deserves wider discussion, taking into account both the impacts on environmental outcomes and the competitive position of farming.

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