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**For an EU Common Agricultural Policy serving the public good  
after 2020: Fundamental questions and recommendations**

Report of the  
Scientific Advisory Board on Agricultural Policy, Food and Consumer Health Protection  
of the Federal Ministry of Food and Agriculture

## For an EU Common Agricultural Policy serving the public good after 2020: Fundamental questions and recommendations

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## Summary

Agriculture fulfills a variety of societal functions: it mainly produces food but also biomass used for energy and materials; it shapes agrarian landscapes and biotopes, and determines the level of animal welfare. In addition, it influences socio-economic structures. In order to promote the societal functions of agriculture, the state should establish framework conditions in such a way that the entrepreneurial activities of farmers simultaneously serve the public good. This can be achieved through the imposition of obligations and the creation of incentives. The Common Agricultural Policy (CAP) of the European Union (EU) is of major importance in this context.

The present CAP, however, is failing to tackle current and future challenges in the policy field of agriculture and rural areas. Since its 2003 reform, the CAP has basically been at a standstill. Due to insufficiently developed incentive systems as well as insufficient regulatory enforcement, numerous important German and European agricultural objectives regarding climate, water and biodiversity conservation have not and cannot be achieved. Incentive systems to improve animal welfare are almost non-existent, resulting in a considerable need for action. Major action is also required when it comes to developing rural areas.

Important decisions about the CAP will be taken in the near future. They will shape the CAP up to the end of the next decade. Hence, there is a window of opportunity to tailor the CAP to meet the current and future challenges that agriculture and rural areas are facing, thereby developing it into a policy serving the public good. This would support the CAP's societal acceptance in the long run and contribute to a reliable agricultural policy framework for the next decade. The Scientific Advisory Board on Agricultural Policy, Food and Consumer Health Protection (WBAE) recommends reorienting the CAP towards a policy for agriculture and rural areas that consistently serves the public good.

Such a reorientation requires overcoming the one-sided focus on support for agricultural incomes as demanded by much of the agricultural profession and endorsed by many political decision-makers. Currently, around 73 % of the European CAP funds (around EUR 40 billion annually) are paid to agricultural enterprises as area-based direct payments (DPs). Many of these DPs are specifically intended to serve income purposes but they cannot be justified from a distributional perspective: they are neither oriented towards maintaining the societal functions of agriculture nor to meeting farmers' personal or operational financial needs. Moreover, a large part is passed on to landowners. Consequently, the financial resources tied up in DPs cannot be used to remunerate public services. This is all the more true since from an environmental perspective the promotion of so-called ecological focus areas (greening) has proven to be largely ineffective. Instead of continuing to spend a large share of the CAP budget on DPs not tailored to the needs and provision of public services, there is an urgent need to (further) develop adequate governance and funding instruments for the remuneration of public services rendered by agriculture.

In its current form the CAP has serious shortcomings in terms of its strategic orientation, its instrumentation and in producing disproportionate administrative burdens. The urgently needed substantive and structural reorientation would inevitably affect long-standing privileges. Since these are often perceived as justified in the sector, a consistent reorientation of the CAP is dependent on political assertiveness. Postponing the necessary reorientation of the CAP, however, would exacerbate both the problems to be addressed and the need for operational adjustments at farm level, leading to additional adjustment costs. Though often claimed, reliable long-term framework conditions cannot be achieved by maintaining the status quo. On the contrary, reliable framework

conditions can only be established through a long-term orientation of the CAP towards public interest objectives that enjoy broad societal support.

**The WBAE recommends transforming the CAP into a policy that consistently serves the public good. Specifically, with regard to decisions taken at EU level and for national implementation, the WBAE makes the following recommendations to the German Federal Government:**

- I) **Rebalance the CAP objectives and pursue them consistently:** (1) identify and operationalise the challenges related to environmental and climate protection, animal welfare and rural development; in particular, consistently implement the missed agriculture-related environmental objectives and orient the CAP more than in the past towards these objectives, (2) develop adequate governance and funding systems for the provision of public services and compliance with obligations in the field of agriculture, (3) align the CAP with the maintenance of the societal functions of agriculture (thereby supporting the interpretation and implementation of the income objective in accordance with the established case law of the European Court of Justice), and (4) initiate and actively shape a broad societal discourse (beyond the current reform decisions) on the objectives and mechanisms of a CAP that serves the public good.
- II) **Rethink the CAPs architecture and revise competences:** (1) untie the two CAP funds (European Agricultural Guarantee Fund - EAGF - and European Agricultural Fund for Rural Development - EAFRD) in particular in terms of financing rules, measures and implementation mechanisms, (2) support the path outlined by the European Commission in its November 2017 Communication towards greater decentralisation of the CAP, (3) in the long run, only finance market regulations and selected parts of climate and biodiversity protection (peatland protection and Natura 2000) to 100 percent from the EU budget, (4) extend support measures for further public services and shift competences regarding their design more to the Member States; these measures should be consistently co-financed by the Member States and programmed by them within a framework of national or regional strategic plans, and (5) develop appropriate incentive, control and sanctioning systems in order to support ambitious target setting by the Member States within the framework of their own subsidiary responsibility.
- III) **Reduce the administrative burden to an appropriate level:** (1) significantly reduce the complexity of the legal framework and the regulatory depth of the CAP by scaling back and codifying the EU implementation provisions, (2) introduce the single audit principle, (3) no longer require Member States to prove the regularity of expenditure, but provide performance statements and checks on the basis of output and result indicators, and (4) promote administrative efficiency through increased use of digital technologies and adequate monitoring systems.
- IV) **Phase-out direct payments and other payments not oriented towards societal objectives:** (1) phase-out existing DPs over a period of about 10 years and grant payments to farmers only in areas where the management of land and related public services would otherwise be at risk, (2) for the transition period, in which there are still DPs, i) implement cutbacks of the EU agricultural budget by reducing DPs instead of reducing expenses for measures currently

programmed via the EAFRD, **ii**) extend the possibility of reallocating financial resources from the EAGF to the EAFRD beyond the current 15 %, **iii**) allow for national co-funding of DPs and nationally funded top-ups in order to increase the level of acceptance for exiting DPs, **iv**) identify further options to bring Member States on board that are critical of co-funding DPs (e.g. higher EU co-funding rates for Member States with currently below-average DPs), **v**) strictly limit the option of coupled DPs to the provision of narrowly defined public services and base the scale of support on the costs of providing these public services, **vi**) end capping or degression of DPs as well as support for the first hectares and young farmers within the EAGF, and **3**) limit investment support exclusively to the pursuit of public interest objectives such as an increased level of environmental protection or animal welfare.

- V) Further develop measures to remunerate agriculture's environmental and climate protection and animal welfare-related public services:** **(1)** progressively develop and finance a new European policy area under which the European Commission, via tendering procedures, purchases greenhouse gas emission reductions through peatland protection, **(2)** allocate a separate share of the budget at European level for the promotion of biodiversity protection in open landscapes within the Natura 2000 nature conservation network, **(3)** further develop existing agri-environmental and climate protection measures, as instruments tailored to different habitat types, and endow them with a larger budget; in particular **i**) introduce more incentives to spatially govern environmental and climate protection measures, e.g. premiums for the linking up of priority areas for biodiversity differentiated according to soil quality, **ii**) further develop result-based remuneration models, **iii**) step up the elaboration of collective approaches to environmental and climate protection, **(4)** make administrative and monitoring provisions for agri-environmental and climate protection measures more efficient, **(5)** require Member States to allocate at least 30 % of the current DPs to targeted agri-environmental and climate protection measures in their strategic plans, **(6)** abolish greening and cross compliance while simultaneously tightening regulatory law and strengthening its enforcement, and **(7)** further develop options to remunerate animal welfare services in the context of the CAP.
- VI) Understand risk management as an entrepreneurial task:** **(1)** clearly distinguish policy measures to support the risk management of agricultural enterprises from income policies and do not present income-motivated DPs as a risk management instrument, **(2)** place more emphasis on promoting knowledge transfer in the area of risk management, **(3)** enable the saving of financial resources in the EU crisis reserve, **(4)** review the justification for and the design of remaining state "safety nets", e.g. intervention prices, and **(5)** communicate significant changes in the political environment in a timely manner.
- VII) Strengthen knowledge systems and innovations:** **(1)** further develop the European Partnership for Innovation in Agriculture, **(2)** employ research funding to enable agricultural enterprises to adapt to changing conditions and societal requirements, and **(3)** make greater use of research results and innovations through cross-national communication.
- VIII) Understand and strengthen rural development as a cross-sectoral task:** **(1)** if rural development remains an area of the CAP, continue providing sufficient opportunities for the

implementation of measures reaching beyond the agricultural sector, **(2)** focus measures more than before on those Member States and regions in which the need for action with regard to balanced spatial development in the EU is particularly high, and **(3)** improve the harmonisation of all policies with spatial impacts within the framework of the European Structural and Investment Funds.

**IX) Better coordinate agricultural and food policy:** **(1)** routinely review the food and human health implications of the CAP, **(2)** clarify conceptual questions regarding the complementary (both supply and consumption driven) pursuit of public interest objectives in terms of environmental and climate protection and animal welfare, **(3)** further develop consumer-oriented food policy instruments in Germany and deploy them significantly more than in the past to pursue public interest objectives regarding environmental and climate protection and animal welfare, and **(4)** strengthen competences at the political and administrative level to understand the sector as an integrated food system and develop policies to make this system more sustainable.

Hence, a CAP reform is strongly required. In addition, the WBAE observes that Germany does not use the scope that the present CAP offers Member States to allocate resources to societal objectives to full capacity. Germany should use the existing and prospective future scope for action for increasing orientation towards the common good.

**The WBAE makes the following recommendations to the German Federal Government:** **(1)** For the remaining period in which there are still DPs **i)** increase the reallocation rate from the first to the second pillar of the CAP to the 15 % currently possible under EU law, **ii)** use the option of coupled DPs with a strict focus on the provision of closely defined public services and base the level of support on the costs of providing these services, **(2)** consistently orient all support measures of the Joint Task "Improvement of Agricultural Structure and Coastal Protection" (GAK) covered by the national framework regulation towards the public good, **(3)** use the GAK for a national expansion of the remuneration of animal welfare services, and **(4)** implement the planned GAK specific framework plan "Promotion of the development of rural areas" in a manner conducive to the public good.

Finally, the WBAE concludes: The decisions to be taken in the near future at EU level will shape the CAP up to the end of the next decade. The German Federal Government should see the CAP reform as a great opportunity and use the CAP reform and its subsequent implementation in Germany to free the CAP from its income orientation and transform it into a policy that consistently serves the public good. A CAP oriented towards the public good would help agriculture to meet the challenges ahead and support the CAP's long-term societal acceptance, thereby creating a reliable agricultural policy framework for the next decade and beyond.

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## List of abbreviations

BGBI	Federal Law Gazette ( <i>Bundesgesetzblatt</i> )
BMEL	Federal Ministry of Food and Agriculture ( <i>Bundesministerium für Ernährung und Landwirtschaft</i> )
BVerfG	Federal Constitutional Court ( <i>Bundesverfassungsgericht</i> )
CAP	Common Agricultural Policy
DG SANTE	Directorate-General Health and Food Safety
DLG	German Agricultural Society ( <i>Deutsche Landwirtschaftsgesellschaft</i> )
DPs	Direct payments
EAFRD	European Agricultural Fund for Rural Development
EAGF	European Agricultural Guarantee Fund
ECA	European Court of Auditors
ECJ	European Court of Justice
EFRD	European Regional Development Fund
EIP-AGRI	European Innovation Partnership “Agricultural Productivity and Sustainability”
EMFF	European Maritime and Fisheries Fund
EPHA	European Public Health Alliance
ESF	European Social Fund
EU	European Union
EUPHA	European Public Health Association
FADN	Farm Accountancy Data Network
FAO	Food and Agriculture Organization of the United Nations
GAK	Joint Task “Improvement of Agricultural Structure and Coastal Protection” ( <i>Gemeinschaftsaufgabe „Verbesserung der Agrarstruktur und des Küstenschutzes“</i> )
GATT	General Agreement on Tariffs and Trade
ha	Hectare
ICT	Information and Communication Technology
NEC	National Emission Ceilings
NUTS	Nomenclature of Territorial Statistical Units ( <i>Nomenclature des Unités Territoriales Statistiques</i> )
TFEU	Treaty on the Functioning of the European Union
UAA	Utilised agricultural area
WBA	Scientific Advisory Board on Agricultural Policy ( <i>Wissenschaftlicher Beirat für Agrarpolitik</i> )
WBAE	Scientific Advisory Board on Agricultural Policy, Food and Consumer Health Protection ( <i>Wissenschaftlicher Beirat für Agrarpolitik, Ernährung und gesundheitlichen Verbraucherschutz</i> )
WHO	World Health Organisation
WTO	World Trade Organisation



## 1 Introduction

1. At the time of the adoption of this report (April 2018) as well as at the time of its English publication (October 2018) the future design of the Common Agricultural Policy (CAP) was and is the focus of intense debate. Numerous stakeholders have made reform proposals and submitted position papers. The European Commission likewise published reform proposals in its November 2017 Communication (EU COM 2017a).
2. The Scientific Advisory Board on Agricultural Policy, Food and Consumer Health Protection (WBAE) understands the key question regarding the design of the future CAP to be the following: Which challenges are European agriculture and rural areas facing and should they be assisted in tackling these challenges? In particular, it is necessary to clarify which competences are to be located on which level of responsibility in the complex multi-level system of the European Union (EU), which instruments are best suited to address different challenges and what budget should be made available for these purposes.
3. The current discussions about the CAP post 2020 show that these design questions are generally discussed in a truncated manner. It must be feared that the budget to be adopted will be spent, as in the past, mostly on one-size-fits-all area-based payments and that the existing system will be only marginally changed. By way of example, more targeted measures might only be extended to a limited degree in order to justify the area-based direct payments.
4. During the last two decades, the WBAE and its predecessor, the Scientific Advisory Board on Agricultural Policy (WBA), have published numerous reports regarding the further development of the CAP (most recently in the course of its reports on climate protection and livestock husbandry: WBAE and WBW 2016, WBA 2015; with a focus on the CAP: WBA 2011a, b, 2010, 2005a, b, 2003, 1998a, b). Specifically, the Scientific Advisory Board has repeatedly advocated to fundamentally redesign the CAP along the reform course embarked upon with the MacSharry reform of 1992. This reform was characterized by dismantling the market- and competition-distorting system of protection of the internal market and by establishing a policy with a stronger orientation towards meeting the diverse challenges of the CAP and allowing for more regional differences – especially within the framework of the rural development programmes.
5. After the pioneering CAP reforms of 1992, 1999 and 2003 the CAP reform process has largely ground to a halt, with the exception of reforms in the field of market policies. This standstill is particularly characterized by the fact that
  - most (around 70 %) of the funds are still tied to direct payments motivated by income policy; for the individual farmer, the level of payments is mainly determined by the size of the area farmed and the Member State in which the farm is located;
  - the measures introduced to give direct payments an environmental focus primarily serve to improve the enforcement of existing sectoral legislation (as with cross compliance) or have little impact (as with greening);

- the overall budget of the second pillar which is urgently needed for effective environmental<sup>2</sup> and climate protection, animal welfare and the promotion of rural areas is stagnating; and
  - the policies relating to the first and second pillar of the CAP are not sufficiently coordinated.
6. Furthermore, the current CAP is hampered by other problems:
- Given the limited targeting of the CAP, the high transaction costs resulting from the complex nature of the CAP are disproportionate both for the agricultural administration and for agricultural enterprises.
  - The design, funding and control of many measures have not been aligned with the subsidiarity principle<sup>3</sup> and are overly centralised.
  - The option of coupling direct payments to production (extended in 2013) carries the risk of distorting competition.
7. Despite these problems, both political decision-makers responsible for agricultural policy at the national and European levels and representatives of the agricultural profession have not injected much momentum into a comprehensive reform of the CAP. Nonetheless, European agriculture and rural areas still face major challenges. Besides the contribution to securing the global supply of safe and diverse foods, these challenges particularly concern environmental and climate protection, animal welfare and rural development. Given the major necessity for action in these areas and the costs involved in an orientation towards the public good, there is a need for far more targeted use of the CAP budget and for the development of adequate governance and funding systems (cf. Box 1: Why we need agricultural policy, p. 4).
8. In an increasingly heterogeneous EU, different starting and problem situations and increasingly open markets make it more difficult to tackle these challenges and highlight the need for a broad set of measures.
9. In the opinion of the Board, the current negotiations about the CAP post 2020 should be used for a fundamental reorientation. There are various options – however, the most important goal of a reform should be to use the CAP funds to efficiently meet the main challenges and derived objectives. Further postponing a comprehensive reorientation of the CAP will result in a tardy reorientation of the sector and thereby incur high adjustment costs.
10. Against this backdrop, the Board once again adopts a position on the further development of the CAP. This report outlines and evaluates fundamental questions and derives

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<sup>2</sup> In this report the term ‘environmental protection’ is understood as encompassing nature conservation.

<sup>3</sup> Within the EU the subsidiarity principle serves to regulate the pursuit of the non-exclusive responsibilities of the Union – including the field of agricultural policy (cf. Article 4(2) TFEU). “Under the principle of subsidiarity, in areas which do not fall within its exclusive competence, the Union shall act only if and insofar as the objectives of the proposed action cannot be sufficiently achieved by the Member States, either at central level or at regional and local level, but can rather, by reason of the scale or effects of the proposed action, be better achieved at Union level” (Article 5(3) TEU). For an operationalisation of the subsidiarity principle using the example of various EU policy areas cf. Gelauff et al. (2008).

recommendations for a viable future design of the CAP. It focuses on policy areas with direct budgetary consequences and not on trade policy instruments or market organisation. In line with the primary mandate of the Board the recommendations address the German Federal Government, particularly decision-makers in the Federal Ministry of Food and Agriculture (BMEL). Germany is a relatively large and high-income Member State. Therefore, the Board considers Germany to bear special responsibility for a viable future reorientation of the CAP. Furthermore, Germany has significant environmental and climate protection and animal welfare problems and faces specific challenges regarding the development of rural areas. In the framework of the current and future CAP, these problems and challenges should be addressed in a far more targeted manner.

11. The report is structured as follows: Chapter 2 gives an overview of the reform debate. It structures this debate along the main fundamental issues raised during the current and – in most cases – also earlier reform debates. In the opinion of the Board, adopting a position on these fundamental issues should guide action for any reform in the policy field of the CAP. Chapter 3 then discusses transformation pathways for the CAP and identifies requirements for the long-term establishment of a CAP that serves the public good. Finally, chapter 4 presents tangible recommendations for the German Federal Government regarding a CAP post 2020 that serves the public good.

### Box 1: Why we need agricultural policy

Agriculture is multifunctional – it mainly produces food but also biomass used for energy and materials; it shapes agrarian landscapes and biotopes, and determines the level of animal welfare. In addition, it influences socio-economic structures. Besides producing services that are paid for on markets, it fulfils societal functions in the areas of environmental and climate protection, nature conservation, animal welfare and beyond.

Which services and products are understood as agriculture's societal functions and to what extent they should be provided is subject to societal negotiation process. Hence, answers to these questions are not static but change over the course of time. Generally, multifunctionality, i.e. agriculture providing multiple societal functions, is desirable. Consequently, the level of environmental protection, the character of agrarian landscapes and the level of animal welfare should not solely be determined by the objective of low production costs but also other societal demands.

This leads to a dilemma: some of the goods produced by agriculture (economists refer to "private goods") such as, for instance, food, are remunerated via the market price mechanism. Other goods or services are not remunerated via the market at all or only to a limited degree (e.g. via market niches or private sector standards). Therefore, the latter, non-remunerated goods or services (to the extent that they do not already accrue as coupled products of agricultural production) are not produced at all or not on the scale desired by society. A sufficient provision of these goods and services requires different governance mechanisms or changes in the institutional framework so that the market mechanism can take effect (e.g. through the establishment of labels).

In a closed economy it would be relatively easy to implement such an approach. Regulatory law could require the fulfilment of societal functions. This would increase production costs and, thus, result in higher market prices, covering (at least some) of the increased production costs. In open economies this only applies to a limited degree: Germany's and also the EU's markets for agricultural products are mostly integrated into the global markets. Price levels are largely determined by the price level on the world market. Consequently, producers cannot transfer an increase in production costs into higher product prices.

Germany and the EU explicitly aim to shape agriculture within the framework of internationally integrated product markets without participating fully in global competition where participants are most successful if they least call for costly societal services from agriculture. Thus, when it comes to our product markets we want to be integrated into global markets. However, concurrently we want to "decouple" from the global race to the bottom regarding the level of animal welfare and environmental protection. Because of international market integration, agriculture's societal services cannot be remunerated by market prices alone. Accordingly, to achieve a higher level of such societal services requires other remuneration mechanisms. In other words: the CAP must support agriculture to generate income for societal functions that go beyond food production.

In this regard, it is necessary to negotiate which societal services are so essential that they should be delivered on the basis of regulatory provisions and which are to be purchased by the state via incentive systems on a voluntary basis (public services, see Box 2, p. 6):

- a. In the case of regulatory obligations, society should only bear resulting costs (e.g. through compensation payments) in justified cases and only partially, if failing to do so would result in too much agricultural production relocating abroad (cf. Chapter 2.3). There seems to be a stronger rationale for such compensation regarding large parts of animal husbandry compared to arable farming, as the adjustment needs of husbandry systems are considerable and will generate extensive costs.
- b. Public services, i.e. services above the level laid down in regulatory provisions, require remuneration systems, e.g. premiums or transparent labelling systems which facilitate the marketing of added values in terms of process quality.

## 2 A CAP oriented towards the public good: reform debate and fundamental issues

12. The key fundamental question about the design of the CAP is whether and, if so, in what form CAP funds and instruments are to be oriented more towards enabling agriculture to fulfil its societal functions and successfully rise to new societal challenges (cf. Box 2: Societal functions and public services of agriculture, p. 6). The precondition for this would be a dismantling of the current system of largely unconditional area-based payments.

13. Both the stakeholders and their arguments are basically unchanged when it comes to this fundamental question. On the one hand there are the agricultural interest groups across the EU that vehemently advocate the continuation of direct payments by pointing to their direct impact on income and farm competitiveness (DBV 2015, 2017a, COPA-COGECA 2017a, Deter 2017). The call for a first pillar which is oriented more towards environmental objectives is, in most cases, vehemently rejected (DBV 2017b, COPA-COGECA 2017b). Most of the national ministries of agriculture call for an extension of state support for farm risk management and measures for “fair” value chains (cf. for instance, COPA-COGECA 2017a, DBV 2017a, AMTF 2016, EU KOM 2017a, EWSA 2016). Disagreement exists particularly on the question as to whether the amount of area premiums should be further harmonised between the Member States and whether the preservation or even the extension of coupled direct payments should be facilitated.

14. On the other hand, stakeholders from environmental protection, nature conservation, animal welfare, development policy and from large parts of the agricultural and environmental sciences repeatedly criticise the limited target orientation of one-size-fits-all area-based premiums. Support that is oriented almost exclusively towards farm size does not create any incentives for the so urgently needed production of public goods and for that reason should be gradually phased out – this is the short version of this position.<sup>4</sup> Beyond this diagnosis, however, there are some very different proposals regarding the focus and the instruments of a redesigned CAP. One good example for this is the ever-present demand in Germany for special support for small farms.

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<sup>4</sup> A comprehensive list of all available position papers and reform proposals is not provided here. A compilation of the most important papers available up to May 2017 is available from Latacz-Lohmann et al. (2017). Various proposals are commented on by Alan Matthews and other authors on the CAP reform blog: <http://capreform.eu/>.

**Box 2: Societal functions and public services of agriculture**

In order to promote the societal functions of agriculture, policy makers should set the general framework in such a way that the entrepreneurial activities of farmers simultaneously serve the public good. This is done by both imposing obligations and creating incentives (cf. Box 1: Why we need agricultural policy).

The term 'public services' is used in various ways by the European Court of Justice (ECJ) and the Federal Constitutional Court (BVerfG) (e.g. ECJ, judgment of 19 December 2013 – C-262/12 – BVerfGE 122, 1 et seq., margin no. 3) but, so far, no clear definition has been provided. Public services can be defined as services which are provided in a voluntary manner by independent entrepreneurs, for instance farmers, or by the rural population. These services benefit the general public in such a way that no-one is excluded from their use. The **voluntary nature** of service provision implies that the term public services can only be used when the services provided in terms of their scale and/or quality go beyond the scale stipulated in regulatory law. Mere compliance with regulatory standards does not constitute a public service but an obligation to avoid a burden for the public good. The **non-excludability** from use implies that public services have the character of a public good. Consequently, the production for instance of marketable agricultural products is not a public service.

Another decisive criterion of public services is that there must be societal appreciation of the services concerned. This is expressed primarily in standards which are laid down in the constitution or by the legislature. When it comes to the impact of agricultural production on societal assets that are to be protected, public services draw their legal justification from the principles of good farming practice, as anchored in regulatory law or sub-legislative standards. A demand for these public services which goes beyond this normative scale is expressed in policy programmes to promote specific societal services which would otherwise not be provided (to a sufficient degree) via the market.

The demand for public services is not static. Over the course of time, there are changes not only to societal appreciation and prioritisation of different goods and services but also to the reference level as to what constitutes a public service. This means the dividing line between a regulatory obligation and a societal service is constantly shifting in the political debate. This shift is reflected in amendments to the regulatory framework.

Many public services of agriculture have an environmental focus. There are, however, also public services with an economic, social or cultural focus. For instance, the preservation of cultural heritage in rural areas can meet the definition of a public service just as much as the preservation of social structures or additional economic development in rural areas. The latter leads, *inter alia*, to improved employment opportunities and higher business tax revenues from which everyone living in the region profits in the final instance.

Public services do not necessarily have to have a physical link to the recipients. This is clear in the case of animal welfare standards. Vegetarians for whom the humane keeping of livestock is important for ethical reasons benefit from knowledge about the existence of animal welfare standards. The decisive factors here are not just the physical relationship (the consumption of meat produced in line with defined animal welfare standards) but also the impact on the well-being of those concerned.

Public services encompass both unintended services (positive external effects of the production of marketable goods) and intended services which are provided because of altruism or because of state or private sector incentive systems or their contribution to economic success (corporate image).

Despite the lack of remuneration by the market, not all public services are worthy of financial remuneration. State support for public services can only be justified if they are in short supply. If unintended public services are the by-product of viable agricultural production, they do not need state support.

15. In the past the Board has adopted a position on several occasions on the future viability of the CAP and the necessary reforms. Given the stressed importance and persistence of a few debates, the following fundamental questions about the design of the CAP are discussed again:

- Are the objectives of the CAP adequately weighted when it comes to current and future challenges? (Chapter 2.1);



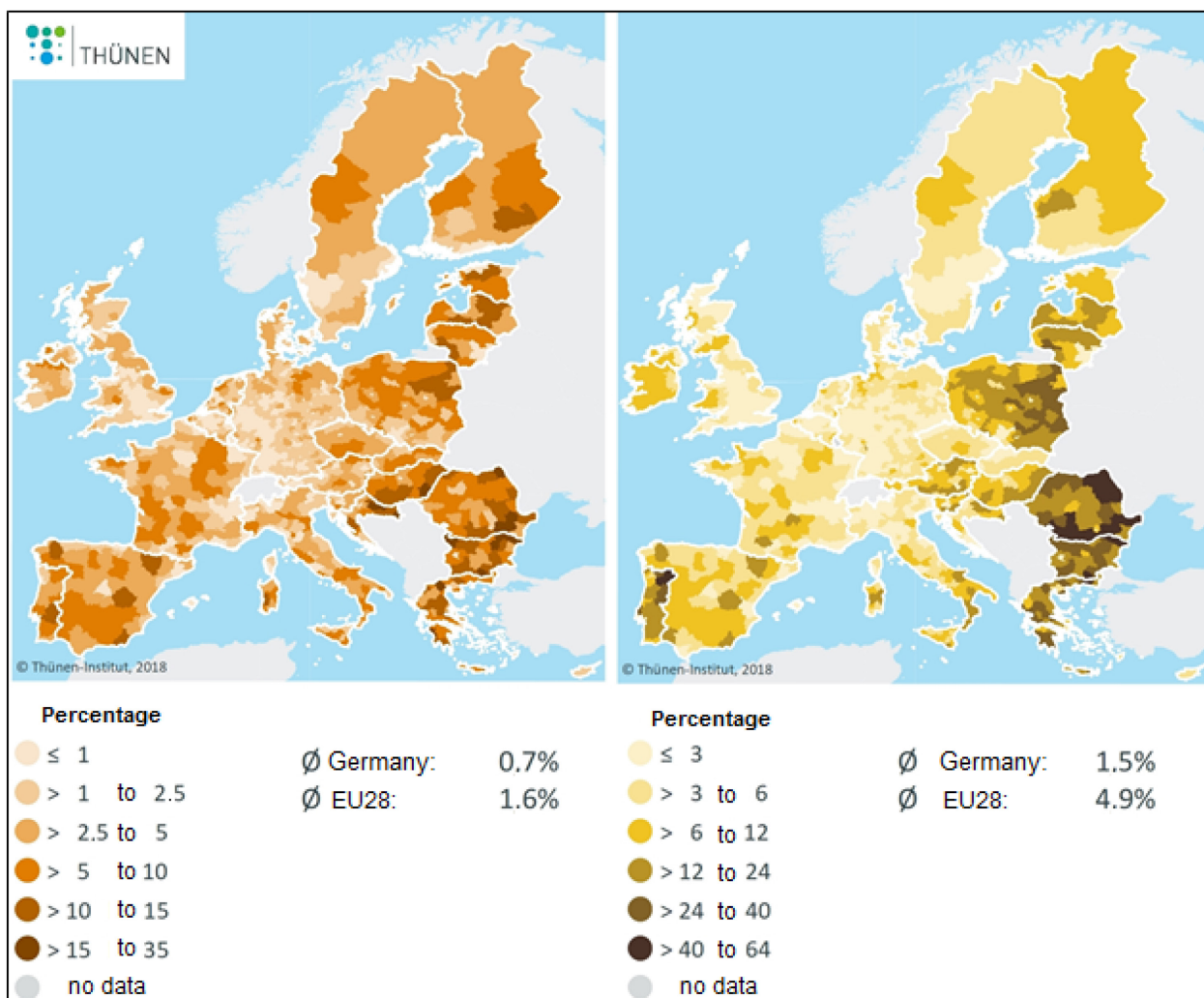
- Which architecture and allocation of competences should be implemented within the CAP? (Chapter 2.2);
- Does European agriculture need sectoral income support and is this justifiable within the framework of the CAP? (Chapter 2.3);
- Should the distributional effects of direct payments be “corrected”? (Chapter 2.4);
- Are direct payments an adequate means of achieving environmental and climate objectives? (Chapter 2.5 );
- Should government support farm risk management? (Chapter 2.6);
- What importance should the development of rural areas beyond the agricultural sector assume within the CAP? (Chapter 2.7).

16. Given that various stakeholders increasingly argue for a further development of the CAP into a Common Agricultural and Food Policy, the WBAE is also discussing whether and, if so, to what extent a greater integration of agricultural and food policies should and can be pursued at the European level (Chapter 2.8).

## **2.1 Are the objectives of the CAP adequately weighted when it comes to current and future challenges?**

17. The first basis for a targeted design of any area of policy must be agreement on which objectives are to be achieved. Objectives, in turn, touch on societal problems and challenges. Within the framework of the CAP these objectives should, therefore, reflect which problematic situations in the policy area of agriculture and rural areas are to be overcome or improved. Given the large degree of regional heterogeneity in the EU the common definition of problems and objectives as well as the derivation of suitable measures constitute a major challenge. Figure 1 depicts the share of agriculture in gross value added and employment to exemplify the given heterogeneity.

**Fig. 1:** Share of agriculture, forestry and fisheries in total gross value added at producer prices (left map) and in total employment (right map) (2014, NUTS-3 level)



Source: own calculations based on Eurostat. Left map: gross value added in production prices according to NUTS-3 regions [nama\_10r\_3gva], Status 12.04.17. Right map: employment (thousand persons) according to NUTS-3 regions [nama\_10r\_3empers] Status 15.09.17.

18. When the CAP was introduced there was sufficient political consensus about the definition of the problems and objectives. The signatories to the Treaties of Rome adopted in 1957 agreed on a set of equal-ranking objectives that were, however, partially in competition with one another. The first objective was to increase agricultural productivity by promoting technical progress, by ensuring the rationalisation of agricultural production and the optimum utilisation of the factors of production, in particular labour. Thus, secondly, to ensure a fair standard of living for the agricultural community, in particular by increasing the individual earnings of persons engaged in agriculture. The stabilisation of markets and ensuring supplies reach consumers at reasonable prices were other important objectives (Article 39, Treaty on the Functioning of the European Union (TFEU), ex Article 33 Treaty establishing the European Community).

19. This original catalogue of objectives of the CAP has remained in force up to now. It can be found unamended in the Treaty on the Functioning of the European Union (TFEU) and already since 1955 in a similar formulation in the German Agriculture Act. With its focus on social policy objectives, the catalogue is a product of its (post-war) period and should be critically examined in the light of current and future challenges:

**a) Higher productivity:** In the first decades of the CAP, the focus was on increasing labour and area productivity. Major increases were achieved here.<sup>5</sup> Since the beginning of the 1980s, however, it has become increasingly clear that agricultural policy support oriented one-sidedly towards production creates false incentives. The debate focussed initially on the side effects of high guarantee prices. These high prices caused production surpluses. Their alleviation by supporting export and storage implied rising budgetary costs and gave birth to trade conflicts. In addition, the negative environmental effects and animal welfare problems linked to the intensification of production became increasingly apparent. Further increases in global production will nevertheless still be necessary in the foreseeable future. This is due to the development of the bio-economy and the growing demand for agricultural products outside Europe. The latter is a consequence of the increasing global population and changing consumption habits in both newly industrialised and less-developed countries. However, against the backdrop of climate change and other environmental challenges, these productivity increases must be associated with a minimum level of negative external effects. It is, therefore, pivotal to refer the productivity to the amount of required natural resources which are in increasingly short supply (eco-efficiency). Given the international development in demand, productivity increases will continue to play a certain role in the EU as well (particularly in central and eastern Europe). The necessary global increases in productivity will, however, have to be achieved predominantly in less-developed and newly industrialised countries.

**b) Fair standard of living for the agricultural community:** Hardly any of the objectives laid down in the Treaties of Rome is being discussed more intensively today than the objective of a fair standard of living for the agricultural community. The agricultural profession and the decision-makers responsible for agricultural policy normally refer to “the income objective” of the CAP. They argue that there is a general gap between the income of farmers and people working in other sectors and that it is the task of the CAP to mitigate this income gap. However, there is no solid statistical information foundation that would allow to derive EU-wide and general statements about the actual income situation of agricultural households. This is particularly because the comparative cost accounting, which is used to support the above stated claims, reports farm income alone but not the off-farm income of agricultural households. This means that the actual income situation is, in some cases, considerably underestimated. Nor is there any evaluation of the income of farmworkers

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<sup>5</sup> At the same time it should be borne in mind that there are still many farms which use out-dated technologies resulting in low labour productivity. These farms can be mainly found in the European regions dominated by small-scale agriculture, increasingly confronted with marketing problems due to tightening product standards.

although they now do almost 45 % of the work in agriculture in Germany (Statistisches Bundesamt 2017a). Furthermore, the arguments advanced in favour of sectoral income support mostly ignore the fact that the European primary legislation does not stipulate any individual entitlement to income support for farms whose livelihood is threatened. On the contrary, the need for special support results from the safeguarding or promotion of the maintenance of societal functions of agriculture (cf. Chapter 2.3). To achieve the objective of supporting societal functions, additional income opportunities for agriculture have been created, particularly since the beginning of the 1990s, within the rural development programmes. This encompasses, for instance, premiums for environmental public services and the establishment of landscape features, grassland extensification or payments to farmers in areas with natural constraints (cf. Box 2: Societal functions and public services of agriculture, p. 6). Given the growing societal demands for the provision of public services, this objective is still very much up-to-date and is dependent on the extension and further development of corresponding measures.

- c) Stable markets:** During the first three decades of the CAP, the main objective behind the goal of stable EU markets for agricultural products was support for agricultural income by means of a largely sealed-off internal market and guarantee prices that were higher than the world market prices. Given the impact of this market regulation policy (high national economic costs, highly subsidised surpluses and negative environmental externalities) and the major international criticism triggered by subsidised exports, this protectionist price policy was successively dismantled with the commencement of the MacSharry reform of 1992. Consequently, the increasing world market integration of European agriculture confronted European producers with mostly lower and, at the same time, more volatile world market prices. Whereas the decision-makers behind the CAP agreed on the granting of price-based compensatory payments to offset income losses caused by price cuts, the opinion prevailed that handling price risks was first and foremost an entrepreneurial task. At the same time important EU markets, in particular for products deemed by the EU to be “sensitive goods” like beef, are still protected by, in some cases, high customs duties. Moreover, the world price volatility in recent years has contributed to the call for state support for farm risk management (cf. Chapter 2.6).
- d) Food security:** The goal of a purely quantitative increase in production to secure food supply is no longer up-to-date in the EU Member States. Given the 815 million people afflicted by hunger (FAO 2017) it is, however, still of the utmost importance globally. Given its size, the EU plays a relevant role in the global availability of agricultural products. It can support this availability both through its contribution to production and through the sustainable consumption of agricultural products (e.g. lower consumption of animal products, cf. WBAE and WBW 2016). However, the primary cause of hunger is not an insufficient quantity of food around the world but poor access to food driven by poverty and conflicts. The key, therefore, to combatting hunger is increased production particularly in countries and regions with a large proportion of hungry people because this not only increases availability of food but also creates income there. In Germany and the EU low

income groups in the population, in particular, have inadequate access to high-value, healthy food (cf. Müller et al. 2010, Fekete and Weyers 2016, Darmon and Drewnowski 2015). However, the repercussions of unhealthy and excessive food intake like overweight, obesity and food-related diseases affect all groups in the population. In 2014 more than half of all adults in the EU-28 were overweight and just over 20% obese (Eurostat 2017a). In Germany, the proportion of overweight adults (52%) is just slightly higher than the EU average. The spread of overweight amongst children at school entry age has remained steady but is nonetheless on a high level (DGE 2017, Schienkiewitz et al. 2018). Last but not least, the repercussions of an unhealthy diet lead to huge social and health expenditure. Nutritional, social and educational policy instruments are particularly suited to tackle these problems. For some years now various stakeholders have, however, called for the greater integration of food and health policy objectives and instruments into the CAP (cf. Chapter 2.8).

- e) **Fair consumer prices:** Over the last 60 years the share of food expenditure in private consumption expenditure in the EU-15 has fallen on average to 10.4 % (Germany: 9.4 %) (Eurostat 2017b). At the same time, the expectations in terms of the product and process quality of foods have risen markedly. In addition, the opportunities for the state to intervene in food prices have declined considerably as a consequence of the integration of the European into the global agricultural markets. Against this background the Board argues, that the term “fair” prices must be interpreted differently: it is less about rather “low” consumer prices but about prices which “fairly” reflect the elevated costs generated by the rising demands with respect to process and product quality. Still, it should be borne in mind that the share of expenditure on food, both in the lower income groups in Germany and in the new Member States of the EU, is far higher given the lower level of income there (e.g. on average 27.9 % in Romania, Eurostat 2017b).

20. By way of summary it can be said that the original set of objectives of the CAP, as laid down in the European treaties, have experienced several shifts in its interpretation because of changing societal framework conditions and sectoral developments. These changes are reflected not least in the enlargement of the original set of objectives of the CAP. The objectives of environmental, water and climate protection (integrated via Article 11 on the sustainable management of natural resources), the objective of rural development (integrated via Article 174) and animal welfare (Article 13) (Martínez 2016b: margin number 15) have been included into the TFEU by means of the so-called horizontal clauses. The original set of objectives of the CAP has not been explicitly adjusted but, in terms of their legal importance, the objectives laid down in the horizontal clauses are on a par with CAP-specific objectives of the Treaties of Rome. This also becomes clear in the secondary law interpretation of the objectives in Article 110(2) Regulation (EU) no. 1306/2013.<sup>6</sup> According to this, the performance of both direct payments and the second pillar is measured with

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<sup>6</sup> Regulation (EU) No 1306/2013 of the European Parliament and of the Council of 17 December 2013 on the financing, management and monitoring of the common agricultural policy and repealing Council Regulations (EEC) No 352/78, (EC) No 165/94, (EC) No 2799/98, (EC) No 814/2000, (EC) No 1290/2005 and (EC) No 485/2008.

respect to the following objectives: (i) viable food production, with a focus on agricultural income, agricultural productivity and price stability, (ii) sustainable management of natural resources and climate action, with a focus on greenhouse gas emissions, biodiversity, soil and water and (iii) balanced territorial development, with a focus on rural employment, growth and poverty in rural areas.

21. The shift away from a market- and trade-distorting agricultural price policy towards a competition-oriented policy with direct area-based income transfer to farmers and voluntary structural, agri-environmental and regional policy support measures (“Policy for the development of rural areas”) was logical and necessary against the backdrop outlined above. Furthermore, the Board appreciates the far-reaching decoupling of direct payments from agricultural production, the further dismantling of state price support implemented in the following reforms and also the relative valorisation of the policy for rural areas over the last decades.

22. At the same time, it should be noted that the change in direction in the CAP triggered by the MacSharry reform is now stagnating and the persistent budgetary prioritisation of the income objective pursued by means of direct payments has resulted in a blatant disparity vis-a-vis the existing societal challenges in the policy field of agriculture and rural areas.

23. Besides the contribution to ensuring the global supply of safe and diverse foods, these challenges are to be found particularly in a) environmental protection and animal welfare, b) climate protection and adaptation and c) in rural development. These challenges result from market failure caused by external effects, the desired provision of public goods and the high ethical demands regarding production conditions:

**a) Environmental protection and animal welfare:** At the present time many of the environmental objectives specified at the European and German levels, which are relevant to agriculture (*inter alia* EU Nitrate Directive, Water Framework Directive, Flora-Fauna Habitat Directive, Marine Strategy Framework Directive, NEC Directive), have not been reached. Moreover, established biodiversity indicators point again and again to critical lows in terms of landscape-related, crop and livestock biodiversity. Furthermore, the husbandry conditions of most livestock do correspond neither to the scientifically justified standards nor to the vision of the population in many Member States – even if it is obvious that in numerous Member States shifts towards greater animal welfare have been initiated. When it comes to ecologically sustainable and animal welfare-friendly food production there is still a considerable need for action (cf. for instance BfN 2017, Butchart et al. 2010, WBA, WBD and SRU 2013, WBA 2015, Maes et al. 2015, Richner et al. 2015, Sutcliffe et al. 2015). However, it is unclear from the Communication of the European Commission (2017a) how the designated higher prioritisation of resource efficiency and environmental protection are to be implemented within the framework of the CAP. The successfully tackling of the above-mentioned challenges is dependent on further regulatory developments and a mixture of instruments tailored to the respective region-specific problems (e.g. training and advice). In addition, a sufficient budget is needed for measures to create incentives for the

provision of public services (cf. Box 2: Societal functions and public services of agriculture, p. 6) or to compensate for the costs for this provision.

- b) Climate protection and adaptation:** Climate change and international commitments to reducing greenhouse gases result in a major need for adaptation in German and European agriculture and the downstream stages of the value chain right through to the consumer. In order to tackle the related challenges, there is a need for a far higher weighting of this objective and more ambitious and more effective instruments than are to be found in the current CAP (cf. Pe'er et al. 2017, WBAE and WBW 2016 for strategies and measures). In its Communication of November 2017 the European Commission (2017a) calls for higher priority for climate protection but avoids detailing the implications of economy-wide greenhouse gas reduction objectives for the agri-food sector in an appropriate manner.
- c) Rural development:** Many rural regions within the EU face major challenges resulting from demographic developments, changing lifestyles, increasingly stiff competition between the regions as a consequence of globalisation and growing integration in the EU, technological change, the development of knowledge economies and a drop in the value added share of agriculture within both the national economy and value chains. The CAP should contribute more to tackle these challenges than it has done in the past (EU COM 2017a). However, this requires to overcome the heavily agriculture-focused implementation of rural development policy within the framework of the CAP (cf. Chapter 2.7).

24. Besides adjustments of the regulatory law and the creation of incentives for the provision of public services, the mastering of the above-mentioned challenges calls for research and innovations and their carry-over into practice. Consequently, **knowledge and innovation systems** take on major importance. Knowledge and innovation have some characteristics of a public good. This applies in particular to knowledge whose use should be open to everyone or knowledge by means of which non-remunerated public goods can be made available or negative externalities can be avoided. Important aspects here are the generation, the provision, the passing on and the capitalisation of knowledge. Regional and national levels are the key players when it comes to the generation of knowledge and the promotion of innovations. Nevertheless, European policy has a major obligation and also the corresponding means to promote knowledge generation, the creation of an innovation-friendly institutional framework, cooperation between Member States, networking and communication between the stakeholders.

25. The above-mentioned challenges are not static. Rural areas, societal requirements, macro-economic framework conditions, agricultural value chains and, last but not least, agricultural technologies are constantly evolving. Over the next few decades, digitalisation will considerably change many of these production conditions which influence agriculture and rural areas. Hence, it is necessary to improve the adaptability of agriculture and rural areas to changing framework conditions – for instance by means of the timely development and provision of suitable or necessary infrastructures and qualification opportunities. Technological, organisational and structural developments in agriculture are sometimes viewed with scepticism (EFSA 2017, Ropohl 2010, EU SCAR 2012, Lowe et al. 2010). Therefore, it is necessary to include societal groups as early

as possible in the development and implementation of innovations, and to develop new paths at the national and European levels to reach societal decisions on controversial innovations. Innovation is essential for the delivery of societal objectives and the international competitiveness of agriculture. Consequently, timely and broadly based societal discussion processes are needed for decision-making taking into account scientific evidence, differing preferences, value judgments and ethical questions.

26. The Board concludes that there is an urgent need to orient the CAP more than in the past towards today's priority objectives. Here two specific aspects are to be borne in mind:

**a) Heterogeneity:** A communitised policy in an EU-28 must reflect the large degree of heterogeneity, both in terms of weighting the objectives and the relative advantageousness of different instruments. With the exception of market and price policy to be determined by the community, a European agricultural policy must therefore offer sufficient flexibility for the Member States. This flexibility, however, must not lead to a "relativism" in national design. Hence, there is also a need for European framing and national strategies adapted to the respective situation. These strategies should be implemented within the framework of national or regional policy programming targeted at the agricultural sector, the food system and rural areas. The current proposal of the European Commission (2017a) can be interpreted as pointing in this direction and should be underpinned by a detailed implementation strategy.

**b) Dynamics:** The EU's agricultural policy, just like agricultural structural change, is path-dependent (Kay 2003, Balmann 1995, Latacz-Lohmann et al. 2001). Furthermore, the two levels are very much interdependent: assuming that the policy is geared towards the problems of agriculture and, at the same time, agriculture is geared towards policy requirements, then a kind of network externality can be assumed where the existing path dependencies of both systems are reinforced. Particularly when it comes to the major challenges facing agriculture as a consequence of technological developments (for instance digitalisation), globalisation, climate change and also changing societal expectations, policymakers face a special challenge that involves not only overcoming their own path dependency but also addressing already now the future challenges facing agriculture and the obstacles to adaptation in the sector.

27. The greater prioritisation of environmental and climate protection and animal welfare objectives requires adequate governance and funding instruments. Furthermore, the one-sided focusing on the income objective demanded by large groups of the profession and supported by policy-makers needs to be corrected. Political science analyses of the German and European decision-making processes in the field of agricultural policy do identify the opening up of agricultural policy networks, which had acted in a rather isolated manner up to the 1980s. However, these analyses also highlight ongoing dominant influence of these networks. This is illustrated by the "watering down" of the greening proposals undertaken in the political negotiation process of the last CAP reform, and, in principle, the ongoing high income transfer for



the agricultural sector (cf. Alons 2017, Erjavec and Erjavec 2015, Hart 2015b, Roederer-Rynning 2015, Swinnen 2015, Daugbjerg and Swinbank 2016).

28. The position advanced by the German Agricultural Society (DLG) shows, however, that a corresponding reorientation is also possible within the sector. In its position paper on agriculture 2030 published at the beginning of 2017 it states, for the first time, that direct payments are “not to be viewed as established rights in the long term” (DLG 2017: 2)<sup>7</sup>. A necessary condition for a change in paradigms in European agricultural policy is, however, far wider communication than was the case in the past of the blatantly weak justification for the ongoing unconditional granting of direct payments. This is the only way of bringing to an end the “entitlement culture” (Matthews 2016) which is particularly obvious in the direct payments.<sup>8</sup>

## 2.2 Which architecture and allocation of competences should be implemented in the CAP?

29. In the current reform debate about the CAP post 2020 different stakeholders frequently adopt a recurring stance on the question of the CAP architecture. In this context the professional interest groups normally vehemently advocate the continuation of the current two-pillar structure. In contrast, many scientists recommend the explicit review of and changes to the instruments, funding conditions and allocations of competences established within this structure (cf. the current reform proposals of Feindt et al. 2018a, b, Fresco and Poppe 2016, Isermeyer 2014, Mahé and Bureau 2016, Matthews 2016).

30. At the current time, the CAP has a so-called first pillar with fully EU-funded direct payments and a second pillar with an extensive set of measures. The second pillar constitutes the basis for the rural development programmes which the Member States or regions program and co-fund nationally or regionally.<sup>9</sup> At EU level the respective measures are administered and funded by the European Agricultural Guarantee Fund (EAGF – first pillar) and the European Agricultural Fund for Rural Development (EAFRD – second pillar) (cf. Table 1).

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<sup>7</sup> Original text in German, translation by the authors.

<sup>8</sup> Matthews (2016: 70f.): “The presumption is also that direct payments are an entitlement to additional income, and that any associated obligations should be minimised (farmers are even allowed to transfer or sell this right to a benefit granted by the taxpayer and retain the proceeds, something unheard of in other sectors). This entitlement culture must be brought to an end. Instead, farmers should be offered the option to enter into a contract with the public authorities to provide stated services (which will mostly be of an environmental nature but not necessarily so).”

<sup>9</sup> In the current funding period, the Member States have an opportunity to reallocate up to 15 % of the national direct payments for measures currently administered by the European Agricultural Fund for Rural Development (EAFRD). These transferred direct payments are then financed 100 % by the EU.

**Table 1:** EAGF and EAFRD in comparison (funding period 2014–2020)

Characteristics	EAGF <sup>1</sup> (1st pillar)	EAFRD <sup>2</sup> (2nd pillar)
Objectives	Increasingly diverse but purely sectoral, e.g. income support, environmental and climate protection, generational renewal	Diverse and cross-sectoral, e.g. competitiveness, environmental and climate protection, territorial rural development (cf. Chapter 2.7)
Types of measures	Only annual measures, in particular direct payments ( <i>inter alia</i> basic payment, greening, payment for young farmers, cf. Chapter 2.3)	Multiannual measures, investment or one-off payment
Beneficiaries	Active farmers	Relatively “freely” definable (farmers, forest owners, communities, etc.)
Programming	No, only to be notified to the European Commission: creation of legal foundations needed at the national level	Yes, multiannual, comprehensive programming documents needed which requires approval by the European Commission
Financial management	Annuality principle	N+3 rule <sup>3</sup>
Premium calculation	Payment may generate income effect	Oriented towards the recipient’s expenses (only cost compensation)
Option of additional national funding (top-ups, without EU funding)	No <sup>4</sup>	Yes
Cross compliance (CC)	Yes	Yes
Funding modalities	100 % EU-funded	Member State co-funding
Proportion of EU agricultural budget	Approx. 75 %	Approx. 25 %

<sup>1</sup>EAGF: European Agricultural Guarantee Fund; <sup>2</sup>EAFRD: European Agricultural Fund for Rural Development; <sup>3</sup>N+3 rule: EAFRD funds may be spent up to three years after approval; hence the last payments will be made up to 2023. <sup>4</sup>Exception: the ten new Member States may grant what are known as transitional national aid payments. Eight Member States made use of this in 2015. Source: own presentation.

31. Two main criticisms of the current design of the CAP are:

**a) Inadequately defined objectives and intervention logics<sup>10</sup>:** In the current CAP the same overarching objectives are pursued in part in the EAGF and in the EAFRD. However, the two funds imply major differences in the measures used and the design and funding competences established. One particular characteristic of the direct payments made via the EAGF is that they are based on unclear and far from explicit intervention logics. This situation has been repeatedly criticised by the Europe Court of Auditors (ECA), recently in

<sup>10</sup> The intervention logic corresponds to the (assumed) causal chain of financial input over output and the results of a measure down to its impact on the desired objective. The intervention logic, therefore, requires sufficiently defined objectives and the robust presentation of (assumed) cause effects relations between measures and objectives.

conjunction with the basic payment rules (ECA 2018b), the greening payments (ECA 2017a) and the young farmer support (ECA 2017b).<sup>11</sup>

**b) Inadequate allocation of funding responsibilities:** A scientifically founded allocation of funding responsibilities is normally done on the basis of the following questions: (i) Are the objectives of supranational or national importance? (ii) To what extent could these objectives be better tackled on a European or global scale? (iii) Has adequate consideration been given to the level of economic development and, thus, to the economic strength of the Member States or regions? At the present time, these principles are not adequately reflected in the CAP. Regarding an effective greening premium, it could be argued that a policy oriented towards general environment and climate protection objectives justifies a high level or even 100 % communitised funding (cf. WBAE and WBW 2016). However, the Board is of the opinion, that there are no sufficient arguments to justify a high level or even 100 % communitised funding for the other direct payment components. Income objectives, in particular, are to be pursued primarily through the economic activities of farmers within the value chain, and existing income problems are to be solved by national social and tax policies and the development of employment opportunities outside farming (cf. Chapter 2.3).

32. Against this backdrop the Board welcomes the restructuring and disentanglement proposals regarding design and funding responsibilities put forward by science (cf. for instance Mahé and Bureau 2016, Matthews 2016, Feindt et al. 2018a, b). The Board likewise welcomes the option of national co-funding of direct payments presented in June 2017 by the Commission in its reflection paper on the future of EU finances (EU COM 2017b) or the option of purely nationally funded top-ups. The 100 % communitised funding of direct payments creates from the perspective of the Member States a financial policy distortion in favour of one-size-fits-all area-based premiums. In the opinion of the Board the introduction of co-financed direct payments, constitutes an important first step towards ending this distortion, and to begin tackling their urgently needed downsizing. The arguments presented against national co-funding in terms of the functionality of the CAP are not very convincing. As direct payments are payments which are very much decoupled from production, they scarcely lead to any output market distortion and the argument that co-

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<sup>11</sup> Just like the basic payment (cf. Chapter 2.3) and the greening premium (cf. Chapter 2.5), the young farmer support in the first pillar is not based on the individual establishment of needs and leads to high deadweight effects. Furthermore, the payments under the first pillar are not adequately coordinated with support for young farmers in the second pillar. What is particularly problematic is that incentives are created that encourage unprofitable farms to keep going, at least during the phase of entitlement to the payment, and to exploit the payment volume for the maximum 90 hectares that are possible under EU law maximum but have still to be specified by the Member States. This form of support, therefore, leads to stiffer local competition for land. Against this backdrop the young farmer support should be granted exclusively within the framework of the second pillar in the opinion of the Board. The precondition for support should, moreover, be business plans which not only project the farm's economic profitability as a consequence of support but also European added value.

funding prevented “the currently smooth functioning of the internal market”<sup>12</sup> is not understandable and seems to be a mere pretext.

33. The EU Council of Agriculture Ministers in Brussels in July 2017 formulated an unequivocal rejection of the national co-funding of direct payments (Agra-Europe 2017). This shows how difficult it would be to push through such a change of the CAP funding structure.<sup>13</sup> The main reasons for this resistance are the distributional implications of such a change. In particular, the new Member States reject the co-funding of direct payments. This is not surprising as the convergence of direct payments desired by them would probably lead to an improvement in their net recipient situation (cf. Hungarian Ministry of Agriculture 2017, Lehmann 2017, Council of the European Union 2017). In order to win the support of the new Member States for national co-funding, a sliding scale of national co-funding rates could be introduced (as is already the case with the EAFRD measures). Lower national shares in economically weaker Member States would constitute a major contribution towards convergence of the Community-funded share of direct payments demanded by the new Member States and proposed by the European Commission (2017a).<sup>14</sup>

34. A central component of a targeted restructuring of the CAP architecture should be a fundamental review and redesign of the allocation of competences in the multi-level system of the EU (cf. WBA 1997, 2005a, b, 2010, 2011b, for Germany Weingarten et al. 2015). Historically speaking, the approach adopted by the EU in both the first and the second pillar involves creating a narrow implementation corridor by means of comparatively detailed measures and eligibility rules. In the more recent past, more scope for action for Member States was opened up along the lines of the subsidiarity principle in a few areas, for instance the design of direct payments.

35. In its Communication of November 2017, the European Commission paints the picture of a future CAP which continues down the decentralisation path. According to this, when it comes to implementing the CAP “the Union should set the basic policy parameters (objectives of the CAP, broad types of intervention, basic requirements), while Member States should bear greater responsibility and be more accountable as to how they meet the objectives and achieve agreed targets” (EU COM 2017a: 9). To ensure implementation in tune with the EU-wide objectives, the Commission proposes the joint programming of all budgetary measures in national strategic plans.

36. In the opinion of the Board, the general approach of creating guiding principles, i.e. an EU-wide catalogue of objectives and a regulatory framework within which the Member States assume responsibility for meeting these objectives, should be pursued. In addition, the Board welcomes, in principle, the joint programming of all budgetary measures. A decentralisation of the CAP in line

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<sup>12</sup> Quote from an earlier version of the Commission Communication of November 2017 (EU COM 2017a). A full copy of this version can be accessed at: <http://www.arc2020.eu/cap-communication-leak-full/> (last accessed: 08.04.2018).

<sup>13</sup> Cf. also the note of the European Council on the debate about the CAP after 2020 on the basis of the Commission Communication of November 2017 (Council of the European Union 2018).

<sup>14</sup> Cf. Matthews (2018) for a more extensive discussion of the arguments in favour of national co-funding of direct payments.

with the principles of result orientation and national flexibilisation facilitates improved adjustment to regional and local conditions and needs. It also has the potential of achieving greater societal acceptance of the CAP. Nonetheless, Member States should be able to deviate from the joint programming of all budgetary measures in one national strategic plan if they prefer implementation via regional strategic plans or a combination of national and numerous regional plans. This is relevant, for instance, for Germany as here the competences for today's second pillar of agricultural policy lie with the federal states.<sup>15</sup>

37. However, pursuit of the approach proposed in the Commission's Communication (EU COM 2017a) does throw up further challenges. Firstly, suitable incentive, control and penalty systems have to be developed which promote an ambitious target setting of the Member States within the framework of their "subsidiary responsibility". Secondly, an eye must be kept on the related administrative costs (both for the administration and the beneficiaries) which should be reduced to an appropriate level.

38. The European Commission must lay down a basic framework with certain minimum standards in order to prevent a race to the bottom by individual Member States. Otherwise Member States could use their "subsidiary responsibility" to create competitive advantages or grant hidden income support to their farmers by way of less ambitious programme designs. This framework could encompass targeted minimum budgets (e.g. for environmental measures) or the delimitation of target areas for certain measures (e.g. Natura 2000) but should not contain any detailed requirements. The review of the programmes (national strategic plans) should – as stipulated for all aid-relevant measures – be undertaken within the framework of a notification procedure. The programme review should focus on the clarity of the objectives, their operationalisation and the plausibility and suitability of the indicators for monitoring success. The definition of the corresponding indicators should be left, more than was the case in the past, to the Member States. The detailed control at the level of the measures should not be in the focus of the programme review.

39. This approach is in line with the subsidiarity principle and is appropriate given the pronounced heterogeneity of the natural and socio-economic conditions as well as preferences within the EU. Furthermore, in the opinion of the Board, mutual recognition of the audits conducted at the various control levels with a view to establishing a single audit system<sup>16</sup> for the

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<sup>15</sup> For the current support period (2014-2020) a multi-fund partnership agreement between Germany and the European Commission for the implementation of the European structural and investment funds had to be concluded under the joint strategy framework in the support period 2014 up to 2020 (BMWE 2014a, b). In the support period from 2007 up to 2013 a "national strategy plan of the Federal Republic of Germany for rural development" (BMELV 2011) had to be prepared. According to Tietz and Grajewski (2016: 38) the governance impact of both strategy documents in Germany is close to zero. According to Weingarten et al. (2015: 44) it has become clear for Germany that the national strategy plan does hardly induce any strategic governance effects, while it does engender major coordination efforts.

<sup>16</sup> The European Court of Auditors has defined the single audit system as an internal control and audit system which is based on the fundamental idea that each control level builds on the previous one (ECA 2013: margin number 12). The single audit system is already used in cohesion policy (cf. Article 148 of Regulation (EC) No 1302/2013). It aims to avoid the duplication of work and to reduce the overall costs of control and audit activities at the level of the Member States and the Commission.

EU and the Member State (or in the case of Germany for the German Federal Government and the federal states) is a model that should be pursued and extended. This would help to reduce red tape. Multiple audits by various auditing bodies mean a higher administrative burden not least for farmers and other beneficiaries and can lead to contradictory evaluations because of the different audit methods.

40. Increased focus on the objectives instead of the procedures of the CAP and an allocation of targeting, decision-making, funding and implementation competences oriented more towards the principle of subsidiarity will not, however, automatically lead to a less complex CAP with less red tape although the European Commission does link this approach with the catchword “simplification” (cf. EU COM 2017a: 10).

41. Many sides stress the urgent need for simplification. For instance the European Court of Auditors (2017c) called its special report 16/2017 “Rural Development Programming: less complexity and more focus on results needed”. The Saxony State Ministry of the Environment and Agriculture describes the second pillar of the CAP as follows: “Over many funding periods, it has developed into such a complex and complicated system that it has become a symbol of an European funding bureaucracy remote from reality for many applicants and administrative authorities in Europe” (SMUL 2016: 3).<sup>17</sup> In the federal government-federal state paper on the new direction for implementing EU policy on rural development (N.N. 2017) it is noted that, as a consequence of the growing formal requirements, specialised goals are increasingly taking a backseat.

42. Administrative simplification or a reduction of the administrative burden is not, however, an objective in itself. It is important for the administrative burden to be commensurate with the target contributions which are to be achieved by implementing the measures. The European Court of Auditors (2018a: 22) remarks in this context “simplification needed but not at the cost of effectiveness”. Studies by Fährmann et al. (2014) within the framework of the evaluation of rural development programmes show that the implementation costs of rural development measures vary considerably depending on the measure.<sup>18</sup> Regression analyses by Fährmann and Grajewski (2013) revealed a statistically significant positive correlation between the level of the relative implementation costs and the efficacy of the measures examined.

43. It is therefore important to increase implementation efficiency without reducing the effectiveness of the measures. Limited implementation efficiency can have several reasons. For

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<sup>17</sup> Original quote in German “Sie ist über viele Förderperioden hinweg zu einem so komplexen und komplizierten System geworden, dass es für viele Antragsteller und die Verwaltungen in Europa zu einem Symbol für eine realitätsferne europäische Förderbürokratie geworden ist.” (SMUL 2016: 3).

<sup>18</sup> Moreover, implementation cost analyses by Fährmann et al. (2014) show that the costs also depend on the specific implementation. Fährmann et al. (2014) examined the relation between implementation costs of the administrative authority and the support funds spent in four rural development programmes in Germany. This share ranged, for instance, from 1 % to 10 % for the compensatory allowance, 22 % to 45 % for contract-based nature conservation and between 4 % to 18 % for individual farm investment support.

the second pillar this has to do firstly with the policy design, i.e. complex objective systems and rampant strategy levels (see footnote 15, p. 19), secondly with the design of the administrative and control system. The main administrative reasons for the limited implementation efficiency have to do with the inadequately designed indirect enforcement<sup>19</sup> of the CAP (which leads to the duplication of control structures), an unclear legal situation (which in some cases can also be amended retrospectively and is exacerbated by fixed term-legislation), stiff penalties<sup>20</sup> and the inappropriately strict EU attitude towards proper fund allocation. The maximum error rate in conjunction with the volatile legal framework is unacceptably low particularly for the heterogeneous and complex support approaches of the second pillar. These causes have led to cascades of documentation, control and reporting obligations (Rechnungshof Baden-Württemberg 2015: 13) where the administrative burden is completely disproportionate to the control result, i.e. the correction of erroneous expenditure. For instance the cases examined by the Court of Auditors Baden-Württemberg (Rechnungshof Baden-Württemberg 2015) generated administrative and control costs that were 21 times higher than the financial error which it corrected. The scale of correction of on average 0.6 % was very low and cannot be justified solely through the dissuasive impact of EU penalties on non-compliance with EU rules.

44. These causes can only be modified to a limited degree by a reform oriented solely towards the CAP. Hence, the Board advocates addressing the main causes of the administrative burdens for the Member State administrations, farmers and others who obtain support from the CAP and not just the short-term symptoms. The Board strongly recommends the following steps:

- a) **Reduce and codify the EU implementing provisions for the CAP:** EU implementing provisions contain instructions for the Member State administrations mainly on fact-finding measures, the process of weighing up various interests, and follow-up control of completed procedures. These implementing provisions are part of all market regulations (including direct payments) of the CAP and in the instrument-related provisions in the second pillar. Specific rules on individual instruments are needed. Moreover, fixed-term legislation leads to a periodical critical examination of the deficits of the system and opens up the possibility

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<sup>19</sup> Enforcement and application of Union law by the Member States in contrast to direct enforcement by EU organs.

<sup>20</sup> These mechanisms exist both in the relationship between the Member State and the European Commission and also in the relationship between the support administration and the support recipient. The first has to do with the financial correction mechanism by means of which, in the opinion of the European Commission, erroneous expenditure involving Community funding can be ruled out. These mechanisms are applied both in the case of concrete errors as well as in the case of abstract risks. The pressure on the implementing authorities is correspondingly high. The EAFRD regulation also imposes penalties on support recipients. They were taken over from the area of direct payments – where they are justified because of the existing payment entitlements – for the EAFRD support. They are perceived above all in the field of investive support measures as alien to the system particularly because they do not exist in other European structural and investment funds. The penalty provisions in the field of investment measures confront the administration with challenges and frighten off applicants. As the German national funding legislation does not envisage any penalties, the applicants must be informed when they apply about the circumstances under which penalties may be imposed. The added value of this instrument that assumes from the outset that the applicant intends to commit fraud cannot be identified for a support area which is dependent above all on partners to achieve the specified objectives (cf. Fährmann et al. 2014).

for public discussion. However, a reduction in the implementing provisions to the necessary EU minimum (see above) and a codification of generally valid rules of procedure, i.e. the systematic compiling of all implementing provisions relevant for the CAP into a single codified law with an unlimited duration, would lead to the emergence of administrative and legal practice and, thus, to certainty in action. Moreover, a critical scientific evaluation of these standards and the related development of own administrative law dogmatics would be facilitated. The Member State authorities and the parties concerned would no longer face the problem of having to reinterpret new legal texts at the beginning of each support period. This creates legal certainty and simplifies existing procedures. The codified and reduced administrative law provisions would basically render superfluous the sub-statutory rules of the European Commission.<sup>21</sup> Such a codified European implementing legislation promotes the principle of legality by creating, in a transparent manner, systematic, clear and coherent rules for the actions of the public authorities. If codification is restricted to administrative procedural provisions, it would not obstruct the periodic review of the substantive regulations of the funding instruments.

A codified European implementing legislation facilitates implementation of the CAP on the Member State level. As the CAP must be enacted indirectly, i.e. by the Member States, implementation in Germany must also take into account federal government and federal state law. Only in justified cases (e.g. higher accuracy) should implementation in Germany be undertaken in a more complex administrative manner than stipulated in EU law.

A codification of implementing provisions can lead in the long term to a simplification of administrative procedures. But this does not remove the need for prior critical appraisal about the soundness of the underlying provisions.

**b) Increase the efficacy of the control system:** The EU, in concrete terms the European Parliament and the European Court of Auditors, currently defines the effectiveness of CAP enforcement exclusively along the lines of European financial control using the yardstick of the error rate in the application of funding instruments. The threshold, i.e. the accepted error rate, is currently 2 %. With strict control measures the European Commission achieved a rate of 3.1 % in 2016 for all EU expenditure (EU COM 2017d: 12). With an error rate of 1.7 % the expenditure of the EAGF (first pillar of the CAP) lie below the threshold whereas that of the EAFRD (second pillar) is far higher at 4.9 % (ECA 2017: annex 7.1). The threshold is not laid down in primary law but is based on a political consensus. Compared to the accepted error rate for German national funds of 20 to 30 %, <sup>22</sup> the EU threshold is disproportionately low. To achieve these low error rates within the support system the prerequisites are low tolerance values, intensive control, reporting and obligations for

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<sup>21</sup> For example, guidelines, guidance documents, working documents or explanatory notes, sometimes a “recommendatory” character.

<sup>22</sup> E.g. Brandenburg 29.5 % (2015) (Courts of Auditors Brandenburg 2017: 58), Schleswig-Holstein 21 % (2016) (Court of Auditors Schleswig-Holstein 2017: 15), Bayern 34 % in the financial administration (Bavarian Supreme Court of Auditors 2017: 108).



financial correction of the Member States and comprehensive competences of the Commission to uniformly change, also retrospectively, the interpretation of the CAP provisions for the purpose of greater budgetary discipline. These preconditions for a tax-efficient CAP are, however, in conflict with substantive effective actions in terms of the policy objective of the Member State authorities. The authorities react by trying to do everything exactly as prescribed. Out of fear of demands for financial correction, they do not take any decisions until the Commission has agreed on a uniform interpretation. This means that indirect enforcement of the CAP by Member State administrations that act autonomously is conducted *ad absurdum*.

In substantive terms, simplified administration – in addition to the approaches listed under a) – can only be reasonably achieved if the EU moves away from the purely fiscal evaluation of the efficiency of the CAP by using the yardstick of an error rate of 2 %. Here the maximum admissible error rate should be laid down in an appropriate manner for the respective policy area as suggested by the European Commission in its proposal on “tolerable risk of errors” presented in 2008 (EU COM 2008). When analysing administrative procedures from an administrative point of view, the direct payments from today's first pillar and the development programmes for rural areas from the second pillar are two completely different support systems.<sup>23</sup> Given the fundamentally different policy design the admissible error rate for the second pillar rate should be larger than for direct payments in the first pillar. For both pillars higher tolerance values and definitive statutory and understandable criteria should be used in the financial correction procedure. From the organisational legal angle, the introduction of a single audit system (see above) should be implemented to simplify administrative procedures. The related reduction in control density is realistic even without compromising the basic principles of budgetary discipline in the EU. With respect to the CAP, the EU should, as is already the case in the field of cohesion policy, have greater faith in the Member State administrations when it comes to implementing financially effective instruments.

Furthermore, existing data and also digital technologies should be used far more than in the past for area-related measures as the basis for the design, application, evaluation and control of measures in order to keep the administrative costs as low as possible despite the pronounced regional heterogeneity of the design of agricultural policy measures (cf. DVL 2017, Feindt et al. 2018a, Fresco and Poppe 2016, WBA, WBD and SRU 2013).

45. To summarise, the Board is of the opinion that in the medium term the funding-related distortion in favour of direct payments should be overcome. Furthermore, the CAP should, in principle, develop into a policy for agriculture and rural areas which is designed and integrated in accordance with the subsidiarity principle. The precondition for this development is a

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<sup>23</sup> The farmer is entitled to direct payments when certain requirements are met. With the rural development programmes, in contrast, that implement the second pillar today, the Member State or region ideally “purchases” public goods from the applicant. Consequently the state or region can much better address its needs than is possible through the granting of direct payments (cf. Fährmann and Grajewski 2018).

programming of budgetary CAP measures and ensuing accounting which is conducted by the Member States or, where appropriate, by the regions within the framework of European guidelines. Under this system, the EU would remain responsible for the review of the ex-ante and ex-post evaluation of the strategic plans with respect to objective coherence, measurement indicators and cause-effect-relations as well as for the monitoring of the national implementation from the angle of competition law. The proposals made by the European Commission (2017a) in its Communication are moving in the right direction when it comes to shifting design competence to the lower levels. However, the inequality in co-funding in favour of direct payments is not addressed and this impedes further development of a CAP that serves the public good. Whether the reduction in detailed rules for the administrative and monitoring systems, including the verification of legitimacy, and the increased outlay for performance checks outlined by the European Commission will result overall in a simplification of administrative procedures depends on the concrete design of the CAP post 2020 including its implementing provisions.

### **2.3 Does European agriculture need sectoral income support and is this justifiable within the framework of the CAP?**

46. Around 38 % of the EU budget is spent on European agricultural policy in the current financial period (2014-2020). Most of these funds (73 % or approximately EUR 40 billion annually) are paid out across Europe to farm owners by means of so-called area-based direct payments. The lion's share (55 % of all direct payments as the EU average) are to serve as basic payments explicitly for the purpose of ensuring a basic income for farmers (Table 2). The so-called greening premium, with a share of 30 % of all direct payments, is in financial terms the second most important direct payment. According to EU Regulation 1307/2013 it constitutes a "payment for agricultural practices beneficial for the climate and the environment". These payments are to remunerate the provision of public environmental goods by farmers. However, given the limited additional environmental impact (cf. Chapter 2.5), this share of direct payments is basically income support (ECA 2017a).

**Table 2:** System of direct payments (DPs) in the current CAP support period (2014-2020)

Components	Details of share of national DP budget	Binding nature <sup>1)</sup>	Number of implementing Member States	Share in overall DPs in EU 2016 <sup>2)</sup>
Small farmer payment	≤ 10 %	vol.	15	1.2 %
Payment in areas with natural constraints	≤ 5 %	vol.	1	0.0 %
Production-coupled payment	≤ 10 up to 15 %	vol.	27	10.0 %
Redistributive payment (first hectares)	≤ 30 %	vol.	9	4.0 %
Payment for young farmers	≤ 2 %	mand.	all 28	1.2 %
Greening payment	30 %	mand.	all 28	30.0 %
Basic payment	Remaining DP budget	mand.	all 28	54.8 %

Note: <sup>1)</sup> vol. = voluntary, mand. = mandatory. <sup>2)</sup> Sum of shares slightly over 100 % because of the possibility of overbooking. Source: Weingarten and Rudloff (in preparation) according to the European Commission (EU COM 2013, 2016a).

47. To justify sectoral income aids, representatives of the agricultural profession and agricultural expert policy (cf. for instance the current Communication of the European Commission, EU COM 2017a) repeatedly state that (a) agricultural production is exposed to specific disadvantages (for example, weather dependency), which is reflected in yield, price and, in the final instance, income volatilities, (b) agricultural enterprises in the EU in comparison to those in other regions of the world with whom they compete must comply with higher product and process standards and therefore had cost disadvantages and (c) there was a major fundamental income gap between the (lower) agricultural and (higher) overall economic income. The classical argumentation is that there was a need for sectoral income aids in order to compensate income volatilities, cost disadvantages because of higher production and process standards, and also the outlined income gap.

48. This chain of arguments does not stand up to critical examination:

**a) Specific disadvantages because of weather dependency.** The conclusion that agriculture enjoys a special status because of its weather dependency is far from convincing. Other sectors are also exposed to “special” factors. For instance, the sales revenues of the tourist sector very much depend on the weather and energy-intensive sectors are likewise affected by major fluctuations in prices for energy sources.

**b) Cost disadvantages through conditions and standards.** Before sectoral income aids can be justified on the basis of higher product and process standards in Europe, the following questions must be clarified: (1) Are there cost disadvantages because of higher product and process standards and, if so, how high are they? (2) Should these be compensated by the state? and (3) if so, are the area-based direct payments a suitable instrument?

(1) Existence and level of cost disadvantages because of higher standards: It is undeniable that the EU has higher state requirements than many countries outside the EU. Information on the related costs is, however, sparse and varies considerably. This has to do not least

with the fact that the quantification of these costs comes with major methodological challenges and restrictions. They are to be found, for instance, in the choice of the requirements/standards considered and the definition of the reference system. Frequently, a situation without any requirements is defined as the reference. This fails to take into account the fact that farmers in countries with few state requirements must frequently meet private sector requirements with similar costs for agriculture (e.g. sustainability programme of Fonterra in New Zealand, GLOBALG.A.P.). The adequate consideration of cost-reducing adjustment reactions of farmers constitutes a challenge. A static evaluation overestimates the costs in comparison to a dynamic consideration. Furthermore, it should be borne in mind that the various production areas and regions<sup>24</sup> are affected to varying degrees by standards which means that various cost effects may emerge depending on the type of farm and region.

Scientifically backed studies on the cost effects in the EU caused by food law requirements and environmental protection and animal welfare standards, for instance, indicate a production cost share of 1 to 3 % in milk production, 2 to 9 % in pig and poultry husbandry and 2 to 3.5 % in wheat cultivation (cf. Menghi et al. 2014).<sup>25</sup> Plankl et al. (2010) calculate that environmental regulations in arable farming contribute to around 2 % of production costs. In the year under review this corresponds to around EUR 19/ha (Plankl et al. 2010). A recently published study commissioned by the German Farmers' Association (DBV) calculates cost effects on a completely different scale (Karl and Noleppa 2017). Annual costs for German agriculture of EUR 5.2 billion are calculated for compliance with environmental standards and other requirements. This would correspond to additional expenditure of EUR 315/ha that is approximately equivalent to the current direct payments. As this study is currently the subject of extensive political debate despite its considerable methodological shortcomings, a short discussion is undertaken here of the critical assumptions and methods on which the calculations are based. There is an overestimation firstly because the authors do not take into account the fact that some of the measures included in the cost estimation are part of normal practice and make business sense (choice of the reference situation). For instance, when calculating the costs of greening, they ignore the fact that only some of the designated ecological focus areas can be attributed to these requirements. A major share of the areas were already there. Hence, there is a major overestimation of the impact.<sup>26</sup> Secondly, results are extrapolated on the basis of case

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<sup>24</sup> For instance the costs of complying with the Fertiliser Application Ordinance in regions with high cattle densities are far higher in regions with little cattle.

<sup>25</sup> Menghi et al. (2014) prove in their study that the requirement-driven costs are, in most cases, not the main reason for any higher production costs for EU farms. The main cause of cost differences are higher prices for inputs, production factors and, in some cases, lower productivity.

<sup>26</sup> An example: slurry containers are necessary for the economically reasonable application of fertilisers in line with the needs of arable crops. In the study no differentiation is made between the costs for the slurry containers which would have to be set up in any case for farm slurry management and the costs which are only incurred because of the provisions

studies from literature. As the case studies used are not representative and refer to particularly affected regions or farms, a simple extrapolation based on area and animal numbers leads to an overestimation of the requirement-driven costs. Thirdly, the condensation of the studies is frequently not done correctly but by means of simple averaging of what are, in some cases, highly divergent values from different years. Furthermore, it must be borne in mind that less strict requirements in other countries are probably also in many cases linked to varying scarcities. Requirements linked to high population and livestock density are also less relevant in countries with lower population and cattle density. Last but not least, in a balanced consideration, the benefits of high population and cattle densities, for instance the comparatively good infrastructure, higher prices and advantages of regional agglomeration, would have to be set against the higher requirement-driven costs and then evaluated. This is not done in the study either.

(2) State compensation for existing cost disadvantages: An interim conclusion is that for a serious and expedient discussion about the cost effects of standards and, where appropriate, the necessary compensations for these effects, it is necessary to set any negative effects caused by the standards against positive cost and price effects. Furthermore, it should be borne in mind that a major share of food and environmental requirements in the EU and in Germany are designed to prevent market risks or to consciously internalise the negative external effects of production (for instance in the case of nitrate leaching in groundwater the costs would otherwise be borne by other societal stakeholders). Many of these external effects occur at the local or regional level. Their internalisation, therefore, constitutes a cost disadvantage which can indeed express the scarcity of environmental goods in an appropriate manner. The extent to which adaptation or compensation payments should be paid for compliance with minimum statutory requirements needs to be discussed on a case-by-case basis. In addition to efficiency criteria, questions of fair distribution may play a role.

(3) Area-based direct payments as a compensation instrument: The degree to which farms are affected by standards varies considerably in Germany and the EU. One-size-fits-all aid per area unit is not, therefore, the right instrument for general compensation of cost disadvantages.

**c) Fundamental income gap.** The argumentation that there was a considerable fundamental income gap between agricultural and overall economic income is based in many ways on questionable assumptions and calculations: (1) by only taking into account agricultural income, the calculations are based on an inadequate reference system and an incomplete information base whereby (2) the actual income situation of the agricultural community is only partially depicted and tends to be underestimated. Furthermore, (3) existing assets are not included in the calculations and, last but not least, (4) detailed evaluations of agricultural

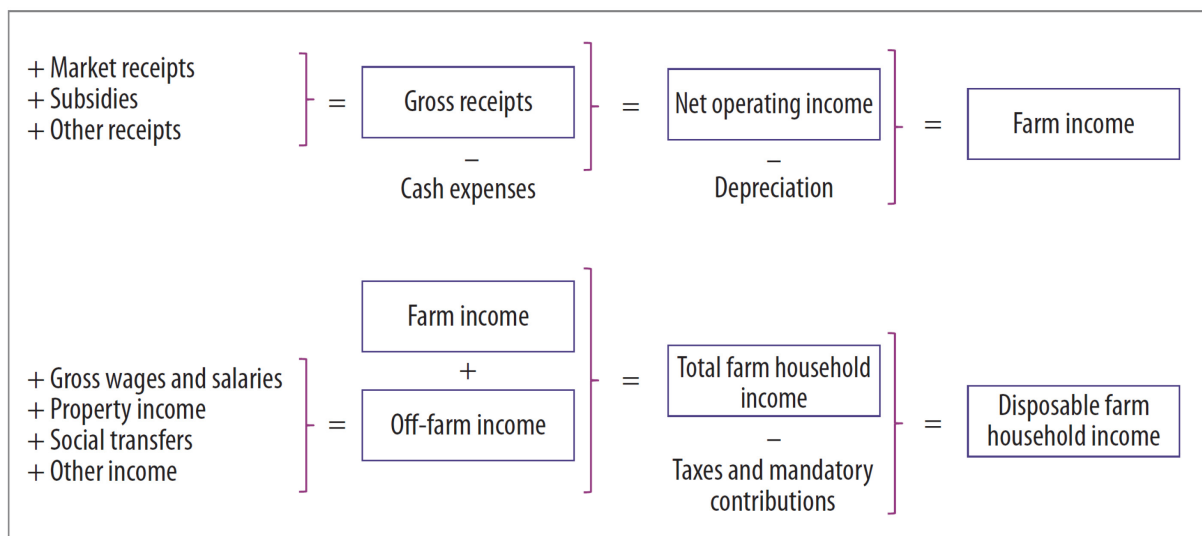
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in the Water Framework Directive. Another example is that the spread of low emission application technology has increased even without the requirements of the new Fertiliser Application Ordinance in recent years and that this technology offers monetary benefits for farms in various regions because of improved nutrient use.

income show that they vary considerably (even in the case of the same size and same farm orientation) – which means that, in this case too, there can be no talk of a fundamental income gap that affects all farms.

(1) Reference system: The calculations to assess the income situation in agriculture are based on a reference system which only looks at agricultural income. In order to be able to adequately assess “a fair standard of living for the agricultural community” (cf. section 39 (l) (b) TFEU), the total available income of farm households should be taken into account (ECA 2003, 2016, 2018a, Hill and Bradley 2015, OECD 2003; cf. Fig 2.). There is no comprehensive information basis available at the present time to the European Commission that would permit an income calculation of this kind. This means that solid statements about the general or average income situation are not possible. This situation has already been criticised several times by the European Court of Auditors (e.g. ECA 2003, 2016, 2018a). As the share of agricultural workers is steadily increasing, a suitable reference variable for their wages would also have to be developed and included in the income assessment.

**Fig. 2:** Components of farm household income



Source: OECD (2003: 16), ECA (2016: 12).

(2) Underestimation of the income situation of farm households: The actual income situation of many farm households is, therefore, only partially depicted and partially considerably underestimated in the income calculations of the European Commission or the BMEL. The analyses by Hill and Bradley (2015) and the OECD (2003) indicate that farmers (based on their average household income) do not constitute a particularly low income group in the population (cf. also ECA 2018a). This means that they have an average household income which is comparable to the rest of society. This conclusion is based in particular on the fact that economically important diversification activities are on the

increase throughout the EU (Augère-Granier 2016, Hill and Bradley 2015). However, they are not adequately recorded or considerably underestimated in the official statistics (for Germany cf. Stecher and Forstner 2015, Forstner and Zavyalova 2016).<sup>27</sup> For example, in Bavaria 70 % of all full-time farms have a combined income, revenue from non-agricultural assets (e.g. rent and tenancies) is growing steadily, and only 16 % generate their income solely from primary agricultural production (Weinberger-Miller 2013, 2011). For Germany exemplary analyses based on wage and income tax statistics show that all individuals liable for income tax with income from agricultural and forestry (i.e. including part-time farming) in 2010 only generated on average 27 % of their taxable income from agriculture and forestry. The remaining income came from commercial enterprises (20 %), non-independent work (43 %) and further types of revenue such as capital assets, etc. (10 %).<sup>28</sup>

(3) Assets not taken into account: In order to be able to adequately estimate the standard of living of agricultural households, the existing assets would have to be taken into account. Family run farms in particular frequently have relatively large assets as many of the production factors belong to them. Assets contribute to the standard of living to the extent that, in the case of an increase in value (e.g. land), when sold they are included in farm income. Furthermore, they are used as a security for loans and can contribute to the overall security and financial stability of farm households (Hill and Bradley 2015).

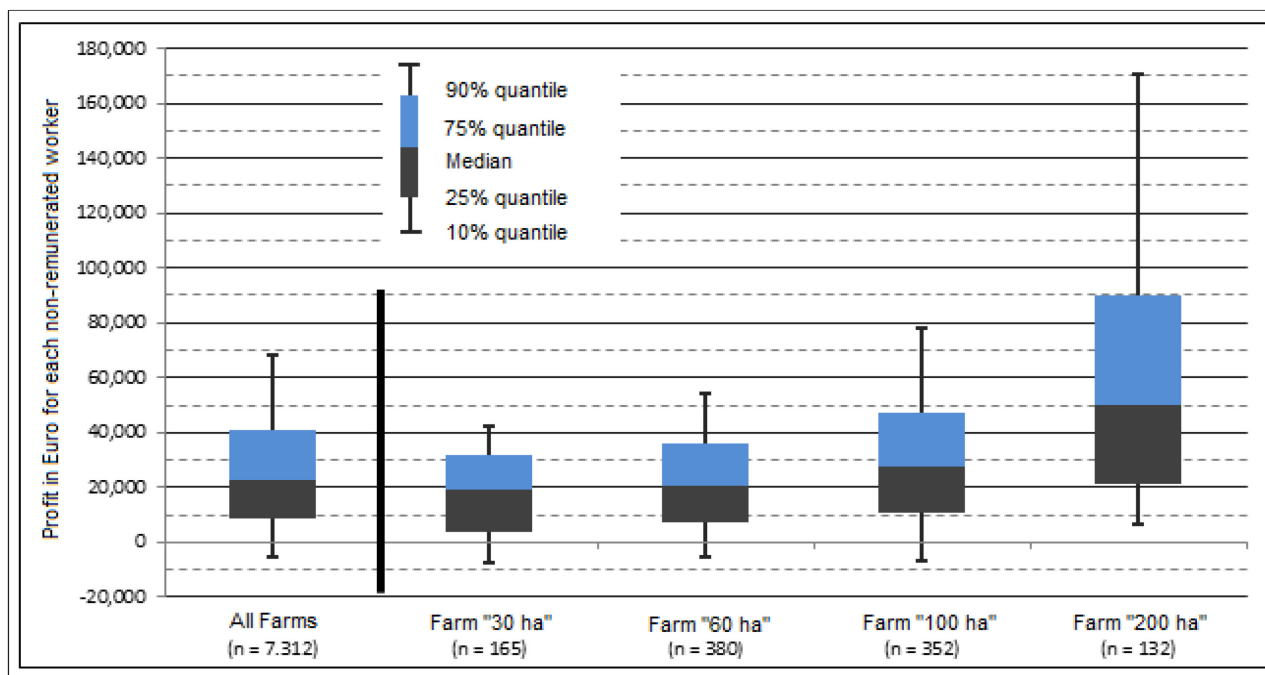
(4) Major spread in agricultural income: Furthermore, detailed evaluations of data from the German Farm Accountancy Data Network (FADN) clearly illustrate just how much the operating profits generated vary between regions and also between different types of farms and individual farms. Whereas in Germany in the financial year 2013/2014 around 40 % of full-time farms were able to achieve factor income above the comparative approaches (BMEL 2015: 55f.), other farms generate below-average (in some cases very much below-average) income from agriculture. On average, farms with larger production capacities are more successful economically in Germany. However, “larger farms” (based on area) do also sometimes generate profits which are way below average (Fig. 3).

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<sup>27</sup> Diversification activities such as, for instance, the renting of holiday apartments or the operation of biogas and photovoltaic plants are only then recorded in the official agricultural statistics if these are agricultural or forestry activities which are of relevance for income tax. As soon as the respective diversification activity exceeds a legally defined limit, the income generated from this is classified as “commercial” and is, therefore, no longer recorded in the agricultural statistics – even if the activity still belongs to the core farm (cf. for instance Forstner and Zavyalova 2016).

<sup>28</sup> Forstner and Zavyalova (2017): Calculation on the basis of wage and income tax data 2010, data set of the Research Data Centre of the Statistische Bundesämter (Statistical Offices) of the German Federal Government and the Federal States.

**Fig. 3:** Differences in success in full-time farms (individual farm) in the financial year 2015/2016



Source: Heiko Hansen, Thünen Institute of Farm Economics. Evaluations based on German FADN data.

Notes: The results are presented for the group of full-time farms with the legal form "individual enterprise". It should be borne in mind that the results vary considerably between the financial years. Whereas, for instance, the median of profits per unpaid labour unit in the financial year 2015/2016 for all farms were slightly more than EUR 20,000, they were far higher than EUR 30,000 in the financial years 2012/2013 and 2013/2014.

The size categories of farms are oriented towards their utilised agricultural area (UAA):

Farms in size category "30 ha" have an UAA of 28.5 up to 31.5 ha.

Farms in size category "60 ha" have an UAA of 57 up to 63 ha.

Farms in size category "100 ha" have an UAA of 95 up to 105 ha.

Farms in size category "200 ha" have an UAA of 190 up to 210 ha.

49. Furthermore, this argumentation fails to recognise when it comes to sectoral income support for farms that the European primary legislation does envisage independent income-policy responsibility in the area of farming<sup>29</sup> but the decisive factor here is neither personal nor farm needs. Instead, the need for special support results from the securing or support for the maintenance of societal functions of agriculture (Martínez 2016a: margin number 7). Deciding what is exactly meant by these societal functions is the prerogative of the legislature which does

<sup>29</sup> Contrary to the widespread interpretation of Article 39 TFEU, according to which the objective of a "fair standard of living for the agricultural community" is to be achieved through higher productivity, the report has established itself in the case law of the European Court of Justice that the guarantee of a fair standard of living is to be classified as a largely independent objective. Productivity and income support simply mean that income support measures are only admissible when the aid recipient is active in the field of farming with a view to making a profit. The measures may not, therefore, be conceived as one-sided social benefits, a primary law foundation for income policy measures within the framework of the CAP is however given and admissible. Cf. ECJ C-373/11, ECLI:EU:C:2013:567 margin number 54f. – Panellinos, Priebe (2017: margin numbers 11-13), van Rijn (2015: margin number 7) and Martínez (2016b: margin number 9f.).



enjoy a broad scope for interpretation recognised by the European Court of Justice (ECJ, C-280/93, margin number 47). This is concretised, however, through the horizontal clauses in primary law in the fields of climate protection, animal welfare, rural areas and health (cf. Chapter 2.1). Because of their standardisation in European primary law (the treaties and the general principles), the objectives contained in these horizontal clauses are defined as European interests, the implementation of which is to be deemed a “societal function” of agriculture. A sub-group of societal functions are the public services discussed in Box 2 on page 6 as they are provided on a voluntary basis beyond regulatory obligations.

50. Income support for agriculture is therefore a “purpose to an end” and this is how it is to be interpreted. A farm whose survival is in jeopardy may be individually in need. Need as specified in Article 39 of the TFEU does not, however, exist to the extent that

- (i) through the farm closure it is not the societal function of agriculture, for instance land management which is jeopardised and
- (ii) sufficient non-agricultural employment opportunities are available to ensure livelihoods (cf. settled case law since ECJ, 5/67, Coll. 1968, 127/147).

51. For the purpose of maintaining this function of agriculture, appropriate framework conditions must be put in place. If societal functions of agriculture are threatened by the closure of farms, for instance because agricultural land is taken out of production, targeted management premiums or premiums for nature conservation and environmental protection services can contribute to raising agricultural income with a view to maintaining these societal functions. Management premiums would have to be differentiated on the regional or local level (as they are already to a certain degree with the compensation allowance in the second pillar). This way, such management premiums would constitute a far more efficient instrument than today’s nation-wide granting of uniform direct payments.

52. Hence, it can be summed up: There is no evidence of a general income gap in agriculture, an argument advanced again and again by agricultural decision-makers. Nor can any justification for the one-size-fits-all support of individual farms be derived from the income objective defined in the TFEU. If income support should still be desired for farms in need, then the need would have to be individually determined on the basis of the farm household’s income. Sectoral policy on the EU level is not an appropriate approach for this. Firstly, a redistribution from high-income to low-income population groups could only be sensibly undertaken with due consideration of all types of income and assets of an individual or a taxable household. Income distribution of this kind is normally undertaken, in Germany too, by means of progressive income taxation and transfers within the framework of the social systems. Secondly, tax and social policy comes under the full responsibility of the EU Member States, not the EU. Against the backdrop of the subsidiarity principle there is no reason to pursue a sectoral income policy on the EU level which is oriented towards the personal need (Grethe 2008, WBA 2010, 2005a).

## 2.4 Should the distributional effects of direct payments be “corrected”?

53. Despite the fundamental criticism presented in the previous chapter about the arguments in favour of an income objective in agricultural policy, direct payments are rarely challenged fundamentally in the public debate. Besides increasing demand for a stronger environmental orientation, the public debates focus mainly on the failure to gear direct payments to the need of the recipients. There are repeated calls for “correcting” the system to make it “fairer” (cf. text numbers 56–58). However, in the opinion of the Board “corrected” direct payments are not a suitable instrument even if a sectoral income policy addressing individual needs were to be desired within the framework of the CAP. The reasons are explained in detail below.

54. The recipients of direct payments are only in part the actual beneficiaries because of the numerous passing on effects:

**a) Passing on to landowners.** With a share of leased land of 43 % in the EU and 59 % in Germany (west German federal states 54 %, east German federal states 68 %)<sup>30</sup> a large share of direct payments are capitalised into land rent and land purchase prices. This means that a substantial portion of direct payments goes to landowners in proportion to the amount of land they own (WBA 2010). Empirical analyses for Germany show that the amount of the passing on of direct payments into farmland rental rates varies considerably on local land markets with an average level of some 50 % (Garvert 2017). Klaiber et al. (2017) observed increasing passing on rates of 37 % to 53 % for decoupled direct payments in Germany between 2005 and 2011. The study by Kilian et al. (2012) and the analysis by Habermann and Ernst (2010) provide indications that the passing on effects have increased as a consequence of decoupling in Germany. For grassland leases, Hennig and Breustedt (2018) identified marginal passing on rates of decoupled direct payments of 49 % to 64 % for the period 2005 to 2010. During this period the premiums paid consisted of regional and individual farm premium shares. During the period after 2010, i.e. after the advanced streamlining of the individual farm premium shares, the estimates by Hennig and Breustedt (2018) indicate passing on rates of 87 % to 94 % for west German federal states.

**b) Passing on to wage income in agriculture.** A major and steadily increasing proportion of agricultural income is based on wage labour. Wage labour does not benefit directly from direct payments; nonetheless direct payments increase its remuneration potential (unless they are directly passed on to higher lease payments).<sup>31</sup> Employed labour can benefit in a twofold manner from this: firstly in terms of the level of its wages and secondly in terms of the employment impact.<sup>32</sup>

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<sup>30</sup> Cf. Statistisches Bundesamt (2017b).

<sup>31</sup> Usually, leases are entered into for longer periods which means that changes in the level of direct payments result in delayed reactions in terms of changes in leasing prices.

<sup>32</sup> In contrast to the passing on to landowners this passing on pursues, in principle, more the intention of income support for people working in agriculture within the meaning of the EU Treaty and the German Agriculture Act (cf. Chapter 2.3).

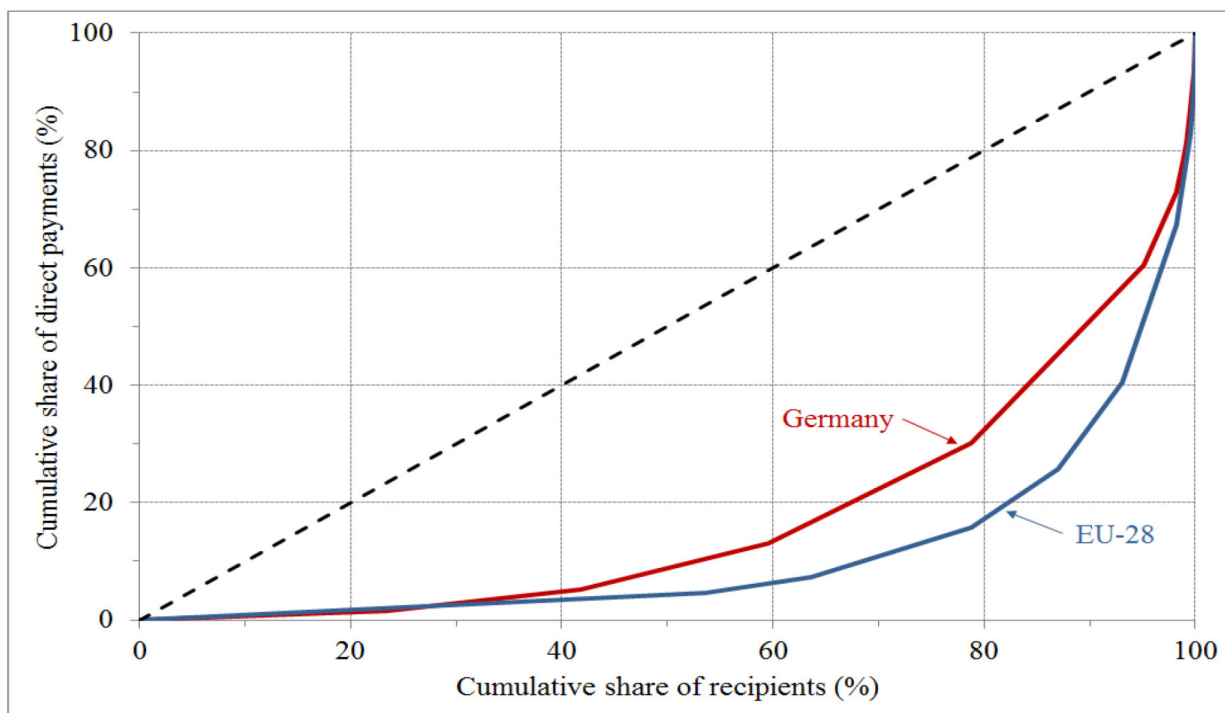
**c) Passing on to input and product prices.** Finally, a small share of direct payments is passed on both to other input prices and product prices (Deppermann et al. 2014).

55. By far the most prevalent passing on effect of direct payments is to land prices. This means that landowners, only some of whom are active farmers, benefit considerably from direct payments. The more land they own, the more they benefit. In order to be able to make statements about which households, depending on the level of the passing on effects, receive 25 % to 50 % of direct payments indirectly, i.e. via land prices, the distribution of ownership of agricultural land in Germany would have to be taken into account. Despite the limited information on this topic plausibility considerations suggest that households who own extensive land are likely to be well-off.

56. While the debate on passing on effects is mainly conducted in expert circles, the broader societal discourse focusses on what is seen as the unfair distribution of direct payments amongst the beneficiaries. As direct payments are granted mainly in proportion to the area farmed (which corresponds to the original logic behind their introduction and the name given to them at the time, i.e. price compensation payments (cf. Weingarten 2017)), the logical consequence is that large-scale farms receive a relatively high share of direct payments. Whereas across Europe 20 % of agricultural enterprises receive around 80 % of direct payments, this distribution in Germany is slightly less “uneven”: 20 % of farmers receive approximately 70 % of the direct payments (cf. Fig. 4).

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However, this is done in an indirect and far from targeted manner. On the other hand, the role of the income impact is scarcely taken into account at all in the societal and political discussion of distribution effects.

**Fig. 4:** Cumulated distribution of direct payments in the EU-28 and Germany (2015)

Source: Cramon-Taubadel (2017: 6) based on EU COM (2016b).

57. Direct payments which explicitly intend to serve the income objective are justifiably criticised in this context for their lack of target orientation and what is deemed to be an unfair distribution. In order to correct this “unfairness”, agricultural associations in regions with small-scale farming or associations that represent the interest of smaller farms frequently articulate the demand for a maximum ceiling per farm or recipient (capping), the degression of direct payments or so-called special support for the first hectares (for instance Verbände-Plattform 2018).

58. The lack of any orientation of direct payments towards personal or farm need cannot be remedied, however, through the further development of the options that already exist today of orienting direct payments towards the size of farms:

- a) Requests for capping or degression of direct payments are often based on the argument that larger farms, because of their economies of scale, do not need any or require fewer direct payments. Such kind of reasoning seems intuitively plausible but it is based on false assumptions. Larger farms are not per se economically better off, particularly if the farm-related and off-farm income of agricultural households are included (cf. Chapter 3). What is particularly critical here is that this argument is based on the implicit assumption that a lack of efficiency would lead to an entitlement to state support. In principle, this argument implies that farmers operating in good locations should receive less support than those in poor ones. Furthermore, the calls for capping and degression ignore the incentive effects they trigger and their consequences, i.e. farm divisions, production adjustments, and distortion on the land market (Sahrbacher et al. 2012). If the lack of efficiency were coupled

with societal services, then the special support could be justified. This, however, is not supported by evidence as outlined below.

- b) The calls for capping or degression of direct payments ignore the fact that there is currently no scientifically backed empirical evidence which links farm size and the provision of societally desired services. Exemplarily, this may be illustrated for the societal goal of providing jobs in rural areas: Contrary to the widespread assumption that as farms increase in size fewer societal services per Euro direct payments are made, there is for instance in the new federal states of Germany, evidence towards a U-shaped relationship between farm size and employment. This stems from the fact that very large farms compared to medium-sized farms are engaged above average in animal husbandry and other activities with high value-added and a high work load. For the societally desired service “provision of jobs” the relationship mentioned above does not, therefore, exist. Analogously, there is no convincing evidence that small farms are generally more environmentally friendly or animal friendly than large ones (Meyer-Hamme et al. 2016, Taube 2016, von Meyer-Höfer 2016, WBA 2015).
- c) Similar to the aforementioned aspects of the supposedly higher need of small (and by extension supposedly inefficient) structures, fairness arguments are advanced on the basis of fairness of needs. The problem with this argumentation is that all too often recipients of direct payments and actual beneficiaries are placed on a par. In fact, a large share of direct payments is passed on to other stakeholders (cf. text number 54f.). Particularly in the case of larger-scale recipients, numerous individuals benefit via co-ownership of farms, wages or securing jobs and lease payments. Furthermore, this fairness discussion also implies a supposed neediness resulting from inefficiency without asking whether the societal services (which could justify state support) could be provided elsewhere in a better and more cost-effective manner.
- d) The additional payments granted in nine Member States for the first hectares (in Germany: the first 46 ha) lead within the Member States, firstly, to redistributions from regions with mainly large-scale farming to regions with mainly small-scale farming. Secondly, they lead particularly in regions with mainly mixed structures in which smaller and medium-sized farms compete locally, to a situation where comparatively unprofitable, mostly smaller farms continue to operate. The resulting stiffer local competition for land leads to restrictions on the development opportunities of adjacent mid-sized farms who manage an area above the “first hectares” (Balmann and Sahrbacher 2014).
- e) A final argument against the attempts to “correct” the distributional effects of direct payments is that this approach reduces political pressure for the necessary fundamental reform. Direct payments with a distribution that is slightly more “fair” may increase societal acceptance for this instrument, but they do not make any targeted contribution to the major challenges that German and European agriculture are facing.

59. The conclusion is that area-based direct payments are completely unsuitable as an income policy instrument. They neither adequately address an individual need as they lack both the information basis and also target setting, nor are they oriented towards the preservation of the societal functions of agriculture. This is not surprising when considering their historical genesis. They were introduced in 1992 as compensation for the reduction in intervention prices. Temporarily, such a compensation may be justified. Today, however, direct payments are an historical artefact. Capping, degression and a focus on the first hectares cannot remedy the lack of targets and lead to unintended side-effects (e.g. divisions of farms). Furthermore, these instruments generate a problematic perpetuation impetus by seeking to increase societal acceptance for scarcely targeted direct payments. Instead, direct payments in this form should be gradually phased out over the next few years or converted into payments which are oriented towards the societal functions of agriculture.

## 2.5 Are direct payments an adequate means of achieving environmental and climate objectives?

60. In the EU around 43 % (just under 180 million ha) of its entire territory is used for agricultural purposes (Eurostat 2017c). Given the considerable external effects caused by agriculture, farming plays an important role when it comes to the preservation of natural resources, the environment and climate (cf. Heißenhuber et al. 2015). The fundamental question of how the provision of public goods can be ensured in these areas is, therefore, a central one and rightly assumes an important position in the CAP reform debate.

61. Whereas agri-environmental support was independently conceived in 1992, a new element was added in 2005 with the mandatory introduction of cross compliance: the linking of direct payments to compliance with basic requirements to be met by farm management (19 EU directives and regulations in the areas of the environment, the health of humans, animals and plants and animal welfare) and the maintenance of farmland in a good agricultural and ecological condition. This principle was developed further in the subsequent reform with the introduction of the greening provisions: since 2015 not only direct payments can be cut back in the event of infringement of cross-compliance conditions, the receipt of 30 % of direct payments is now tied across Europe to three greening conditions: (i) minimum requirements in the field of crop diversification, (ii) rules on maintaining existing permanent grassland, and (iii) the earmarking of 5 % of arable land as so-called ecological focus areas. As of 2017, infringement of these conditions leads to a maximum 125 % reduction of the greening premium (and, thus, to cuts of the basic payment).

62. This system of tying one-size-fits-all area-based payments to environmental objectives has, at first glance, the potential to pursue such objectives on the entire agricultural area – one of the major challenges in agri-environmental support. The following arguments however, oppose this approach:

- a) Cross compliance serves primarily to enhance the enforcement of existing sectoral legislation as cross compliance leads to elevated control requirements and more effective penalty options through the coupling with direct payments. If, however, such an improvement to enforcement is necessary, this clearly means that the existing sectoral legislation has not been afforded sufficient control and penalty options, or there is no desire for effective enforcement. It would therefore make sense to adapt the sectoral legislation and its enforcement correspondingly (cf. for instance Bennett et al. 2006).
- b) Greening – at least in its current form – is largely ineffective when it comes to the environmental benefits it is meant to deliver (Nitsch et al. 2017, Pe’er et al. 2014, 2016, Hart 2015a, ECA 2017a). This has firstly to do with the many exceptions granted and secondly with the unambitious design of the greening provisions. The rules on crop diversification are hardly constraining for the vast majority of farmers, and the agronomic options for meeting ecological focus areas requirements make a comparatively limited contribution to achieving environmental objectives or have already been carried out beforehand. For instance, mixed cropping is no more than good agricultural practice. The same applies to Germany when it comes to the rules on grassland conservation. Since 1991, Germany has lost over 800,000 ha of permanent grassland. As, from an economic and environmental perspective, the remaining areas are mostly absolute grassland locations (climate-relevant peat soils), which cannot be used sustainably as arable land, this grassland should be protected independently of greening through sectoral legislation (regulatory law, e.g. orders, bans).
- c) The current premium level for greening is much higher than the average additional costs incurred through the conditions imposed (cf. de Witte and Latacz-Lohmann 2014, ECA 2017a). This implies over-compensation and major deadweight effects – coupled with only marginal environmental benefits in the current form.
- d) The current greening provisions relate to individual farms. This means that the instrument is not effective in achieving environmental benefits at the landscape level. This would require spatially coordinated conservation efforts such as spatial linking of ecological focus areas across different farm holdings (Sahrbacher et al. 2017).
- e) The expectation frequently associated with greening of introducing environmental protection to all agricultural land is understandable and urgently needed from an environmental perspective.<sup>33</sup> However, it cannot be efficiently achieved with the current

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<sup>33</sup> The measures of the previous agricultural policy were not sufficient in order to reduce the dramatic species decline in agrarian landscapes over the last 30 years. The necessary minimum provision of ecological focus areas of differing quality has already been researched scientifically by Haber (1971, 1998). The work by Tschardt et al. (2005) highlights the importance of structural landscape elements for biodiversity. The group from Göttingen succeeded in impressively demonstrating that a sufficient level of structural landscape elements (hedges, boundary strips) in cleared landscapes is able to raise biodiversity (despite highly intensive conventional farming on arable areas) to a level which would correspond to organic farming in a cleared landscape without these structural elements. Furthermore, more recent studies point to the need for a greater structuring of arable land, e.g. through reduced parcel sizes or a different structuring of refuge areas (cf. Hass et al. 2018, Holzschuh et al. 2010).

system of greening. This is because the principle of uniform EU-wide greening requirements does not sufficiently take into account the spatial heterogeneity of environmental benefits (due to different resource settings or different societal preferences) and compliance costs (above all opportunity costs of reduced land use intensities). Both can vary greatly from region to region and even within the same region. This calls for highly differentiated measures. In a few areas there is a need for payments for preserving agriculture to ensure an open countryside (WBA 2010). In other locations, by contrast, payments are needed to establish ecological focus areas without or with only extensive agricultural production. This means that greening would have to be designed in a manner that is far more regionally differentiated than is the case today if efficient remuneration of environmental services is to be achieved without significant deadweight effects in one region and the inadequate delivery of objectives in the others.

63. In the opinion of the Board greening in its current form is to be understood primarily as an attempt to justify societally the direct payments motivated by income policy (cf. Alons 2017, Erjavec and Erjavec 2015, Daugbjerg and Swinbank 2016). This strategy, and the Board is convinced of this, will not be tenable in the long run given the external pressures on the CAP budget and the major challenges in exactly those areas for which greening is erroneously presented to the public as an effective remedy. In the long-run, the Board sees the risk of losing these budgetary resources which will be needed to tackle environmental, climate and animal welfare related challenges.

64. To conclude, the current greening policy constitutes an ineffective and inefficient use of public funds. Instead of relatively unspecific greening measures that are defined EU-wide and receive 100 % EU-funding, more effective measures should be implemented which are targeted to regional problem settings and have a greater potential to deliver environmental outcomes. In addition, pursuing environmental and climate-related policy objectives with two different funding models and with two different implementation mechanisms (first pillar 100 % EU and second pillar, co-financed and programmed over a multiannual period, cf. Table 1) leads to administrative challenges which would be exacerbated through spatially differentiated greening. In particular, prevention of double support would only be possible if remuneration within the framework of agri-environmental and climate protection measures of the second pillar were to be tailored to the regional specific design of greening.

65. The Board, therefore, supports in principle the approach of the European Commission to jointly programme the measures anchored in the first and in the second pillars within the framework of a new “green architecture” which could encompass both mandatory and voluntary measures (EU COM 2017a: 19).<sup>34</sup> In this kind of approach, conservation measures could be combined that cover several years or just one year. In principle, given the major heterogeneity of agri-environmental challenges as well as the different regional preferences of the population for

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<sup>34</sup> As presented in text no. 36 national programming should perhaps be supplemented or replaced by regional programmes. This flexibility is particularly important for federal Member States like Germany where responsibilities are divided between the German Federal Government and federal states.



environmental goods, it would be desirable to define agri-environmental objectives and devise the appropriate policy measures based upon a bottom-up approach at the Member State level. However, overarching EU objectives like ecological network formation for biodiversity are to be taken into account. It is not yet clear how the interaction between Member States and European Commission with this kind of bottom-up approach could function.

66. Aside from the reflections presented above concerning the integration of measures located in the first and second pillar, agri-environmental and climate protection measures should be developed further. Here, a balance must be struck between the challenges of targeting the measures to specific environmental outcomes, the creation of network structures for biodiversity at the landscape level and the spatial design of focus areas for biodiversity and structural landscape elements on the one hand, and administrative costs on the other. Particularly in light of the greater flexibility that Member States may enjoy in the future design of the CAP it needs to be ensured that the prominent agri-environmental problems in each region are sufficiently addressed.

67. Beyond the agri-environmental and climate protection measures to be programmed at the Member State level, environmental and climate protection objectives of EU-wide importance should be fully designed and financed at the EU level. To this effect, WBAE and WBW (2016) already proposed establishing an EU-wide tendering procedure for peatland conservation as a climate protection measure.

68. Finally, it should be noted that further development of regulatory law in the field of environmental protection and its consistent enforcement are central preconditions for achieving environmental objectives. This is even more the case if cross compliance – as recommended in this report – is discontinued with the phasing out of direct payments. The advantage of regulatory law is that specific bans and requirements, for instance regarding nutrient surpluses or the use of plant protection products, can be implemented nationwide. One major disadvantage of a purely regulatory approach without any complementary measures is that the costs incurred can only be covered to a limited extent by raising the prices of agricultural products because of international market integration. Such costs are thus primarily borne by domestic farmers. Any effects of relocating production abroad or to locations with less strict environmental standards can be problematic, particularly when the environmental impacts concerned have cross-border characteristics (e.g. greenhouse gas emissions). There are limits to the regulatory delivery of environmental objectives both through the relocation mechanism and also through the constraints of social responsibility of ownership.

## 2.6 Should government support farm risk management?

69. Farms are “outdoor workbenches” and have always been confronted with uncertainties and risks. Crop production is highly weather-dependent and must cope with diseases, pest infestation and natural disasters. Animal diseases can threaten livestock farms and the livelihood of companies linked with them along the value chain. Furthermore, high price volatility on the sales and procurement markets can pose a major risk for farms. Finally, given the economic importance

of diverse policy areas for farms (e.g. support policy, environmental policy, animal welfare and trade policy, building law) policy risks should also be mentioned. Under certain circumstances short-term changes within the political framework can mean the end for farms.

70. Dealing with risks is not anything new for agricultural entrepreneurs. They have a wide range of management instruments at their disposal which include risk reduction, risk spreading (diversification) and risk transfer (WBA 2011b, Mußhoff and Hirschauer 2016). Some examples are the choice of species and varieties, chemical and biological plant protection, new farm segments (e.g. biogas, farm shops), off-farm income, reserves, savings and cover by means of future markets and insurances.

71. The EU agricultural policy supplements entrepreneurial risk management with a series of policy measures and instruments. Market organisation instruments (like intervention prices and public storage) aim to ensure a minimum price level.<sup>35</sup> The importance of market intervention has fallen considerably in the EU in recent years. To this end, a financial reserve was set up to offer support in market crises. Furthermore, the options in the Common Agricultural Policy for state support of risk management instruments, particularly to counter production risks, have been extended. Up to 2013 support by means of risk management instruments was located in the first pillar of the CAP. With the most recent agricultural reform the focus of funding of these measures shifted to the second pillar. The EAFRD Regulation (EU Regulation 1305/2013) envisages the subsidising of mutual funds or insurances for adverse climatic events, animal diseases, plant diseases, pest infestation or environmental incidents of up to 65 % of the insurance premiums or compensatory payments. One new option in the above regulation is the possibility to cover up to 65 % of the costs for a general income stabilisation instrument.<sup>36</sup> It would provide compensation from a mutual fund for farmers who have sustained a considerable drop in their income (>30 or 20 %).<sup>37</sup> These support instruments are often supplemented by national measures. In Germany state support for dealing with extreme weather conditions mainly involves a considerably reduced tax rate for multi-peril insurances in agriculture, support for farm (e.g. investment in anti-hail netting) and inter-farm (e.g. flood protection) preventive measures and disaster relief in the form of compensatory payments (Gömann et al. 2015). Furthermore, a resolution was passed to

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<sup>35</sup> These collective stabilisation instruments oriented overall towards the sector do not, however, cater for individual risk preferences and generate high fiscal and national economic costs (WBA 2011b). Furthermore, a state “safety net”, in the form of intervention prices, poses major risks, particularly in the long term. Depending on price and productivity development, intervention thresholds may be too low and lose effectiveness, or too high and prevent in the long term the necessary adjustments and lead to overproduction. Furthermore, minimum prices can also impede reactions in terms of offers that relieve the burden on the market and delay price increases.

<sup>36</sup> As part of their respective rural development programmes, this income stabilisation instrument is programmed in Italy, Hungary and in one region in Spain. However, it has not been implemented in practice there either (cf. also Bardají and Garrido 2016).

<sup>37</sup> Change by the so-called Omnibus Regulation of 16.10.2017: “Simpler risk management instruments to support farmers, including a sector-specific income-stabilising instrument and improved insurance arrangements by means of which farmers whose production or income is at least 20% lower, can obtain compensation of up to 70%” ([https://ec.europa.eu/germany/news/eu-agrarpolitik-wird-weiter-vereinfacht\\_de](https://ec.europa.eu/germany/news/eu-agrarpolitik-wird-weiter-vereinfacht_de)).

introduce a sector-specific special scheme to smooth taxable agricultural income over several years.<sup>38</sup>

72. Based on the expectation that the enhanced market orientation of the CAP leads to greater producer price volatility and climate change leads to more frequent and more extreme climatic events, discussions about the risks in agriculture and the resulting potential income risks both at the national and on the EU levels have increased markedly. The occurrence of individual concrete crisis events like the large-scale crop damage as a consequence of the 2013 flood, the pronounced drop in milk prices 2015/2016 or the extreme frost damage in fruit cultivation in the spring of 2017 have ramped up interest in new solutions for risk management in agriculture and increased the demands for greater state intervention. In its Communication on the CAP post 2020 the European Commission also explicitly stressed the need for improved risk management in agriculture (EU COM 2017a).

73. As the results of Kahneman (2011) clearly show, subjective risk perception is frequently distorted and can deviate considerably from actual risk exposure. This phenomenon can be observed partly in Germany when discussing the development of agricultural risks as well. Analyses of farm accountancy data show that, over the last 20 years, the increase in yield and price variability has not led on the same scale to an increase in income variability (Duden and Offermann 2017). A general increase in income volatility has not been observed; depending on the production focus, volatility in total agricultural income has increased or fallen. Also the risk of bankruptcy is far lower than in other sectors (e.g. manufacturing industry, construction industry or commerce) because of the high value of land in the farming sector.

74. Furthermore, increased or different risks do not provide any mandatory justification for state action. The Advisory Board voiced a comprehensive report most recently in 2011 (WBA 2011b) on the role of the state in risk and crisis management. The Board is convinced that dealing with price and yield risks is, above all, an entrepreneurial task. State action should be limited to correcting problems caused by market failure. Nothing has changed from today's perspective in this fundamental estimation. For agriculture in Germany only in a few cases valid arguments can be advanced for the occurrence of market failures which justify (temporary) state intervention:

- a) Catastrophic events with systemic damage:** It is generally accepted that the state has special obligations when it comes to "catastrophic" events. These are events that occur relatively rarely, are not foreseeable but lead to a high level of damage which often threatens the livelihood of many of those affected. As the damage frequently occurs in a concentrated spatial area, catastrophic events bear the risk that the economic and social structure of a region could be permanently impaired. Often it is not possible to insure these risks. The emergency aid ("ad hoc assistance") granted in the case of a disaster aims to ensure the survival of farms (liquidity, profitability) and to relieve the acute income situation (consumption options) of those affected. The meaningful design of emergency aid

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<sup>38</sup> Cf. BGBl. I 2016 (No. 63), p. 3045. It has not yet entered into force as the European Commission is still examining this (status: 25.01.2018).

faces the challenge of differentiating in a workable manner between catastrophic non-insurable events (with the corresponding justification for state action) and “insurable” events. Furthermore, there is a risk that the prospect of ad hoc assistance could undermine active risk management by the farms themselves and hinder the emergence of insurance-based solutions.

In the EU the principles of state aid for natural disasters and comparable adverse climatic events conditions are laid down in the “European Union Guidelines for State Aid in the agricultural and forestry sectors and in rural areas 2014 to 2020”. These EU Guidelines aim to prevent distortion of competition and impairment of trade. In Germany these requirements are set out in a national framework regulation which aims to facilitate prompt aid in acute cases of damage. For instance the large-scale floods in 2013 triggered a comprehensive aid package. In this package EUR 237 million were channelled into rural infrastructure, agriculture and forestry, of which EUR 156 million were used to compensate for damages to crops (Gömann et al. 2015). Criticism was voiced about the delay in the paying out of assistance, the differing procedures of the federal states for calculating the level of compensation and the handling of hardship cases (Landesrechnungshof Brandenburg 2016, Sächsischer Rechnungshof 2016).

In the so-called crisis reserve EUR 400 million are available annually for market crises in order to facilitate a flexible and prompt response to crises on the agricultural markets. The fact that these funds have not yet been used has nothing to do with the non-occurrence of market crises but rather with a fundamental construction error in funding: if the crisis reserve is not used up, the funds are “reimbursed” to the farmers as direct payments. The self-interest of Member States who are not at all or only affected to a limited degree by a crisis clearly lead to a situation where the financial advantage of paying out direct payments in one year is weighted more highly than the concept of solidarity and the possibility of benefiting at some other time themselves from the crisis reserve. This disincentive has rendered this instrument ineffective.

**b) Animal diseases, plant diseases and plant pests:** In many cases prophylactic measures or the acute, rigorous control of animal diseases, certain plant diseases and pests may make sense in the overall economy in order to ward off high levels of damage that often go beyond the agricultural sector. From the angle of the individual farm the ratio of the costs incurred (e.g. through preventive culling of non-diseased but potentially infected animals) to the potential benefits is frequently less favourable than from the overall economic angle. In these cases, damage prevention always means positive external effects. This is where the state is called on to put in place suitable framework conditions (e.g. hygiene requirements for disease control, compulsory insurance) in order to promote from the societal angle the optimum implementation of prophylactic control measures. This normally also includes compensation for farms who are negatively affected by disease measures (e.g. culling of affected animals or destruction of plant stocks, marketing bans for adjacent farms). This need not necessarily mean a financial contribution from the state, but financial

compensations do increase acceptance amongst the farms that carry out the measures and is widespread in the field of animal diseases in the EU.

For instance in Germany there is a liability to pay contributions to the animal disease fund (Tierseuchenkasse) for most livestock. The animal disease fund is an institution under public law but is run along similar lines to an insurance company. According to its provisions, financial compensation for animal losses is covered to 50 % by the animal disease fund and drawn from the contributions of livestock keepers. The other half is borne by the respective federal state. In special cases the EU also contributes to the costs incurred.<sup>39</sup> Next to indemnity payments covered by the Animal Disease Act (Tierseuchengesetz) the animal disease fund compensates further costs (e.g. collection of samples, vaccinations) which are solely financed from livestock keeper contributions.<sup>40</sup> Damage arising from marketing bans and costs that go beyond the pure animal value (e.g. income losses as a consequence of production downtimes) are not refunded by the animal disease funds but can be insured in Germany through established consequential loss insurance.<sup>41</sup>

**c) Systemic yield risks in conjunction with genuine uncertainty:** The emergence of a market solution to insure risks can fail in the case of systemic risks<sup>42</sup> linked to the existence of so-called “genuine uncertainties”, i.e. where the probability of occurrence is unknown. Market failure of this kind has been acknowledged by the WBA (2011b) for Germany only in the case of drought and flooding risks. In this context, Gömann et al. (2015) in their study on the relevance of extreme climatic conditions for agriculture concluded that currently available information on the (future) importance of income losses caused by drought with regard to the income stability and liquidity of farms in Germany does not warrant increased state engagement for the spread of insurance solutions. Given the dynamics of climate change there is a need for further research here.

**d) Competition distortions as a consequence of political intervention in other countries:** Distortions of competition can arise as a consequence of interventions on insurance markets in other countries. A number of EU Member States promote insurance systems with national funds or make increasing use, since the last support period, of the options of financial support of risk management instruments within the framework of the EAFRD rural development programmes. The USA has almost completely switched its direct support for the agricultural sector to the promotion of risk-related instruments. Besides the classic,

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<sup>39</sup> The contributions are staggered depending on the animal species. The contribution level in Lower Saxony in 2016 was EUR 7 per cow and EUR 0.75 per pig. The overall contribution sum was approximately EUR 35 million. The federal state Lower Saxony refunded just under EUR 8 million, the EU 1.5 million of expenditure.

<sup>40</sup> See the homepage of the Lower Saxony animal disease fund: <https://www.ndstsk.de/index.php?bereich=6>.

<sup>41</sup> The contribution revenue for consequential loss insurance amounted to EUR 147 million in 2015 (GDV 2016).

<sup>42</sup> In the case of systemic risks many companies are affected at the same time by the damage event which means that the maintenance of an entire system may be in jeopardy. Drought and flood damage, for example, are frequently systemic at least in regional terms. In contrast, risks of a specific nature only affect individual farms (for instance hail).

damage-related plant crop insurance a number of different programmes for index-based insurance of yields, prices or returns in plant production and margins (performance not including feed costs) in dairy production enjoy state support. Under these measures around 90% of agricultural area and more than 60% of milk production are insured.<sup>43, 44</sup>

Consequently, the question about competition distortions is taking on increasing importance. However, it is still not possible to give a general answer to the question whether higher subsidies for insurance premiums in other countries will lead to competitive disadvantages for German agriculture. The effects on the competition situation of German agriculture depend firstly on the level of subsidies of insurance premiums and the related effects on aggregate production and secondly on whether state support influences crop structure in the respective countries (e.g. because the promotion of high-risk crops is preferable or because the subsidy rates differ from product to product). Furthermore, attention should focus on whether this leads to a situation in which products that compete with conventional crops in Germany are promoted or perhaps even at a disadvantage. The insurances subsidised in other EU Member States normally cover various arable and special crops and do not usually present any product-specific differences when it comes to subsidy rates. The wider spread of support for weather insurance in the southern EU Member States prompts the assumption that, in some cases, products are supported which are not in direct competition with the crops typically grown in Germany. However, no quantitative assessment is available.

75. The discussions about the need for action and opportunities for dealing with uncertainties in agriculture are not dying down despite significantly extended state and private sector instruments. A series of proposals aims to increase the distribution of existing CAP instruments, to redistribute direct payments in order to fund these risk management instruments or to place them on a more anticyclic basis, i.e. higher direct payments for low agricultural prices and vice versa. However, these proposals do not normally establish any explicit link to a market failure which would justify corresponding state action. The Communication of the European Commission on the CAP post 2020 also expressly touches on the need for improved risk management in agriculture. Here the Commission points to the existing CAP instruments by means of which farmers are (can be) supported in preventing and managing risks, and suggests first of all examining how the design of these instruments can be adapted in order to increase their functionality. The Commission sees deficits above all in the understanding and acceptance of risk management instruments by the farmers. It recommends *inter alia* increasing knowledge about the benefit of these systems through initiatives on knowledge transfer and incorporation into agricultural advisory services.

76. The WBAE also sees a need to improve the information situation on risk exposure and the knowledge of the stakeholders along the overall value chain particularly with a view to new or newer risk management instruments (index-based insurance, futures, commodity futures market

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<sup>43</sup> <https://www.ers.usda.gov/topics/farm-practices-management/risk-management/government-programs-risk.aspx>.

<sup>44</sup> <https://www.fsa.usda.gov/programs-and-services/Dairy-MPP/index>.

milk). The objective here is to improve the individual farm opportunities for the optimum design of risk management and, in this way, help farms adjust to changing economic and agricultural framework conditions.

77. The WBAE sees a particular need for greater assessment of the consequences of changing framework conditions for risk management in agriculture from a longer term strategic perspective in order to promote instead of prevent the necessary adjustments. The subsidising of insurance premiums or other risk management instruments does not make any sense particularly if, because of climate change, there is an increased incidence of extreme climatic events which, in turn, lead to such high (risk) costs that certain production systems or crops are no longer adjusted to the location conditions in Germany or Europe (i.e. no longer competitive). Using subsidies to ward off these developments is unlikely to be successful. Furthermore, there is in principle a major risk of crowding-out on-farm adjustment measures to climate change and private sector risk management instruments outside the farm and promoting potentially undesirable high-risk crop systems.

78. In summary, the Board sees risk management first and foremost as an entrepreneurial task. The role of the government should be to create framework conditions which offer the individual entrepreneur a broad, if possible, spectrum of private risk management instruments. Support measures should, therefore, be oriented particularly towards strengthening market forces by means of information support, the creation of transparency and the provision of infrastructure. State action should be limited to correcting problems caused by market failure. It should be low key and limited in time so as not to jeopardise the emergence of private sector solutions. Particularly when it comes to foreseeable fundamental changes in framework conditions, state activities in terms of risk management should be assessed from a long-term strategic perspective in order to promote the necessary adjustments instead of preventing them.

## **2.7 What importance should the development of rural areas beyond the agricultural sector assume within the CAP?**

79. In the objectives for the Common Agricultural Policy set out in EU legislation no mention is made of rural development in Article 39 of the TFEU (cf. text no. 18). Nonetheless according to Article 174 of the TFEU the EU seeks to strengthen “its economic, social and territorial cohesion” and here “particular attention shall be paid to rural areas”.

80. In the CAP regulations which are relevant for 2014-2020, Article 110(2) Regulation 1306/2013 mentions “balanced territorial development, with a focus on rural employment, growth and poverty in rural areas” as one of three objectives against which the performance of direct payments and of the second pillar shall be measured (cf. text no. 20). In Article 4 Regulation 1305/2013 on support for rural development by the EAFRD the following objectives are listed:

- a) “fostering the competitiveness of agriculture;
- b) ensuring the sustainable management of natural resources, and climate action;

c) achieving a balanced territorial development of rural economies and communities including the creation and maintenance of employment”.

81. The EAFRD Regulation also contains six priorities, one of which (Priority 6)<sup>45</sup> addresses rural development from a more comprehensive angle whereas the other priorities are very much oriented towards agriculture (competitiveness, environmental impact) (Table 3). There are no minimum budgetary appropriations for the individual priorities.<sup>46</sup> In the EU the Member States have planned to earmark on average 16 % of EAFRD funds in their rural development programmes for Priority 6. In Germany the share is 26 %.

**Table 3:** Priorities of EAFRD support 2014–2020 and planned allocation of EAFRD funds in the EU-28 and in Germany (as %)

EAFRD priority	Share of all EAFRD funds	
	EU-28	Germany
1. Fostering knowledge transfer and innovation	Horizontal task	
2. Enhancing competitiveness of agricultural enterprises	20	13
3. Promoting food chain organisation and risk management in agriculture	10	5
4. Restoring, preserving and enhancing of agricultural and forestry eco-systems	44	49
5. Promoting resource efficiency and supporting the shift towards a low-carbon and climate resilient economy	8	5
6. Promoting social inclusion, poverty reduction and economic development in rural areas	16	26
/ Technical assistance	3	2

Source: European Commission (EU COM 2018).

82. The “policy for the development of rural areas” (currently second pillar of the CAP) encompasses a broad spectrum of priorities and measures. It can be described as a “hybrid of agricultural, environmental and regional policy” (Weingarten et al. 2015: 25). Which position the development of rural areas beyond the agricultural sector should adopt in here is first and foremost a political and not a scientific question. It depends very much on whether the second

<sup>45</sup> The following areas are indicated as the main ones for Priority 6: “a) facilitating diversification, creation and development of small enterprises, as well as job creation; b) fostering local development in rural areas; c) enhancing the accessibility, use and quality of information and communication technologies (ICT) in rural areas.” (Article 5, Regulation 1305/2013).

<sup>46</sup> For the measures there is the stipulation that at least 30 % of the EAFRD funds must be used in the sum for payments for agri-environmental-climate measures and organic farming, payments to farmers in disadvantaged areas, payments for forestry measures, payments within the framework of Natura 2000 and the promotion of climate- and environmentally-relevant investments. Furthermore, at least 5 % of the funds must be used for LEADER.



pillar of the CAP is understood primarily as part of the Common Agricultural Policy or is deemed to be a policy for the development of rural areas (Weingarten 2011: 183).<sup>47</sup>

83. The Directorate-General for Agriculture and Rural Development stressed in 2011 the complementarity of the two pillars: “the two pillars work together in a complementary way towards the CAP objectives, with rural development responding to needs for structural adjustment generated by reforms in the first pillar. (...) Thus, the structural measures offered in the 2<sup>nd</sup> pillar complement the more general income support in the 1<sup>st</sup> pillar and open alternative employment opportunities in rural areas, while more targeted environmental measures in the 2<sup>nd</sup> pillar allow farmers to go beyond the compulsory requirements in the 1<sup>st</sup> pillar” (DG Agriculture and Rural Development 2011: 3).

84. In line with the CAP objective of balanced territorial development, the second pillar should, however, react to the need for structural adjustments in rural areas irrespective of whether this adjustment need resulted from the reforms of the first pillar or other reasons. A rural development policy geared to the objective of balanced territorial development should be oriented in a territorial and problem-driven and not in a sectoral manner (to agriculture and forestry) (OECD 2007, WBA 2010).<sup>48</sup> In this respect it should reflect the diversity of rural areas.

85. If one looks at the Commission Communication from November 2017, then this reveals a slightly modified formulation of the objective compared to today's agricultural policy. In its Communication the Commission names as one of the three most important objectives “to strengthening of the socio-economic fabric of rural areas” (EU COM 2017a: 11). This could be understood as an upvaluation of rural areas. Up to now the objective was “balanced territorial development”; in future rural areas in general are to be strengthened. What is noticeable in the Communication is that the objective of strengthening the socio-economic fabric of rural areas is addressed primarily from the angle of agriculture, namely via the two sub-chapters “Growth and jobs in rural areas” and “Attracting new farmers”. Even the first sub-chapter, with its focus on the bio-economy, has a strong link to agriculture. Furthermore, establishing “smart villages” and the LEADER approach are mentioned (EU COM 2017a: 20f.).

86. According to the Commission Communication “through its rural development policy, the CAP is the ‘rural champion’ of the Union” (EU COM 2017a: 22). If the Commission has this high expectation of the CAP, then it is somewhat contradictory that, at the same time, a stronger

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<sup>47</sup> The formulation “beyond the agricultural sector” subsumes those measures which are of relevance for rural areas, but have no link to agriculture or agriculture-related value chains. This includes particularly support in line with Article 20 of the EAFRD Regulation which focuses in Germany primarily on village renewal and development, infrastructure for rural tourism, basic public services and broadband infrastructure (Tietz and Grajewski 2016) and LEADER support (Articles 42-44 of the EAFRD Regulation).

<sup>48</sup> On average 4.9 % of all gainfully employed people worked in agriculture, forestry and fisheries in the EU-28 (Germany: 1.5 %). The share in total gross value added was 1.6 % in the EU-28 (Germany: 0.5 %). The large spread of both indicators at the NUTS-3 level is highlighted in the maps presented in Figure 1.

agricultural sector orientation of the CAP can be concluded from the Commission's Communication.

87. There is a wide spectrum of spatial policy measures of relevance for the development of rural areas. On the EU level this is manifested particularly clearly in the range of measures of the EAFRD, the European Fund for Regional Development (EFRD), the European Social Fund (ESF) and the Cohesion Fund. For Germany the action areas at federal government level which are listed in the "Report of the German Federal Government on the development of rural areas 2016" (BMEL 2016)<sup>49</sup> illustrate the spectrum of spatial policy measures. The measures in the second pillar of the CAP which extend beyond the agricultural sector can, therefore, only make a small contribution to the development of rural areas and are to be viewed in interaction with other spatial policy measures.

88. The importance which the development of rural areas beyond the agricultural sector should adopt within the CAP cannot be answered separately from the question about the distribution of competences between the EU and Member States. Here, as set out in Chapter 2.2, it would be necessary to examine (i) whether the addressed objectives are of supra-regional importance, (ii) the extent to which these objectives can be delivered more readily at the European or global level than at the national level and, where appropriate, financed by the Community and (iii) whether the degree of economic development and, thus, the economic strength of regions are given adequate consideration. Furthermore, it should be examined whether this development should be attributed to the CAP or whether it would make more sense to attribute this to a different policy area.

89. The objective of balanced territorial development is of supra-regional importance. However, the Board does not generally agree with the view that this objective could be delivered more readily at the European rather than at the national level by means of the measures listed in the EAFRD Regulation and should, therefore, be financed by the Community. Moreover, it is not generally true, that the economic level of development in the regions can be adequately reflected in Europe-wide measures.

90. To the Board it is of crucial importance that a rural development policy, which does justice to its name, has a territorial and problem-oriented focus and does not concentrate on a specific sector. Furthermore, it should reflect the diversity of rural areas in the EU. Whether responsibility (and the budgetary resources) for measures in the current second pillar that go beyond the agricultural sector should continue to be an area of the CAP or should be assigned, for instance, to regional policy is in the opinion of the Board a secondary question. If, however, the second pillar is to be called, in the future too, the "policy for the development of rural areas", it should contain support measures that go beyond the agricultural sector. Otherwise the name would constitute a bogus claim. What seems to advocate assignment to the CAP is that vibrant rural areas with non-agricultural employment opportunities help to facilitate or cushion structural change in agriculture

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<sup>49</sup> These are the action areas „housing, infrastructure and services of general interest“, „regional economy and employment“, and „land use, natural resources and recreation“.

and that agriculture, a largely immobile sector, is dependent on sufficient infrastructure and living conditions on site which are attractive for workers. One argument against assignment to the CAP is the purely quantitative dwindling importance of agriculture for gross value added in rural areas that has been apparent for decades and will continue in the future. There must also be critical examination of whether assignment to the CAP means that a genuine “overcoming” of the focus on the agricultural sector is possible or likely.

91. What is important in any case is that the different spatial support policies for rural areas are sufficiently coordinated. This applies both to the substantive coordination of the support areas and also to technical implementation. With the joint strategic framework (cf. Regulation 1303/2013) which applies to the EAFRD, the EFRD, the ESF, the Cohesion Fund and the European Maritime and Fisheries Fund (EMFF), closer coordination was already introduced for the ongoing support period. But this is in need of improvement (cf. Chapter 4.8).

92. Rural areas in the EU and also in Germany are diverse. They differ markedly with respect to economic, social, demographic and natural conditions. Hence it is important for Member States to have extensive freedom to set their own priorities in terms of their preferences as well as needs and opportunities for action. This also applies to the differences in terms of the status of the development of rural areas beyond the agricultural sector (even if this can only be established in a limited manner from the priority setting in the programmes on rural development because of the different other opportunities for action). The relocation of measures that go beyond the agricultural sector from the EADRF fund to another fund would, in principle, reduce the flexibility of the Member States to set their own priorities within the current second pillar of the CAP.

93. Hence it can be concluded: a policy to develop rural areas, which does justice to its name, should have a territorial and problem orientation and should not target a specific sector. Furthermore, it should reflect the diversity of rural areas in the EU, which would mean that competences would be located more than in the past on the Member State level. This report cannot engage in comprehensive discussion of whether the competence (and the budgetary resources) for support measures of the current second pillar which go beyond the agricultural sector should remain within the CAP or should be assigned for instance to regional policy. If – as suggested by the European Commission – cross-sectoral rural development should continue to be a priority of the CAP, then the CAP should however still contain support measures that go beyond the agricultural sector. An argument in favour of assignment to the CAP is that vibrant rural areas with non-agricultural employment opportunities help to facilitate structural change in agriculture and that agriculture, for the most part an immobile sector, is dependent on the existence of sufficient infrastructure and living conditions on site which are attractive for workers. Furthermore, a shift to a different policy area would reduce the possibilities for Member States to set their own priorities in the second pillar of the CAP. An argument to back reassignment is that this policy area would then be viewed by policy-makers less from the agricultural sector perspective. The fact that the shift to another policy area would also generate costs (restructuring costs, learning costs) is another argument for leaving the policy for the development of the rural areas at the European level as part of the CAP. In this case it should be implemented with less emphasis on agriculture than in the past. Aside from the assignment question it can be said that rural development is a

horizontal topic and there are many spatial support policies of relevance for rural development. In future they should be better coordinated.

## 2.8 Should the CAP in the long term be further developed into a Common Agricultural and Food policy?

94. In the current debate on the future design of the CAP various stakeholders have explicitly called for an integrated, sustainable “Common Food Policy” or a “Common Agricultural and Food Policy” (cf. Bailey et al. 2016, Fresco and Poppe 2016, The Netherlands Presidency 2016, Falkenberg 2016, IPES 2016a, b, The Netherlands Scientific Council for Government Policy 2016). This demand is based on the view of a food system that “gathers all the elements (environment, people, inputs, processes, infrastructures, institutions, etc.) and activities that relate to the production, processing, distribution, preparation and consumption of food, and the outputs of these activities, including socio-economic and environmental outcomes” (HLPE 2014: 29). Hence, such a perspective encompasses all value chains for food and sees a major share of agriculture as part of the food system.

95. In line with this systemic perspective, food policy has a very broad definition. It encompasses all policy areas that impact what is eaten by whom, when and where and includes in its definition agricultural policy as well as all policy areas that address the value chains (Lang et al. 2009). Based on the historically established set of food policy measures three areas can be differentiated: food security, food safety and consumer-oriented food policy. Consumer-oriented food policy has increasingly grown in importance at the Member State level over the last decades and encompasses measures targeting consumers involving nutrition information, advice and education, nudging<sup>50</sup>, fiscal governance, orders and bans (cf. Barlösius 2016: 250ff.).

96. Integrated policy design in line with the aforementioned broadly formulated definition of food policy is not currently being practiced on the EU level. Here, food policy is largely seen as health policy and is, therefore, located within the Directorate-General for Health and Food Security (DG SANTE).<sup>51</sup> According to Article 6 in conjunction with Article 2 (5) TFEU the competence of the European Union is restricted to the protection and improvement of health and basically to supporting, coordinating or supplementing measures of the Member States (Kingreen 2016:

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<sup>50</sup> The term “nudge” (“Stups“, Thaler and Sunstein 2008, Marteau et al. 2011) or more recently “tippme” (Hollands et al. 2017) describes environmental conditions which do change but do not hamper the choice architecture. The idea is that a nudge helps to more easily show the desired behaviour if the structuring of the situation presents the desired behaviour as a default (cf. also Renner 2015). In the food sector the nudging approach can, for example, be applied by the desired option being the default or being made more readily available. Various studies show that the design of the environment such as for instance the presentation of food can change behaviour (cf. Hollands et al. 2013, Marteau et al. 2011, Campbell-Arvai et al. 2012, Gravert and Kurz 2017).

<sup>51</sup> The central reference point for the area of nutrition and health is the “European Action Plan Food and Nutrition 2015–2020 of the World Health Organisation (WHO 2014).

margin number 4). Beyond the issues of food security and labelling<sup>52</sup> which are dealt with by the European legislature, health-oriented food policy, which seeks amongst other things to change consumer habits, is therefore explicitly incumbent on the Member States.

97. Health policy objectives are scarcely pursued within the framework of the current CAP. The European Commission does state in its Communication “The Future of Food and Farming” that the CAP “has a role to play in promoting healthier nutrition, helping to reduce the problem of obesity and malnutrition, making nutritious valuable products such as fruits and vegetables easily available for EU citizens” (EU COM 2017a: 24). Apart from the much quoted school programme (fruit, vegetables, dairy products) there are, however, scarcely any further instruments explicitly targeting health policy objectives.<sup>53</sup>

98. This is not least because the CAP has, since its introduction, primarily targeted the agricultural sector. Whereas in the first two decades the focus was on securing the supply situation, the official spectrum of objectives has since been successively extended (cf. Chapter 2.1). While environmental and climate policy objectives are now established action areas of the CAP, the call to equally address nutritional and the related health policy targets opens up the discussion about the inclusion of new objectives in the CAP.

99. Two central reasons are usually given for greater policy integration of the CAP along these lines.

**a) Impact of agricultural policy on a healthy diet.** Against the backdrop of an alarming increase in food-related diseases (cf. Chapter 2.1, text number 20d), the European Public Health Association (EUPHA 2017) and the European Public Health Alliance (EPHA 2016) explicitly call for public health to be taken up into the catalogue of objectives of the CAP and to focus the CAP more on supporting sustainable eating habits. Agricultural policy interventions within the framework of the CAP, this is the argument advanced by these and other stakeholders, influence the availability (volume) and affordability (prices) of food products in terms of level and volatility and, thus, consumer decisions in the area of food. However, opinions differ as to how strong this link actually is. It is difficult to quantify and only a few scientific studies are available (cf. Hawkesworth et al. 2010, Hawkes et al. 2012, EPHA 2016). One example of a fundamental link is the deregulation of the EU sugar market (agricultural policy) which led to a fall in the price of sugar and, more particularly, isoglucose syrup. Given the small but negative own price elasticities of demand, such price reductions lead to increased consumption of sugar and isoglucose syrup. This also holds for food consuming industries, which alter their formulas, whereby processing companies often

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<sup>52</sup> Cf. for instance the fully harmonised legislation since 2006 in Europe for food hygiene and harmonisation of the main principles of food production (for instance EU Regulation 834/2007 – Eco-Regulation) and food labelling (for instance EU Regulation 1169/2011 – Food information Regulation).

<sup>53</sup> For the legal foundations and the design of the EU school programme, i.e. of the “Union aid for the supply of fruit and vegetables, bananas and milk in educational establishments” (cf. Commission Delegated Regulation (EU) 2017/40 of 3 November 2016 in Germany please refer also to the BMEL website: [https://www.bmel.de/DE/Ernaehrung/GesundeErnaehrung/KitaSchule/\\_Texte/Schulobst.html](https://www.bmel.de/DE/Ernaehrung/GesundeErnaehrung/KitaSchule/_Texte/Schulobst.html)).

react more sensitively to changing price relations than consumers. If elevated consumption goes hand-in-hand with negative health effects, then it makes sense to include such a change in consumption in an overall consideration of well-being and, where appropriate, to implement suitable complementary measures. Another example is the relatively high customs protection today of between about 25 % and 60 % for meat in the EU (WBA 2015: 246). If this were to be dismantled, then this would lead, as a consequence of the falling prices, particularly for beef, to an increase in meat consumption which is not wanted in terms of climate policy. It would, therefore, make sense in such a case to consider complementary measures on the demand side.

Direct price policy interventions within the CAP have, however, become less important in recent decades. Nonetheless, subsidies for agricultural products on the supply and demand side and input subsidies can likewise have a distorting effect on price relations. At the present time, the main instrument used in the EU are direct payments decoupled from production but tied to agricultural land. However, their potential for distorting price relations is limited. It is indeed true that land-intensive crops such as cereals or oilseed benefit more from these payments than less land-intensive crops like fruit and vegetables. However, the price impact in the case of cereals and oilseeds is low because of international market integration (Deppermann et al. 2014). Furthermore, available analyses show that from the nutrition angle within the EU it is less about whether the agricultural products manufactured by agriculture are “healthy” or “unhealthy” than about how they are transformed, substituted and marketed along the value chain (i.e. by the food processing industry (Hawkes et al. 2012).

Lastly, there is extensive discussion particularly in the international literature about the effects of agricultural research policy on the relative prices of food and the related impact on nutrition. International agricultural research has focused above all on productivity increases for those crops which supply staples that are rich in starch (rice, wheat and maize) whereas crops important for supplying micronutrients (fruit and vegetables) have been somewhat neglected (Pingali 2015). As a consequence, prices of staples are relatively lower than prices of vegetables and fruit. This has contributed particularly in poorer households to food habits shaped by a high energy density but low food diversity and consequently deficits in micro-nutrient supply (Gómez et al. 2013: 132). For industrial countries like Germany examination should be undertaken of the extent to which there is a similar link particularly as, here too, public and private agricultural research very much concentrates on the main crop species. From the nutritional perspective there are calls around the world for a greater focus of agricultural research on fruit, vegetables and pulses in order to make these products available at lower prices through productivity gains and improvements in the value chain (cf. for instance Jones and Ejeta 2016: 228).

**b) Effects of consumer-oriented food policy on agricultural production.** The clear reduction in the consumption of animal products (consumer-oriented food policy) also called for by the Board for climate protection reasons (WBAE and WBW 2016) affects the meat and dairy industry which are the two largest sectors in the EU agribusiness. This would have a major

impact on agriculture and rural areas and such impacts should be taken into account when weighing up the corresponding food policy measures.

The climate protection recommendation to reduce the consumption of animal products, makes sense partly also for health reasons. Moreover, it is an example of how it can be expedient to start with consumption (in this case eating habits) instead of directly focusing on the supply side (in this case animal husbandry). If the demand for animal products were not to change, a regulation on the supply side would lead to relocation effects given international market integration. Germany or the EU would import more animal products and the related greenhouse gas emissions would occur in other countries. As this would not rule out failure to meet the objective for a global environmental good like climate, the Boards, therefore, suggest tackling this from the food habit angle. This example demonstrates not only the growing relevance of governance measures on the demand side. It also illustrates that interventions of this kind could have major effects on agriculture, which may, in turn, trigger a need for action in the CAP.

100. The demand for an integrated policy for agriculture and food makes initial sense given the existing interactions: much of what is produced in agriculture serves human nutrition – and most of what is eaten comes from agriculture. Changes in agricultural production, therefore, have an impact on the food on offer and, by extension, on nutrition and human health. Changes in eating habits too (also where politically induced) have medium to long-term effects on agricultural production decisions and, by extension, on the food on offer.

101. This link between agricultural production and nutrition is, however, only clear on the global aggregate level. It varies on the level of nation states and takes a back seat in the largely integrated national economies of the EU as a consequence of the import and export of food. Products can be consumed which are not produced in the respective region or country but are imported and foods can be produced which are not consumed in the respective region or country but exported. Against this backdrop it is hardly surprising that the debate about nutrition-sensitive agriculture<sup>54</sup> is conducted initially foremost in the development policy context: the lower the level of market integration (infrastructure, political market integration, geographical situation), the higher the volume of regionally manufactured products that shape the food options. The relevance of nutrition-sensitive agriculture is then obvious. In recent years there have been increasing calls for industrial countries too, including the EU, to give greater consideration to nutritional aspects in agricultural policy (cf. for instance Walls et al. 2016). This is based on the perspective of the food system defined above and on diverse complex interactions within the system that can lead in modern food systems too, particularly for disadvantaged groups, to negative effects in terms of nutrition (HLPE 2017: 109).

102. Whether and, if so, the extent to which the CAP should be developed further into an integrated agri-food policy, is a complex question which cannot be comprehensively discussed or

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<sup>54</sup> See Sibhatu and Qaim (2017) as well as Global Panel on Agriculture and Food Systems for Nutrition (2016).

definitively answered in this report. Here the Board refers to its report on sustainable nutrition to be published in 2019. In the opinion of the Board the following considerations are currently to be taken into account:

- Individual food decisions are based on and influenced by multiple factors. The potential of the current CAP as an instrument to guide food consumption is deemed to be limited against this backdrop. If the objective were to be to extend the CAP into such a governance instrument, then not only agricultural producers but also above all the downstream areas of the value chain would have to be involved.
- An anchoring of food policy in the CAP would have to take into account the division of competences within the primary law of the TFEU. The CAP provisions only contain an explicit link to food policy with a view to securing supply mentioned in Article 39 TFEU. Up to now, this objective has only been interpreted from the quantitative angle. An interpretation which brings in quality standards for supply, has not had any foundation in legal practice up to now (Martínez 2016b: margin number 12). Furthermore, the EU does not currently have any legal competence for an independent, comprehensive food policy. A link between the CAP and food policy could, however, result from the horizontal clause on public health which is regulated in Article 168 (1) first sentence TFEU. This horizontal clause does not itself establish any competence but merely contains provisions about how the existing competences are to be exercised. So if there is political scope for action, this must be used to the extent possible as “conducive to health” (Kingreen 2016: margin number 9). The extent to which this horizontal clause opens up the exercise of competences in favour of independent policy perception by the Union depends on the political will of the Member States (Walls et al. 2016: 22). Within the framework of a general consensus of the Member States, a European food policy could indeed be formulated on this basis. However, it has still to be elucidated whether this would make sense in line with the subsidiarity principle.
- Irrespective of the concrete institutional design, it is expedient because of the aforementioned interactions to increase the coordination of policies on the production and consumption side if interactions are to be expected. Agriculture and the food industry in the EU are very well integrated into the national and international markets and – as outlined above – the food processing industry in particular is responsible for the quality of the foods on offer. This would be an argument in favour of using mainly nutritional measures for the objectives that primarily concern human nutrition (e.g. health) and agricultural measures for mainly agricultural policy objectives. Nonetheless, it might indeed make sense to supplement policies in the agricultural sector with complementary policies in the field of nutrition.
- At the present time responsibility for nutritional objectives and their instrumentation is largely in the hands of the Member States. The institutional classification of consumer- oriented food policy has developed in very different ways. In most EU Member States food policy is assigned to and shaped by (public) health departments. In the German context agricultural policy and food policy are often discussed within a related construct. This is reflected in the area of competence of the Federal Ministry for Food and Agriculture (BMEL).



- The German assignment of the area to BMEL weakens on the one hand the societal role of food policy if this is mainly pursued from the agricultural angle. Some possible reasons for this are the culture and traditions of the Ministry and extensive access for organised agricultural and food industry interests. On the other hand, when it comes to integration into agricultural policy there are major opportunities to take into account the interactions between health and other sustainability dimensions such as, for instance, environmental and climate protection. Finally, health policy is also a controversial societal policy area where considerable influence is exerted by organised interests and where it is common knowledge that it does not lend itself easily to the assertion of prevention interests.

103. The conclusion is that the question asked at the beginning about whether and, if so, to what extent the CAP should be developed further into an integrated agri-food policy cannot be answered in a definitive manner in this report. However, greater mutual consideration of the policy areas, agricultural policy and food policy, is something which the Board believes is necessary. For the objectives which primarily affect human nutrition (e.g. health), measures should be implemented above all in the area of food safety, food labelling and consumer-oriented food policy, and agricultural policy measures for objectives which primarily affect the agricultural sector. However, given the systemic links in the food system, it may be necessary to supplement measures in one policy area (agriculture or food) with complementary measures in the other policy area. The Board sees a particular need, on the grounds of climate protection, to extend the policy area of active consumption governance, with the goal of more sustainable nutrition which would trigger a major need for adjustment in agriculture. The Board also sees major potential here for pursuing other public interest objectives through a change in dietary styles (e.g. animal welfare).

104. No recommendations are made in this report concerning questions about the institutional framework within which agricultural and food policy should be coordinated, and about appropriate levels of competences (see on this subject the report of the Board on the policy for more sustainable nutrition which is in preparation).

### 3 A CAP oriented towards the public good: preconditions and transformation pathways

105. The CAP is one of the oldest and most heavily communitised policy areas of the EU. It has enjoyed major importance up to the present day and represents a cornerstone of the integration process. Whilst it is about preserving fundamental achievements like the creation of a common market for agricultural products, the remarks above have shown that the current CAP does not adequately address the current and future challenges in the policy area of agriculture and rural areas.

106. The shortcomings outlined – both in respect of the substantive orientation and instrumentation of the CAP and also in terms of the rampant complexity and red tape – only permit one conclusion: the CAP is in need of a fundamental review. This review should be strictly oriented towards the current and future challenges presented in Chapter 2.1.

107. Emphasis needs to be put on developing and implementing governance and funding systems which help agriculture to fulfil its diverse societal functions within an open economy (cf. Box 1: Why we need agricultural policy, p. 4). Feindt et al. (2018a) describe the need for a future viable social contract with agriculture. They suggest that in this contract agriculture should undertake to provide specific services whereas society should undertake to create the appropriate framework conditions for them. This includes in particular the appropriate remuneration of the public services of agriculture. The DLG (2017: 13) states in its position paper on agriculture 2030 “The EU agricultural budget can only be deemed legitimate if it sets out a clear, long-term policy objective for the sector. In this context the following criteria *inter alia* are to be observed: subsidies should be linked to the provision of public goods.”<sup>55</sup> And the WBA also wrote in 2005 (2005b: 4): “Legitimation for support measures in the medium and long term cannot be based on increasing farm efficiency but is to be justified with the provision of public services (either on a voluntary basis or enforced by regulatory law).”<sup>56</sup>

108. A comprehensive redesign of the CAP does, however, constitute a mammoth political task. This has to do not least with the major path dependencies which are to be found in the CAP as a consequence of the one-sided focus on income policy objectives and the related creation of established rights. The fact that changes in pathways or interruptions of the pathway will necessarily involve a change in established rights, impedes the political enforceability of a comprehensive CAP reform.

109. In the opinion of the Board all reform efforts will be pointless if the development of targeted funding and governance systems for European agriculture on the basis of the current

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<sup>55</sup> Original quote in German: „Das EU-Agrarbudget ist nur bei klarer, langfristiger politischer Zielsetzung für den Sektor legitimierbar. Dabei sind u. a. folgende Kriterien zu beachten: Subventionen sollten an die Erbringung öffentlicher Güter gekoppelt werden“ (DLG 2017: 13).

<sup>56</sup> Original quote in German: „Mittel- und langfristig kann die Legitimation für Fördermaßnahmen nicht von der Steigerung der betrieblichen Effizienz ausgehen, sondern ist mit der Bereitstellung öffentlicher Leistungen (sei es freiwillig oder ordnungsrechtlich erzwungen) zu begründen“ (WBA 2005b: 4).

structures of the CAP were not tackled in a proactive manner. This includes the necessary gradual but consistent dismantling or conversion of the current system of largely unconditional direct payments. These funds are urgently needed for the targeted remuneration of the public services provided by agriculture.

110. If the necessary reorientation of the CAP is postponed, this means that the problems to be addressed and also the need for farm adjustments will become more urgent resulting in additional adjustment costs. An orientation towards the status quo and the attempt to increase the legitimacy of direct payments by changing their name will, therefore, end up in a dead end. The standstill invoked with the argument of “reliable framework conditions” is an illusion: reliable framework conditions can only be established through a long term-orientation of the CAP towards public interest objectives that enjoy broad societal support.

111. A concept is presented below for a CAP oriented towards the public good and a transformation pathway to get us there. It should be borne in mind that at this point only fundamental principles and transformation steps can be discussed. In the final instance, any reorientation of the CAP towards a greater focus on the public good must be open to learning processes and will require continuous fine-tuning.

112. In order to orient the CAP primarily towards the remuneration of public services provided by agriculture, a transformation process must take place that encompasses various dimensions. They include (a) adjustment of the overall budget to the societal demands of the public services of agriculture and adjustment of the distribution of CAP funds to the Member States, (b) merger of the EAGF and EAFRD or (in the event of the continuation of both funds) reallocation of funds between the EAGF and EAFRD, (c) changes in the funding responsibilities established within the funds, (d) changes to the measures implemented in the funds and (e) changes in the administrative, control and penalty mechanisms established within the funds.

**a) Overall budget and regional distribution.** The overall budget of European agricultural policy has developed historically. Up to the beginning of the 1990s it consisted above all of funds to finance market organisations with high expenditure on intervention and export subsidies. Today, it mainly reflects the decision taken at the beginning of the 1990s to compensate the fall in administered prices via state-funded direct payments to farmers. If the CAP had a stronger focus on achieving public interest objectives, the budgets required for the desired target level of public services would have to be identified and calculated. Furthermore, the distribution of funds to the Member States would have to be examined. Today’s allocation of funds for direct payments results from the yield level of an historical reference period, the composition of production in this reference period and, in the case of the new Member States, their negotiating position during the accession negotiations. Today’s allocation of funds in the second pillar of agricultural policy results from the importance of agricultural sectors when it comes to land, unemployment, and per capita income in the Member States. It is likewise subject to varyingly strong country-specific influences (Grethe 2008: 202f.). In the long term, this allocation of funds is to be based on clear and transparent criteria. The allocation of funds should take into account the scale of

action needed, which has still not been systematically analysed and therefore needs to be estimated in the medium term, and the role of the agricultural sector in the respective national economies. This could include, for instance, the number of workers in agriculture and the extent of agricultural land, the need for action in terms of environmental protection and animal welfare policy, imbalances in the field of rural development and the potential target contribution to be achieved with the funds towards defined European public interest objectives.

The WBAE does not make any recommendations about the level of the overall CAP budget as the need for action has neither been estimated nor weighed up with the need for action in other EU policy fields. Since the current distribution of the CAP budget is historically established and delicately balanced with other policy fields, the Board recommends a pragmatic approach. For instance, the current distribution of funds could be adapted to a yet to be defined scale of external convergence just as it is currently under discussion for direct payments. Such a pragmatic approach could be the starting point for the allocation of CAP funds, also in the event of changes to measures and funding models. However, in the long term, more transparent criteria (see above) should be used for fund distribution.

**b) Merger of the EAGF and EAFRD or reallocation of appropriations.** The WBAE believes the transfer between various “funding pools” is not the key factor in the long term as both funding models and measures within the EAGF and the EAFRD can be changed. The funds can, therefore, continue to exist or be merged. Here, it is important to move away from the mind set involving the links between funds, funding rules, measures and implementing mechanisms. This is how the CAP can be fundamentally revised even if the fund structure were maintained.

**c) Funding responsibilities.** With reference to funding responsibilities the WBAE suggests that:

... merely the budget spent in the field of market organisations, a central peatland protection program organised as a tendering procedure by the EU and support within the framework of the nature conservation network Natura 2000 should be completely financed by the EU. In case of both, the market organisations and climate-action driven peatland protection, economies of scale of a central organisation and major EU-wide external effects are pronounced. Both for climate-action driven peatland protection and for the promotion of Natura 2000 areas the following applies: these are policy areas with substantial European added value which can be considerably strengthened by removing them from national competition for funds.

... all other payments, i.e. also the direct payments that are to be gradually phased out, should be co-financed by the Member States in order to defuse positioning oriented towards recovery of funds. In this context, the co-funding rates should still reflect the economic development stage of the regions and also the spatial spread of the public goods and services involved (e.g. climate protection with a higher EU funding share than for instance village development).

National co-funding of direct payments that remain in place during a transition phase is in the opinion of the Board an expedient transformation strategy for two reasons. Firstly, the related saving of EU funds would be an appropriate starting point for dealing with the expected cutback in the CAP budget as a consequence of Brexit. Secondly, there is less incentive for Member States to adhere to the instrument of direct payments because of the funding model. Alternatively, or also in addition, it would be conceivable for those Member States who prefer the option, to be allowed to offset cuts in the EU budget in part by national top ups for the decoupled direct payments.

**d) Measures:** In terms of the instrumentation of the CAP the WBAE suggests that:

- ... direct payments in their current form should be completely phased out by the end of the next financial period. As a first step, the direct payments are to be reduced by the contribution that was attributed up to now to greening (30 % of direct payments). Consequently, from the very beginning – as suggested by the European Commission (2017a) – greening should be abandoned and instead the agri-environmental and agri-climate policy measures listed below should replace them. Other annual dismantling steps are to be laid down in a binding manner with the resolutions on the CAP post 2020. The binding of direct payments to other regulations (cross compliance) should be equally reduced step-by-step and accompanied by adjustments to the regulatory framework.
- ... most of the EU agricultural budget in the period 2021-2028 should be used for the co-financed remuneration of public services of agriculture and the pursuit of other public interest objectives (for instance in the field of rural development). These measures are in principle to be programmed by the Member States or regions and notified to the European Commission.
- ... in the field of peatland protection a new policy area should be established at EU level within which the European Commission purchases greenhouse gas emission reductions at the lowest possible price by means of tendering procedures.<sup>57</sup>
- ... support for protection of biodiversity in open landscapes should be extended within the framework of the Natura 2000 nature conservation network. An independent share of the agricultural budget is to be reserved on the European level for basic cover in Natura 2000 areas and for the ensuing nature conservation upvaluations by means of voluntary contractual nature conservation measures (with no purchase of land). This would give priority to protection and upvaluation measures within the EU-wide Natura 2000 network and extract them from national competition for funds. Member States would apply for these funds by means of targeted programmes whereby a transition would be introduced

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<sup>57</sup> Besides the centrally organised peatland protection which exploits the high target contribution to climate protection and the very unequally distributed greenhouse gas mitigation potential between the Member States, Member States can and should, within the framework of the co-financed policy area, implement peatland protection measures on the basis of diverse environmental and nature conservation goals.

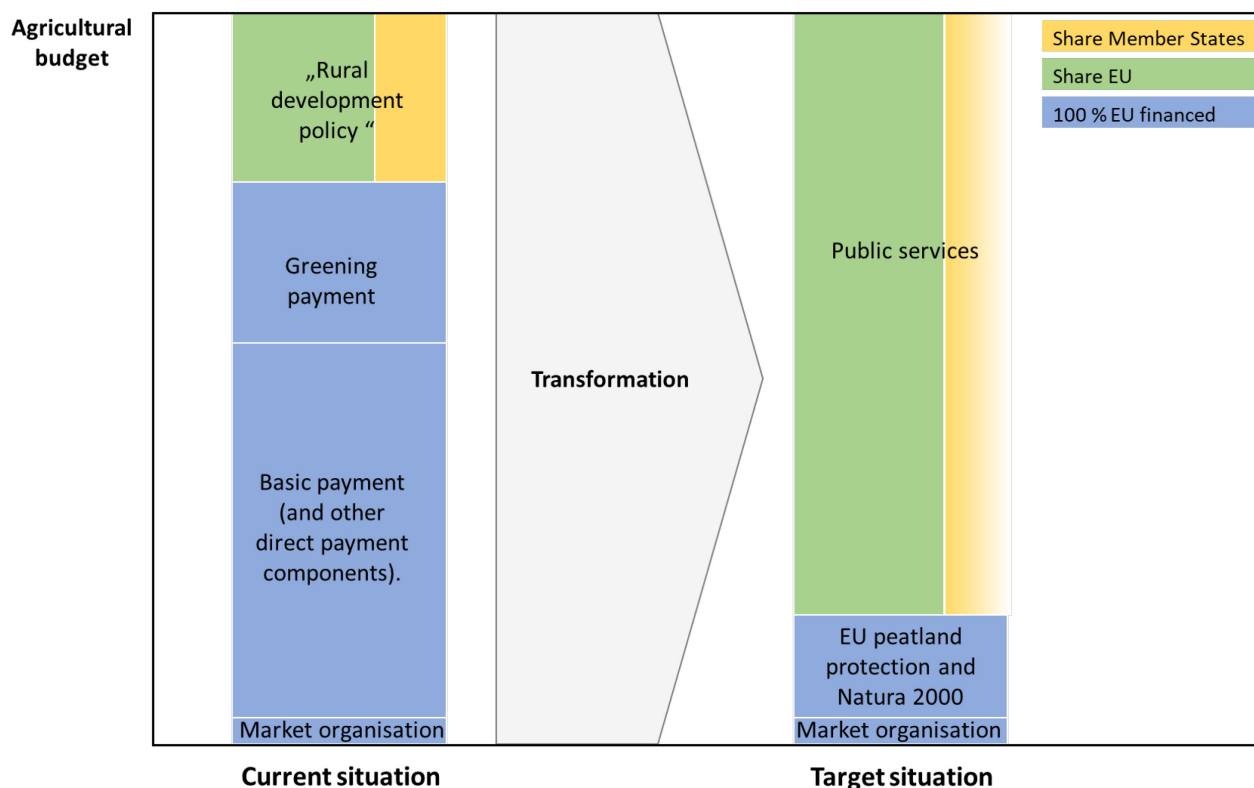
to objectively justified fund allocation within the CAP. To maintain spending discipline, low national co-financing shares could be envisaged.

**e) Implementation, control and penalty mechanisms:** The WBAE proposes:

- ... giving the Member States more freedom and responsibility for programming the CAP in line with the Communication of the European Commission (2017a).
- ... jointly programming all measures that remunerate public services in line with the Communication of the European Commission (2017a) (excluding peatland protection by means of the above-mentioned tendering procedure and Natura 2000 measures).
- ... improving the efficiency of controls by applying the single audit principle.
- ... reducing EU implementing provisions on the CAP to the necessary minimum and codifying them beyond the individual support periods.

113. A corresponding transformation, which should be undertaken over a period of around 10 years, is presented in Figure 5. In this figure the area of the column segments represents the size of the respective budget. In addition to the above-mentioned reflections, the option of compensating for the reduction in EU funds (resulting, for example, through Brexit) via higher national co-financing shares is presented. As the co-financed policy areas are considerably enlarged, it would be possible to extend the existing national co-financing resources, in combination with reduced national co-financing rates, to larger areas of policy. Likewise, it is also possible to increase the overall Member State co-financing resources and co-finance additional policy areas with the original rates. These options are visualised by the column representing Member States' funding share diminishing towards the right. The entire diagram is to be understood as a schematic representation as neither the amount of the future CAP-budget nor the future budget needs of EU-financed peatland protection and Natura 2000 areas are foreseeable. To establish the budget for an EU peatland programme and the promotion of Natura 2000 areas, an estimation of financial needs would have to be undertaken which was not possible within the framework of this report.

**Fig. 5:** Transformation of the agricultural budget (EU and national co-funding, schematic diagram)



114. In the opinion of the Board, a period of 10 years is sufficient for the transformation presented in Figure 5. The German Federal Government should grasp the opportunity to fully reallocate the maximum possible 15 % of national direct payment funds to the second pillar and use this in a targeted manner to finance environmental and climate protection as well as animal welfare measures. In this way, the sector would be given guidance and the level reduced from which direct payments would be downsized during the forthcoming financial period. Germany should also use this period to validate and further develop the existing models for the measurement and assessment of public services (e.g. Neumann et al. 2017).

115. All policy instruments are to be included in the further development of governance and funding systems, both budget-relevant instruments as well as non-budget relevant ones in the field of regulatory law or agricultural trade policy. At the same time, these governance and funding systems are not the sole responsibility of the state but can and must combine state, private sector and civil society components in an expedient manner.

Consequently, the WBA recommends in its report on animal husbandry (WBA 2015), for example, developing the WTO rules in terms of ethical and moral concerns along the lines that animal welfare driven labelling obligations and import constraints can be permitted under clear and closely defined rules. What is interesting in this context is that animal welfare criteria were recognised in a more recent WTO dispute for the first time as “moral concerns” under Article XX (a) GATT by WTO arbitrators, thus permitting trade constraints. Sonntag et al. (2017) discuss in this

context which institutional preconditions must be put in place in order to distinguish “justified moral concerns” from protectionist motives and suggest the setting up of a WTO institution on the basis of a pilot study which conducts neutral studies to determine the degree of concern in society about controversial production forms on the basis of a validated and standardised survey approach.



## 4 Paths to a CAP oriented towards the public good: what the German Federal Government should promote

116. Germany is a major stakeholder in the negotiation processes about the future design of the CAP. At the same time, there is a major need for action in Germany regarding environmental and climate protection, animal welfare, and specific challenges in the development of rural areas. Against the backdrop of the preceding analysis an outline is given below of what the Board believes the German Federal Government should advocate in order to secure and implement the urgently needed shift towards a CAP that serves the common good. Furthermore, the Board presents recommendations for implementation in Germany. Already today Germany could make more use of various implementation options to ensure a stronger orientation of the CAP towards the public good. The use of this scope in future will probably become even more important as the implementation of the reform proposals of the European Commission (2017a) would offer the Member States even more extensive choices for CAP implementation.

### 4.1 Rebalance and consistently pursue the CAP objectives

117. The determining feature of the current CAP is its one-sided focus on the objective formulated in the Treaties of Rome of a fair standard of living for the agricultural community. This income objective is, in fact, the reason for more than 70 % of all CAP expenditure (cf. Chapter 2.3). In contrast, the existing problems and challenges with regard to environmental and climate protection as well as animal welfare are neither adequately named nor addressed. Instead of continuing to point out the need for direct income aids and endeavouring to justify them politically by repeatedly renaming direct payments, the Board recommends that the German Federal Government both at the European and the German level:

- identify and clearly state the existing challenges in the areas of environmental and climate protection, animal welfare and rural development;
- derive objectives from the challenges and operationalise them by means of interim objectives and timeframes;
- elaborate adequate governance and funding systems for the provision of public services and the obligations of agriculture;
- consistently implement in particular the missed agri-environmental objectives, and orient the CAP more than in the past towards these objectives;
- advocate interpreting and implementing the income objective in line with the established case law of the European Court of Justice (cf. Chapter 2.3) and support the orientation of European and German support policy towards preserving the diverse societal functions of agriculture;
- initiate and actively shape a broad societal discourse about a future-viable design of the CAP which goes beyond the forthcoming reform decisions in order to broadly anchor the funding and design of a CAP oriented towards the public good in society and ensure its long-term

viability. This also includes broad societal discussion of technological, organisational and structural developments in agriculture bearing in mind scientific evidence, different preferences, value judgments, ethical questions and the development of new paths for societal decision-making.

## 4.2 Rethink the architecture of the CAP and revise competences

118. The CAP has a historically established structure, which is often referred to as a two-pillar architecture composed of the EAGF (first pillar) and the EAFRD (second pillar). In this architecture, there are reflective and substantive links between the two funds and their respective funding regulations, measures and implementation mechanisms. A transformation process towards a future-viable CAP, i.e. an efficient CAP consistently oriented towards the public good, means moving away from these interrelations and reviewing and changing the allocation of competences established within the current CAP. In terms of the CAP architecture, the Board advises the German Federal Government to:

- support the path of greater CAP decentralisation proposed by the European Commission in its Communication of November 2017. A relocation of design and funding competences to the level of the Member States and regions corresponds in many areas to the subsidiarity principle and is logical given the heterogeneous problems and preferences of the EU Member States;
- advocate that, in the long term, only market organisations and areas of climate and biodiversity protection (peatland protection and Natura 2000) be left under the (almost) complete funding competence of the EU. The design of support measures for further public services (including those in the field of rural development) should be shifted more than in the past to the responsibility of the Member States. These measures are to be consistently co-financed by the Member States and jointly programmed within the framework of national or regional strategic plans;
- promote the development of suitable incentive, control and penalty systems for an ambitious target setting of the Member States within the framework of their subsidiary responsibility. This challenge exists already today but will take on more importance with the desired further decentralisation and result orientation of the CAP. At Member State level it is about identifying the intervention logics and indicators to monitor the delivery of objectives. At EU level the European Commission must develop transparent monitoring criteria for the notification of national and regional strategic plans and appropriate and effective penalty mechanisms.

## 4.3 Reduce the administrative burden to an appropriate level

119. The current CAP is characterised by a high degree of complexity and administrative formalities. This excessive red tape should be dismantled in the course of the reorientation of the CAP post 2020. The main reasons for the existing administrative complexity are, firstly, an unclear legal situation which fundamentally changes with every new support period and which can

continue to change during the support period, in some cases retrospectively. Secondly, an unduly strict stance of the EU on the proper allocation of resources. Besides an inappropriately heavy administrative burden, this creates other negative consequences in that when member states implement the CAP, substantive objectives increasingly take a back seat to minimising the risk of financial burden (cf. Chapter 2.2). The Board recommends that the German Federal Government advocates at EU level:

- a clear reduction in the complexity of the legal framework and the regulatory depth of the CAP. They lead to an inappropriate administrative burden, changing legal interpretations and related permanent learning costs coupled with a high infringement and financial correction risk. A central approach to this would involve scaling back and codifying the EU implementation provisions for the CAP with indefinite scope and their presentation in a timely manner prior to commencement of the new support period;
- the introduction of the single audit principle;
- that the Member States no longer have to prove the regularity of expenditure but provide performance statements and checks on the basis of output and result indicators. If the regularity of expenditure is also to be proven in future, then maximum admissible error rates should be established for each specific policy area in such a manner that the administrative procedures can be carried out with an appropriate effort. For the area of today's second CAP pillar this would mean an increase in the current maximum admissible error rate of 2 %.

120. Furthermore, the German Federal Government should advocate together with the Federal State Governments (Landesregierungen):

- improvements to administrative efficiency through increased use of digital technologies and adequate monitoring systems particularly in the case of area-related schemes. In principle, all support measures should go hand in hand with an obligation for the recipient of support to provide relevant data in a digital database in order to monitor the measures and be able to evaluate them at a later date in an unbiased and efficient manner. When designing support conditions, attention should be paid to ensuring that there are no overriding data privacy reasons.

#### **4.4 Phase-out direct payments and other payments not oriented towards societal objectives**

121. Inefficient transfer payments oriented above all towards the agricultural area currently tie up a large share of the CAP budget and are no longer available to tackle the weighty societal challenges. The phasing-out of direct payments is, therefore, a major precondition for a new direction of the CAP which serves the public good. It will only be possible to successfully tackle the actual societal challenges if those payments which are not tailored to need are successively but consistently scaled back. In order to overcome political resistance to this transformation path at the European level, the resulting distribution effects between the Member States must be taken

into account and partially compensated. Against this backdrop the Board recommends to the German Federal Government:

- strive to achieve the complete dismantling of all 100 % EU-funded direct payments within the framework of the CAP over a period of around 10 years. This includes all current direct payment components whereby the greening and young farmer premiums allocated via the EAGF are to be halted on the commencement of the new support period. In the long term, payments should only be made to farmers in areas in which land management and the related public services (such as the promotion of biodiversity or the preservation of diverse agrarian landscapes) would otherwise be in jeopardy (cf. Chapter 2.3).

122. For the transition period, in which there are still direct payments, the Board recommends:

- implement overall budget cuts (which may result due to Brexit) by reductions in direct payments and not in the areas of objectives and measures currently programmed via the EAFRD;
- extend the option of reallocating financial resources from the EAGF to the EAFRD beyond the current 15 %;
- advocate at the European level optional national co-financing of direct payments or, where appropriate, the introduction of optional nationally funded top-ups in order to increase acceptance for abolishing direct payments (cf. Chapter 2.2);
- identify further ways and means of getting Member States on board that are critical of the co-financing of direct payments. Options include (a) lower national co-financing rates for Member States in which the direct payments are clearly below average today which means that convergence would be achieved de facto in the EU-funded share of direct payments, and (b) compensation in other policy areas within the CAP (e.g. budgets for the remuneration of public services, convergence of direct payments) or also outside the CAP (e.g. structural policy);
- strictly limit the option of coupled direct payments to the provision of narrowly defined public services (as defined in Box 1) (e.g. premiums for extensive grazing) and base the scale of support on the costs of providing these public services;
- reject capping or degression of direct payments and speak out against more support for the first hectares. These modifications cannot overcome the lack of orientation of direct payments and lead to undesirable side-effects (for instance virtual divisions of farms). As all such instruments strive to increase societal acceptance for direct payments, these modifications also oppose a consistent new orientation of the CAP (cf. Chapter 2.4).

123. Finally, the Board recommends in principle limiting investment support exclusively to investment costs which arise through the pursuit of public interest objectives such as an increased level of environmental protection or animal welfare.

## 4.5 Further develop measures to reward environmental and climate protection and animal welfare-related public services in agriculture

124. The current instruments established within the CAP to deliver environmental, climate and animal welfare policy objectives do not do justice to the major pressure for action in these areas. A CAP which wishes to live up to its ecological sustainability claim, international obligations and the growing ethical demands from the population in terms of livestock husbandry, needs a far more effective and efficient mechanism to remunerate public services in the fields mentioned above. This encompasses advancements of existing instruments and the integration of new, innovative approaches. The Board recommends:

- in the field of peatland protection, the progressive development and funding of a new European policy area in which the European Commission, by means of tendering procedures, purchases greenhouse gas emission reductions at the lowest possible price (cf. WBAE and WBW 2016);
- fostering the protection of biodiversity in open landscapes as part of the Natura 2000 nature conservation network. A part of the budget is to be earmarked at the European level for legally binding conservation measures in Natura 2000 areas as well as for more demanding conservation work in the form of voluntary nature conservation contracts (excluding purchase of land). This will give priority to both basic and enhanced biodiversity conservation within the EU-wide Natura 2000 network and remove them from national competition for funds. Member States would apply to the Commission for these funds by proposing targeted programmes. This would imply a transition of CAP funding rules away from proportional allocations among Member States towards fund allocations based on objective and transparent needs within the Member States (cf. Chapter 3). To ensure spending discipline, low national co-financing shares of 5 % to 10 % could be envisaged;
- requiring Member States to allocate to targeted agri-environmental and climate protection measures in their national strategic plans at least as many financial resources as are currently given to the greening premium, i.e. 30 % of the current direct payments;
- advancing existing agri-environmental and climate protection measures as instruments tailored to different types of habitat and equip them with a larger budget. Here the right balance must be struck between appropriate targeting on the one hand and administrative costs on the other. In particular:
  - incentives for spatial targeting of environment-climate protection measures should be strengthened, e.g. premiums or bonuses for linking up priority areas for biodiversity, or payments differentiated by soil quality;
  - result-oriented remuneration models should be further developed;
  - collective approaches to environmental and climate protection should be developed. The Dutch model of collectively organised and regionally coordinated contractual nature conservation could serve as a model;

- changing administrative provisions in the field of agri-environmental and climate protection measures in such a way that (a) the higher costs associated with more targeted measures can be funded from CAP resources, and (b) Member States have the opportunity to make the term of the contracts fit the objective pursued;
- abolishing greening and cross compliance whilst further developing regulatory and other specific law areas. In order to avoid the enforcement deficits caused by dismantling cross compliance, there is an urgent need for enhancing regulatory and specialist law and its consistent enforcement (enhanced control systems, adjustment of penalty levels, etc.). This will then serve to ensure the preservation of valuable landscape structures and species-rich grassland and support overall the enforcement of regulations whose effectiveness has largely been reliant on the presence of cross compliance rules.

125. Moreover, the Board recommends advancing the options for remunerating enhanced animal welfare within the CAP. In particular, the Board recommends:

- creating an option for those Member States whose regulatory animal welfare standards are significantly higher than the EU average to compensate some of the costs incurred for this through state payments within the framework of the EAGF or the EAFRD; making more use of animal-based indicators (for instance: hoof health, somatic cell count in milk, joint inflammations) to remunerate animal welfare enhancements.

126. Finally, the WBAE recommends that the German Federal Government strive to change the WTO rules in respect of ethical and moral concerns such that animal welfare-related labelling obligations and import constraints are admissible under clearly and strictly defined rules.

#### 4.6 Understand risk management as an entrepreneurial task

127. There are a number of strategies for risk management in agriculture whose suitability varies depending on the farm situation and farm operator preferences and whose optimal use only can be determined on the individual farm level. State support should, in principle, be limited to the action areas of market failure. So as not to distort optimum farm risk management, one-sided support for selected risk management instruments should also be avoided in these cases and comparable support rates should be the goal for different risk management instruments. Support measures should be limited in time and mainly oriented towards strengthening market forces by means of information support, the creation of transparency and the provision of infrastructure. Against this backdrop the German Federal Government should advocate the following within the framework of the CAP negotiations:

- Agricultural policy measures to support risk management should limit economic loss risks and should be clearly delimited as such from income policies. The support rates of up to 70 % of eligible costs possible under EU law (EAFRD Regulation No 1305/2013) for many risk management instruments are deemed to be too high and should be reduced across the EU as part of the CAP reform. Furthermore, the German Federal Government should advocate, both

within the EU and beyond it on the international level, a regular, strict review of state support for risk management instruments with a view to potential distortions of competition.

- Conversely, direct payments motivated by income policy should not be deemed to be a risk management instrument. Given the lack of orientation towards income level and volatility, they do not make any targeted contribution to reducing the income risk.
- Within the framework of the CAP more weight should be attached to promoting the transfer of knowledge in the field of risk management. Here it is about strengthening the information situation on risk exposure and the knowledge of the stakeholders in the overall value chain particularly with a view to (more) recent risk management instruments (index-based insurances, futures, commodity futures markets milk). The aim here is to improve the individual farm options for the optimum design of risk management and to support farms in adjusting to changing economic and agricultural policy framework conditions.
- The EU crisis reserve should be strengthened as an emergency instrument by saving up unused funds and thus enabling the reserve to offer effective assistance even in the case of larger market crises.
- The remaining state “safety nets”, e.g. in the form of intervention prices, should be regularly reviewed in terms of need and design<sup>58</sup>.
- To reduce the political risk, major changes in the policy framework should be communicated in a timely manner (like, for instance, in the case of the withdrawal from the milk and sugar quotas). If direct payments are dismantled, this should be done in clearly prescribed stages. In this way farmers can make timely adjustments within the framework of their entrepreneurial freedom and avoid structural breaks.

128. At the federal government level the BMEL should:

- further develop the specified framework in the case of ad hoc disaster relief in such a way that private sector risk management is not crowded-out. In order to avoid possible distortions of competition within Germany, there should be greater standardisation throughout Germany, first, of compensation calculations and, second, of the procedures launched to identify target groups for emergency aid (examination of an individual need and/or threat to livelihood);
- examine, against the backdrop of the elevated risk of the introduction of invasive pests with high damage potential resulting from the growing movement of goods, whether and, if so, in what form compensation rules (e.g. private sector or subsidised compulsory insurance or funds) could also contribute in the case of plant diseases and pathogens to risk reduction and more effective disease prevention.

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<sup>58</sup> The intervention rules for dairy products led in 2017 to major stockpiling of skimmed milk powder although the milk price was comparatively high (major demand for milk fat).

## 4.7 Strengthen knowledge systems and innovations

129. The tackling of existing challenges in the areas of environmental and climate protection and animal welfare whilst safeguarding the elementary functions of agriculture (e.g. the production of safe and diverse food) calls for major technological, organisational, and institutional innovations and their implementation in practice. These challenges are to be tackled mainly by the private sector and at the national level. However, given that the challenges are of supra-national importance and that knowledge is partially a public good, these challenges do also lead at the European level to a number of tasks that should be understood as part of the CAP. Against this background, the Board recommends that the German Federal Government advocates for:

- the continued linking up of problem-solving strategies and research, as is currently established in the European Innovation Partnership “Agricultural productivity and Sustainability” (EIP-AGRI). The EIP-AGRI brings together farmers, agribusinesses, advisers, scientists, non-governmental organisations and other stakeholders to work together on agricultural and forestry innovations. Such partnerships should be carried on, evaluated regularly, and – on this basis – developed further;
- by means of research funding, the adaptability of farms should be strengthened in order to support them in effectively and efficiently fulfilling their societal functions and enable them to adjust to changing framework conditions, including changes in the agricultural policy framework. Furthermore, research funding should facilitate the transition towards a more sustainable food system. Against this backdrop, the focus on resilience indicated in the Commission Communication of November 2017 should be assessed in a critical manner as this focus may overly emphasise maintaining the status quo instead of adjusting to future challenges;
- facilitating a broader use of research findings and innovations by enhancing communication across Member States about research and innovation processes underway and about the findings obtained. Here in particular, ways are to be found in order to enable Member States with low income and limited research capacities to participate more effectively in innovation processes than up to now.

## 4.8 Understand and strengthen rural development as a cross-sectoral task

130. The development of rural areas is a prominent position in the current opinions of agricultural policy decision-makers. According to the European Commission “strengthening the socio-economic fabric of rural areas” is one of the three most important objectives of the future CAP (EU COM 2017a: 11). The German Federal Government mentions “attractive vibrant rural areas worth living in” (BMEL 2015: 8, own translation) as the first objective in its guiding principle for agricultural policy. The current orientation of the CAP and its implementation in Germany do not, however, reflect this priority. Furthermore, in the policy field of rural development there is a coordination deficit amongst the various spatial policies and substantial extensive multilevel interdependencies. Furthermore, the varying degrees of the need for action in the Member States



regarding the objective of balanced territorial development in the EU are not adequately taken into account. Against this backdrop the Board recommends that the German Federal Government:

- strive to ensure – if rural development continues to be in the CAP – that sufficient options for the implementation of measures beyond the agricultural sector along the lines of a territorial, problem-oriented policy for rural areas are provided;
- work towards the EU focusing their policy measures in this field – more than before by means of different co-financing rates – on those Member States and regions in which the need for action with regard to balanced territorial development in the EU is particularly high;
- strive to ensure that responsibility for rural development measures outside the above-mentioned regions is assumed more than in the past by the Member States, thereby contributing to a major reduction in multi-level interdependencies and a decrease in transaction costs;
- also take into account the different regional condition of the rural areas’ “socio-economic fabric” when distributing EU funds to the federal states - in the event that support does not focus on Member States with particularly extensive needs for action;
- work towards ensuring that the exchange on the various spatial policies currently underpinned by the EAFRD, the EFRD, the ESF, the cohesion fund and the EMFF is intensified thereby resulting in improved coordination.

#### 4.9 Improve the coordination of agricultural and food policy

131. Given the links between agriculture and food within the food system, production- and consumption-driven policy measures should be coordinated if (a) interactions are to be expected such as, for instance, a possible reduction in border protection for animal products or (b) overarching public interest objectives can be achieved more effectively through complementary governance mechanisms in both policy areas. The latter is particularly the case when it comes to climate protection but also to animal welfare. Given the international market integration of the agricultural and food sector, there are only limited governance opportunities here on the supply side. Consequently, it might make sense to also pursue these objectives through measures which aim to bring about a change in consumer eating habits, in particular the reduced consumption of animal products. At the present time, there is no such coordination of measures in these two policy areas on the European level. This is not least because responsibility for consumer-oriented food policy currently lies completely in the hands of the Member States.

132. Against the backdrop of the reflections set out in Chapter 2.8, the major need for action in the areas of environmental and climate protection and animal welfare policies, and of the health problems linked to nutrition, the WBAE recommends that the German Federal Government at the EU level:

- routinely re-examine agricultural policy decisions in conjunction with the CAP for their food and human health implications;

- clarify conceptual questions regarding the complementary (both supply and consumption driven) pursuit of public interest objectives in terms of environmental and climate protection and animal welfare. What must be clarified in particular is: a) are there areas in consumer-oriented food policy for which there is European added value which means that they should be financed in part and organised at the European level too? And b) by means of which institutional and procedural structures can the cross-sectional character of consumer-oriented food policy be adequately taken into account?

133. Furthermore, the WBAE recommends that the German Federal Government at the federal level (WBAE and WBW 2016, see also the expert report of the WBAE on sustainable nutrition to be published in 2019):

- further develop consumer-oriented food policy instruments and deploy them significantly more than in the past to pursue public interest objectives relating to environmental and climate protection and animal welfare;
- strengthen competences at the political level to consider the sector as a food system and develop policies for its transformation into a more sustainable food system.

#### **4.10 Use the scope that the CAP offers to allocate resources to societal objectives to full capacity**

134. As an overarching policy area established at the European level the CAP sets out the fundamental framework for the respective Member State design of its policy for agriculture and rural areas. The support policy established through the CAP is neither very effective nor efficient in meeting diverse challenges. It is therefore urgently necessary to reform the CAP along the principles and recommendations set out in this report. At the same time, already today the CAP offers more scope for the allocation of resources oriented towards societal objectives in the Member States than is currently exploited in Germany. The WBAE holds that the existing and prospective future (post 2020) scope for action for increasing orientation towards the common good should be used. In particular, the Board recommends that the German Federal Government:

- increase the reallocation rate from the first to the second pillar of the CAP to the 15 % currently possible under EU law;
- use the option of coupled direct payments with a strict focus on the provision of closely defined public services and base the level of support on the costs of providing these services (e.g. premiums for extensive grazing);
- consistently orient all support measures of the Joint Task "Improvement of Agricultural Structure and Coastal Protection" (GAK) covered by the national framework regulation towards the public good, e.g. a stronger orientation of investment support for individual farms towards public interest objectives;
- use the GAK for the national expansion of the remuneration of animal welfare services (WBA 2015), e.g. by extending the set of measures in the field of animal welfare and by earmarking

federal funds available in the context of the GAK for animal welfare measures, for instance through the establishment of a special framework plan (Sonderrahmenplan) “animal welfare in livestock husbandry” that features an independent budget;

- implement the planned GAK specific framework plan “Promotion of the development of rural areas” (as envisaged in the coalition agreement between the CDU, CSU and SPD) in a manner conducive to the public good. Ensure that the establishment of this special framework plan does not reduce the opportunities to use the GAK for the remuneration of agriculture’s public services in the areas of environmental and climate protection and animal welfare.

## 5 Conclusion

135. The decisions to be taken in the near future at EU level will shape the CAP up to the end of the next decade. The German Federal Government should see the CAP reform as a great opportunity and use the reform and its subsequent implementation to free the CAP from its income orientation and transform it into a policy that consistently serves the public good. A CAP oriented towards the public good would help agriculture to meet the challenges ahead and support the CAP’s long-term societal acceptance, thereby creating a reliable agricultural policy framework for the next decade and beyond.

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