

The economic nature of the Single Farm Payment

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Introduction

An analysis of the economic character of the Single Farm Payment (SFP), introduced by the Fischler reform, is needed in Europe. Is it, even if decoupled, still a support to production? Is it an income support measure? A payment for multifunctional services delivered by the farmer to society? An economic rent? A mixture of all these things together? Or is it still something else? This article tries to analyse the nature of the SFP aiming to understand its very economic nature and which are the consequent implications deriving from it.

It is not a support to production

The price support of the old CAP is at the origin of the SFP. Whatever the specific instrument adopted (import duties, export restitutions, deficiency payments, withdrawal from the market etc.), the price support measures had the common economic nature of being coupled to production. They were, in fact, directly related to the objective of food security, established in 1957 by the Treaty of Rome. Some decades later in the Nineties, however, the generalised over-production and the overall demand for more liberalised markets pushed the EU to change, passing first to the Mac Sharry reform compensatory payments and then to the Agenda 2000 direct payments. The nature of the CAP support changed as well. The payment still maintained a link to agricultural production, even if it was with the per hectare/head compensation formula. But the objective was that of shifting the nature of CAP payments in the direction of an income support. This was at least the aim of the Commission as one can argue while observing that it systematically proposed the introduction of an individual ceiling for the payments, or at least a digressive support beyond a fixed threshold. As a matter of fact, such a proposal was rejected in the final decision of the Mac Sharry reform and approved in Agenda 2000, but transferring the decision to the autonomous choice of the member states. Agenda 2000 also left to the member states the option to connect the payments with environmental obligations under cross-compliance. But most of them generally chose to impose feeble obligations and to apply only weak control measures. As a consequence it is difficult to affirm that the eco-conditionality was actually introduced broadly. One can still discuss if and until what point the direct payments were indeed decoupled. But today, because of the fact that the SFP is calculated on historical bases, all possibility of misunderstanding is dissolved. The decoupled SFP no longer has the nature of being a support to production. To be specific, it maintains only an indirect effect on production due to the permanence of marginal farms, without which they would have to eventually stop.

It is not a payment for multifunctional goods and services

Together with the SFP, the Fischler reform has also introduced compulsory cross-compliance. The kind of connection between the SFP and cross-compliance obligations is very important, because it could influence its very nature. If, in fact, the cross-compliance constraints have been conditioning

effectively, one could argue that the SFP has the nature of being a flat-rate payment for the multifunctional benefits that agriculture provides for the whole of society. It would have been, in other words, a “greening” of the first pillar. As a result, the pillar I would have converged de facto to the II and, at the same time, the EU could have a stronger claim to put the SFP into the “green box” at the WTO.

A strong, widespread and effective cross-compliance could have been interpreted like a re-coupling of the SFP to the environment. It would have also resolved the discussion on the opportunity to put a ceiling on the per farm payment. If the SFP in fact were the equivalent sum for a multifunctional service effectively delivered, there would not be any reason to impose a ceiling. In other words, if the Queen of England on her 108 thousand hectares of land (so many it seems she owns) produced the environmental maintenance service on each hectare that a small farmer produces on his one hectare only, they should both be paid in proportion, as well as when they sell their barley or their milk. It is perfectly legitimate that one receives the market price for each ton (or gallon) produced, in proportion to the productive capacity of his farm. The same treatment should be reserved if the production of a multifunctional service is concerned.

However another conclusion should be reached: that the SFP is not a multifunctional payment, if no severe commitments are linked to the SFP.

It is not a transitory adjustment assistance measure

The Buckwell Report in 1996 proposed a transformation of the compensatory payments of the Mac Sharry reform to "transitory adjustment assistance" payments. Considering the fact that the farmer has been frequently induced to invest in some forms of production in response to the coupled price support, it would have been unfair that the EU, when changing its strategy and abandoning or weakening its support, did not help the farmer in consequent repositioning.

Due to their nature, a "transitory adjustment assistance" payment has to respect three necessary conditions: a) being related to the costs of the adjustment and conditioned on a contractual basis to the shift of farm activities towards products not in excess and demanded by the consumer and/or multifunctional services paid by public expenditure; b) to decrease in volume in relation to the progress of the adjustment process; c) to end some years later, when all the farms were expected to have completed their adjustment.

This solution also had the advantage of gradually freeing an increased sum of money to fund the new policies which would take the place of the old ones: namely those under pillar II oriented to foster competitiveness, pay for multifunctional services, diversify and improve the quality of life in rural areas. A consistent and strong modulation would have been necessary in this case, so that in a few years a real budget balance between the two pillars would have been established. As is well known, Agenda 2000 has been in this respect no more than a low profile compromise. The adoption of a more radical strategy as that suggested by the Buckwell Report was postponed. The precariousness of the Agenda 2000 compromise was so evident that a Mid Term Review was scheduled for the year 2003; and this resulted in the Fischler reform. But, even in this case, the recalled three conditions, necessary to the SFP for being considered a transitory adjustment assistance were missing.

It is not a redistributive income support

It is often said that the SFP should be considered as a support to the farmer's income. Generally a transfer of public money is considered as an income support if it is aimed at alleviating the existing discrepancies in terms of personal (or family) income between social categories, that are considered unfair and unacceptable penalizations. The income support clearly has therefore a redistributive aim advantageous to those social categories that are considered the weakest. For this reason, its amount is generally correlated to the actual difference between the beneficiary's income and a comparable income level (higher for definition) inside or outside the same social group. Such a support is correlated therefore to some indicator of the actual redistributive need.

Moreover a maximum level of support should be introduced in relation to the level of the comparable income. It is moreover questionable if the most appropriate place for such a redistributive policy should be included in a sectorial (agricultural) policy. Poverty is a social problem of a general character, that should be tackled with social (and not sectorial) policies, in other words with policies targeted at all people who live in poor condition.

Moreover, for a long time the farmer's profession in Europe has by now caught up to a level of income similar or even better than that of other comparable professions. It would be therefore unacceptable and disqualifying to claim the necessity for an agricultural policy for these reasons. In fact the SFP do not have the characteristics of income support for redistributive purposes.

It is not a support to investments

The SFP cannot be considered a support for the agricultural enterprise development, finalized especially to alleviate the short term difficulties faced by farmers who undertake new strategies, that produce economic returns only in the medium-long term either. The recovery time of the investment in agriculture, as is well known, is often very long and the short term financial needs are particularly heavy, especially for new and small farms as well as young farmers, that during their start-up, have no real guarantees to offer. But in these cases, the support should be concentrated and selectively reserved for those farmers who actually possess those personal conditions (profession, age, factors availability) suitable for the undertaking of new entrepreneurial initiatives and commit themselves to invest and risk.

The procedures generally adopted under the measure a) of the pillar II are generally of the kind described here. Also the measure of the setting up of young farmers, especially if combined with a business plan as a selection device, is of this kind. But there are no similar conditions in the case of the SFP. The SFP cannot even be included in this category.

What is then the SFP?

The SFP cannot be defined as any of the afore-mentioned typologies. What is then its economic nature? The question to answer is not to understand what can be done with such a payment, but to which main purposes it is actually devoted and what does the taxpayer receive in exchange for bearing its burden. In this light, the SFP is first of all an "aid to the past". It is in fact finalised to reconstruct the income for those people who, otherwise, would have been penalized by the redistributive effects of the Fischler reform. The SFP, in fact, one should remember, is a kind of support distributed (before as well as after the reform) in a discriminatory way across Europe favouring mostly the centre, the plains and not the hilly and mountainous regions, some products and not other ones and have benefited more standardized production than that of quality and the agricultural services both for the market and with multifunctional character.

That uneven distribution was the origin of one of the most severe criticisms of the old CAP and of the claim for reform, but, with the Fischler reform, it has substantially been confirmed. This paradox was highlighted again by a recent study of the Commission: 85% of CAP direct aid is received by only 23% of European farmers.

The adopted solution has bought the consensus on the reform, convincing the principal beneficiaries of the old CAP to accept the Fischler reform and stop the radical opposition adopted in the past to any significant changes. At the same time the solution adopted was so expensive that a large part of the available budget dried up and allowed only a very modest redistribution to the advantage of more consistent objectives and more effective policies.

As is well known, the right for the farmer to receive the SFP is linked to the condition of having been a beneficiary of the direct payments in the years 2000-2002. Tied, as the SFP is, to backward looking status conditions and not to forward looking behaviour and strategies, the SFP reveals its very nature as being an economic rent, rather than an incentive. Its beneficiaries, in fact, have no substantial commitments to counterbalance the right to receive it, while for the farmers that have no

right to receive it (for the simple reason that they did not receive any direct payments during the years 2000-2002) it constitutes a supplementary direct or indirect cost.

It is a direct and explicit cost which must be faced by all the farmers (the young above all) that invest in either opening a new farm or enlarging the existing one and engage themselves in plans and projects for the future. In order to make available the eligible land both for sale and rent, the person entitled with the right to the SFP claims its actualisation. Therefore the old farmer who stops farming receives a supplementary payment paid by the new farmer who enters the business or continues enlarging his farm.

The indirect cost comes from the overwhelming budget absorbed by the SFP. Its amount is so huge as to hinder the transfer of funds to the pillar II through a suitable modulation (as one may remember, the initial proposal for the modulation in the Mid Term Review was fixed to 20%, but it was reduced during the negotiation to only 5%). Presently, due to the fact that the EU is going through a political crisis (after the French and Dutch referenda), the exorbitant and rigid weight of the SFP (until the year 2013) falls on to the pillar II emphasizing the effect of the financial decrease of funds due to the new financial perspectives. The implicit cost consists of a lack of adequate funds for the rural development policy: the policy aimed at reorienting the old CAP to a future perspective that is more coherent with the other structural EU policies. Those who hoped to receive a larger support from that policy, will either have to settle for a reduced support or not to starting up their development project at all.

Some final remarks

Some conclusive remarks can be derived from the analysis carried out here.

- 1) The first, broadly speaking, concerns the need for more light to be thrown on agricultural policy objectives. The SFP, central axis of the CAP after the Fischler reform, that absorbs the bulk of the budget reserved to the CAP, can not have a hybrid and undetermined nature. The European tax payer must know clearly, as well as for all the other policies, for which precise objectives he is called upon to bear its burden. These objectives, on the other hand, should be collectively shared. The recurrent charge to the decoupled payments: "farmer are paid for doing nothing", could lead to new indiscriminate cuts on the CAP budget in 2013, if not early in 2008-9. These criticisms are neither new nor occasional: the Commissioner for the budget, Mrs. Grybauskaitė, starting up in office said the CAP is "*antiquated and obsolete* and swallow a portion of EU resources out of proportion to its real value", the Sapir report proposed reducing the CAP to 5% of the EU budget.

It is obvious that criticizing the present support to agriculture does not mean that one wants the abandonment of agriculture, but simply to underline that agriculture and rural development deserve much more and much better than the present CAP, in terms both of economic efficiency and social justice.

- 2) Undoubtedly, compared to the previous directed payments, the decoupling of the Fischler reform has generated a positive "competition effect". If only for this reason, should it be appreciated and defended. But its merits cannot hide the main fault of the SFP: its economic nature is that of an "aid to the past". Its main scope being to restore the distribution of the CAP pre-reform. Its character of *economic rent* is evident: it consists of an acquired right, not conditioned by substantial obligations (except for the good maintenance of the eligible hectare). The amount of the SFP anyway has no substantial correspondence with the cross-compliance commitments.

Naturally, those farmers who add the two conditions: being entitled for the right to the SFP and having a long term strategy, can also use the SFP as a support to their income and an aid to farm adjustment towards competitiveness. But if this were the principal objective, why the European Council did not move many more funds to support the business plans under the pillar II, accompanying them with the introduction of "transitory adjustment assistance" measures, as proposed in the Buckwell Report? It would have been a more efficient,

effective and fair solution. The distribution of the support would have been actually concentrated on strategies for the future.