

HOUSE OF LORDS

European Union Committee

13th Report of Session 2008–09

The Review of the Less Favoured Areas Scheme

Report with Evidence

Ordered to be printed 19 May 2009 and published 4 June 2009

Published by the Authority of the House of Lords

London : The Stationery Office Limited
£price

HL Paper 98

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We would like to take the opportunity to thank all our witnesses for their submissions to our inquiry.

NOTE: References in the text of the report are as follows:

(Q) refers to a question in the oral evidence

(p) refers to a page of written evidence

(para) refers to a paragraph of written evidence

SUMMARY

The Less Favoured Areas scheme is intended to channel aid to farms in areas afflicted by natural handicaps, and forms part of the rural development component of the European Union's Common Agricultural Policy (CAP). The scheme is driven by the view that there are public benefits to be secured by promoting the maintenance of farming activity in disadvantaged areas where land might otherwise be abandoned.

In this report, we explore the review of the Less Favoured Areas (LFA) scheme that is currently underway, prompted by a damning Court of Auditors' report on the implementation and oversight of the LFA scheme published in 2003. We focus in particular on the European Commission's emerging proposals for how the most commonly used category of Less Favoured Area should be designated, and how the payment system should be adapted in light of the provisions of the 2005 Rural Development Regulation, which has now become the legal underpinning for the measure.

We see a distinctive role for the Less Favoured Areas scheme, which by contrast to the main element of the CAP, Single Farm Payments, offers a means of channelling support in a much more discriminating way, to those farms that are least able to earn compensation from the market, yet contribute most to the maintenance of the landscape.

We welcome the Commission's intention to introduce a common set of biophysical indicators to be used in identifying Less Favoured Areas. We note, however, that it is not yet clear whether the specific characteristics of the United Kingdom's maritime climate will be adequately captured by the proposed criteria.

We support the proposed move away from socio-economic indicators of disadvantage towards designations based purely on natural handicap, on the basis that the new Rural Development Regulation makes provision for more targeted and cost-effective ways of pursuing socio-economic goals in rural areas.

Our report also recommends the introduction of a common EU-level framework for eligibility criteria, whose focus should be on extensive farming systems, and WTO-compatibility, while ruling out criteria that are irrelevant to the objectives of the measure or impede mixed farming.

Like the Court of Auditors before us, we have been unable to draw firm conclusions about the effectiveness of the LFA scheme in meeting its objectives, and therefore call on the Commission and the Member States to assemble the evidence base with which the scheme's effectiveness as a mechanism for protecting the environment and the landscape might be assessed and kept under review.

Perhaps most importantly, we call for a prompt execution of the review. We believe that the deficiencies highlighted in the Court of Auditors' report cannot continue to be left unchecked, and emphasise that a successful review should lead to a more efficient allocation of LFA funds, benefiting not only the taxpayer, but also those farms most deserving of support under this scheme.

The Review of the Less Favoured Areas Scheme

CHAPTER 1: INTRODUCTION

The Inquiry

1. The aid scheme for farms in areas deemed “less favoured” forms part of the European Union’s Common Agricultural Policy, and dates back to 1975. It is based on the view that there are public benefits to be secured by promoting the maintenance of farming activity in marginal areas where land might otherwise be abandoned. From the perspective of EU Member States, it is a voluntary element of the Common Agricultural Policy (CAP), and unlike the bulk of CAP payments, it is co-financed from both national and EU budgets.
2. In 2005, the legal underpinnings of the Less Favoured Areas (LFA) scheme were overhauled as part of a wider reorganisation of rural development policy. Existing programmes and budget lines targeting rural development, including the LFA scheme, were drawn together into a single funding and programming instrument known as the European Agricultural Fund for Rural Development (EAFRD). The EAFRD supports projects across three strategic “axes”, as outlined in Box 1 below.

BOX 1

The EAFRD

The EAFRD provides financial support for actions under three headings or “axes”, with minimum spending requirements attached to each. Rules on co-financing rates (determining the relative financial contribution of the EU and the Member State) also apply.

Axis 1 of the Fund—on which a minimum of 15 per cent of allocated funds must be spent—aims to support measures designed to improve the competitiveness of the agriculture and forestry industries (e.g. restructuring holdings, improving human capital and product quality).

Axis 2 of the Fund—on which a minimum of 25 per cent of allocated funds must be spent—aims to support land management measures designed to enhance the environment and the countryside (e.g. agri-environment schemes, animal welfare commitments).

Axis 3 of the Fund—on which a minimum of 15 per cent of allocated funds must be spent—aims to support policies that target improvements in the quality of life in rural areas (e.g. basic services provision, rural heritage conservation) and promote economic diversification towards non-agricultural activities (e.g. tourism).

A minimum of 5 per cent of EAFRD funds are ring-fenced for LEADER initiatives across the three axes. Under the LEADER approach, local action groups can secure funding for local development projects.

3. During the course of the 2005 reorganisation, the LFA scheme was placed under Axis 2 of the EAFRD, and its objectives adjusted accordingly. The

Rural Development Regulation¹—that is, the legal instrument that set up the EAFRD in 2005—specifies that financial assistance offered under this axis shall support “the sustainable use of agricultural land”. Payments to farmers in areas with handicaps are identified as one way of promoting this objective. The Regulation stipulates that such payments should be paid annually per hectare, and “should compensate for farmers’ additional costs and income foregone related to the handicap”. Article 50 of the Regulation reformulates the basic criteria for designating certain categories of LFA.

4. At the time of this overhaul, however, the Council of Ministers (at which the governments of EU Member States are represented) failed to reach agreement on a system for classifying Less Favoured Areas that would reflect the new overarching objective of the policy (the sustainable use of agricultural land) and the new criteria for designation. It was therefore decided to delay the entry into force of the changes to the LFA scheme until 2010. In the meantime, the European Commission would be charged with undertaking a review of the implementation of the LFA scheme, and presenting proposals on how Less Favoured Areas should be designated in future, as well as how the payment system should be adapted, for adoption as a Council Decision.
5. Our inquiry sought to examine the Commission’s emerging proposals, as trailed in a consultation document published in the summer of 2008, and published in a Communication on 21 April 2009.² We took a particular interest in the extent to which the emerging proposals would address the criticisms levelled by the European Court of Auditors in its 2003 report³ on the LFA scheme, which provided the impetus for amending the legal framework underpinning the scheme.
6. Our report begins with a brief explanation of how the LFA scheme works at present, and an outline of the review currently underway. Chapter 2 examines the purpose of the LFA scheme and its relationship to other CAP instruments. Chapter 3 then turns to the content of the review, touching on biophysical criteria, eligibility criteria and the payment formula. In Chapter 4, we conclude by considering the timing of reform, and the arrangements for monitoring and evaluating the scheme. Chapter 5 presents a summary of our Conclusions and Recommendations.
7. The inquiry that led to this report was carried out by Sub-Committee D, whose Members are listed in Appendix 1. We received written evidence and took oral evidence from a range of witnesses, who are listed in Appendix 2. We are grateful to them all for their contributions. We make this report to the House for information.

How the LFA scheme works at present

Eligibility for Aid

8. There are currently several conditions for receiving aid under the LFA scheme: first, farms must be located in an area classified as Less Favoured and second, they must meet eligibility rules and thresholds, some of which

¹ Council Regulation (EC) No 1698/2005 of 20 September 2005 on support for rural development by the European Agricultural Fund for Rural Development (EAFRD)

² “Towards a better targeting of the aid to farmers in areas with natural handicaps”, COM (2009) 161.

³ Court of Auditors Special Report No 4/2003 concerning rural development: support for less-favoured areas, together with the Commission’s replies (OJ C151, 27.06.2003, pp 1–24).

are common across the EU, and some of which are set by Member States (a devolved matter in the UK). So while 58 per cent of the EU's Utilized Agricultural Area was classified as Less Favoured in 2005, less than half of the farms in those areas were receiving aid under the LFA scheme. The proportion of farms in LFA areas that receive aid varies widely across Member States: more than 90 per cent of farms in Less Favoured Areas receive aid in Ireland, Finland and Austria, while less than 10 per cent receive aid in Italy and around 15 per cent receive aid in Spain.

9. Council Regulation 1257/1999 lays down three mandatory EU-level eligibility criteria. Recipients must first, farm a minimum area (thresholds set by each Member State); second, undertake to farm in the Less Favoured Area for at least five years from the first payment of aid; and third, adhere to some basic land management requirements defined as Good Farming Practice.
10. In addition to these EU-level criteria, Member States apply a range of additional eligibility criteria, mainly at a national level but in a few instances (including the UK) also at the sub-national level. Examples include restrictions on farmers over 65 receiving aid, place of residence conditions, or requirements to keep livestock.

Designation of Less Favoured Areas

11. Under Council Regulation 1257/1999, an agricultural area may be classified as Less Favoured if it falls into one of the four categories listed in Box 2. The total proportion of agricultural area classified as Less Favoured varies widely from Member State to Member State, ranging from 1 per cent in Denmark to more than 98 per cent in Luxembourg.⁴ These proportions have also changed considerably over time in some Member States: between 1975 and 1998, the proportion of agricultural area deemed Less Favoured went up from 37 per cent to 56 per cent in Italy, and from 51 per cent to 70 per cent in Ireland. The Court of Auditors pointed out that this is suspect: “given that mountainous areas have not changed, the increases are all the more remarkable in view of the advances in soil improvement and varietal development.”⁵

BOX 2

Categories of LFA

- Areas subject to **environmental restrictions** (Art. 16)—characterised by limitations on agricultural land use imposed by Community environmental protection rules.
- **Mountain** areas (Art. 18)—characterised by a short growing season due to high altitude or by steep slopes at lower altitude.
- **Other** Less Favoured Areas (Art. 19)—characterised by poor productivity as a result of the natural environment which results in appreciably lower than average economic performance and a low or dwindling population predominantly dependent on agricultural activity.
- Areas affected by **specific handicaps** (Art. 20)—where farming needs to continue in order to conserve or improve the environment, maintain the countryside and the area's tourist potential or protect the coastline.

⁴ See Graph 2 in the Court of Auditors' 2003 report.

⁵ Court of Auditors' report, Para 8.

12. It is left to Member States to interpret the EU-level criteria that define the four categories of Less Favoured Area, with mixed results:
- (a) The EU-level criteria for identifying areas subject to environmental restrictions are clearly defined and Member States have interpreted them in a consistent and comparable way.⁶
 - (b) This is also true of the criteria for identifying mountain areas. However, these two categories together accounted for only around one-third of total LFA land in 2004–05.
 - (c) Around 66 per cent of LFA land has instead been classified into the “other” category. The Court of Auditors pointed out that the EU-level criteria for identifying this type of LFA are not sufficiently clear. Member States have consequently used a wide variety of indicators to give effect to the EU-level criteria for this category. These include 17 different indicators relating to the productivity of agricultural land, 12 different indicators for economic under-performance, and 3 different indicators for population.⁷
 - (d) “Specific Handicap” areas make up the rest. Member States have again resorted to a wide variety of indicators to give effect to the EU-level criteria, ranging from natural handicaps to security considerations (in parts of Cyprus). In Malta, the Institute for European Environmental Policy (IEEP) found that the entire agricultural land area had been classified as suffering from a specific handicap, but no attempt had been made to identify the specific handicaps facing particular areas.⁸
13. In its 2003 report on the LFA scheme, the Court of Auditors warned that the variation in indicators for classifying LFA areas may lead to disparities in treatment among beneficiaries. It recommended that the Commission should perform a complete review of existing LFA classifications, and develop a more appropriate set of indicators for identifying Less Favoured Areas that would be consistent and guarantee equitable treatment of beneficiaries.

Level of the aid payment

14. The level of aid should in principle reflect the degree of handicap facing the farmer, thereby acting as a compensatory allowance. Member States fix the specific level of aid per hectare within a range set at EU level. Levels of payment vary significantly across Member States, ranging from national average payments per eligible hectare of between €15 and €55 in Spain, Sweden, Poland and the UK, to payments of between €175 and €250 per eligible hectare in Austria, Finland and Malta. Within countries, payment levels may vary further, for example across different categories of LFA. The payment ceiling set at EU level may be exceeded in individual cases, provided that the average level of aid paid out by each Member State adheres to the limit. In an evaluation report prepared for the European Commission,

⁶ “An Evaluation of the Less Favoured Area measure in the 25 Member States of the European Union”, report prepared by the Institute for European Environmental Policy for the European Commission’s DG Agriculture, November 2006, Executive Summary, p.5.

⁷ See Annex II to the Court of Auditors’ report.

⁸ “An Evaluation of the Less Favoured Area measure in the 25 Member States of the European Union”, report prepared by the Institute for European Environmental Policy for the European Commission’s DG Agriculture, November 2006, p.64.

the IEEP highlighted payment rates of up to €800 per hectare on certain Austrian and Italian mountain farms, and Portuguese island farms.⁹

15. Payment levels are typically calculated in relation to a baseline—the absence of handicap—defined in most cases in terms of agricultural income. This is usually measured in relation to a norm, such as agricultural income in non-LFA areas in the same country, or by reference to previous LFA payment levels or historic income. In its evaluation report, the IEEP pointed out that there is no consistent European baseline for such calculations.

Where does the money come from?

16. The CAP rests on two “pillars”: Pillar I, out of which direct payments to farmers (Single Farm Payments) and market management measures are funded, and Pillar II, which supports rural development programmes. The bulk of CAP expenditure is allocated to Pillar I (see Table below). Pillar II is financed through the EAFRD.

TABLE

CAP Expenditure over the 2007–2013 Financial Perspective

Figures in billions of euros, based on 2004 prices	Total 2007–2013
Pillar I—Direct Payments and Market Support	293.105
Pillar II—Rural Development	69.750

17. Each Member State receives a fixed share of EAFRD funds to help finance its rural development policy. It must prepare a national plan specifying how it proposes to allocate those funds, based on domestic priorities. In drawing up their plans, Member States must respect certain minimum spending requirements: at least 25 per cent of each Member State’s share of EAFRD funds must be spent on measures under Axis 2 (see Box 1 above). However, whether or not they choose to spend some of those Axis 2 funds on an LFA scheme is up to each Member State. At present, all Member States of the European Union have chosen to operate an LFA scheme. However, England’s LFA scheme—known as the Hill Farm Allowance—is to be discontinued from 2010, and will be replaced with a new uplands strand to the Environmental Stewardship scheme instead.
18. All spending on rural development measures under the EAFRD must be co-financed according to fixed percentages, meaning that Member States must contribute national resources in addition to the funds provided by the EU. In 2003, the overall cost of the LFA scheme amounted to around €2 billion, of which around half was funded through the EU budget. This represented around one fifth of total rural development expenditure. However, the amount invested in the LFA measure varies widely across Member States: France, Finland and Germany allocated more than 30 per cent of their share of the EAFRD budget to the LFA measure, while Spain spent only 12 per cent of its share and Italy spent 7 per cent.

Division of responsibilities

19. The rural development plans prepared by Member States must be approved by the Commission before they can access EAFRD funds. Once plans have

⁹ Ibid, p.92.

been approved and are being implemented by Member States, the Commission records the expenditure declared each month by each Member State and reimburses it for the Community's share of the funding. The Commission is also responsible for monitoring and evaluation of rural development programmes, including the LFA scheme.

20. Member States are responsible for classifying Less Favoured Areas, designating the authorities responsible for drawing up rural development plans and implementing the measures contained therein (including the LFA scheme). Member States bear the primary responsibility for administration and control. Member States must also supply the Commission with the necessary data for it to monitor the implementation of rural development programmes.
21. In its 2003 report, the European Court of Auditors noted that since the entry into force of Regulation 1257/1999, the Commission no longer holds final responsibility for the validity of the classification of Less Favoured Areas, and described this as a "major weakness" in the Regulation. It also identified a number of weaknesses in Member States' management, control and reporting systems, which had knock-on effects on the monitoring that the Commission was able to undertake.

The current review of the LFA Scheme

22. A review of the LFA scheme has been pending for some time. The European Court of Auditors first raised concerns about oversight of the scheme's application, and in particular the validity of classification decisions, as far back as 1990. In response, the Commission began a review of LFA classifications in 1993, as part of which it asked Member States to provide justification for their classification decisions. However, some Member States submitted incomplete data, inaccurate data, or no data at all. In its 2003 audit, the Court found that the Commission had been faced with serious opposition from Member States when it attempted to examine the continuing validity of the data underlying LFA classifications. The Court could not find evidence that the review was properly completed.
23. When the new Rural Development Regulation was introduced in 2005, the opportunity was seized to address some of the concerns raised in the Court of Auditors' report by redrafting some of the provisions relating to the LFA scheme. Two changes of particular significance were:
 - (a) *The redrafting of the criteria for designating "other" Less Favoured Areas to include only natural handicaps:* Article 19 of Regulation 1257/1999 stipulates that areas falling into this category should exhibit land of poor productivity, economic performance lower than the average, and a low or dwindling population predominantly dependent on agricultural activity. The 2005 Regulation replacing it removes the socio-economic criteria and instead stipulates that these areas must be "affected by significant natural handicaps, notably a low soil productivity or poor climate conditions and where maintaining extensive farming activity is important for the management of the land".¹⁰

¹⁰ Council Regulation 1698/2005, Art. 50–3(a).

(b) *The inclusion of a payment formula in place of payment guidelines:* Article 15 of the 1999 Regulation stipulates that compensation payments should be fixed at a level which is sufficient to make an effective contribution to compensation for handicaps but should avoid overcompensation. Article 37–1 of the 2005 Regulation replacing it stipulates that payments should “compensate for farmers’ additional costs and income forgone related to the handicap for agricultural production in the area concerned.”¹¹

24. However, as was noted earlier (paragraph 4), the Council of Ministers decided to postpone implementation of these changes until after 2010, and asked the Commission to take the matter forward by presenting proposals on how Less Favoured Areas should be designated and how the payment system should be adapted in light of the new provisions in the Rural Development Regulation.
25. The Commission published a consultation document outlining options for reform in the summer of 2008.¹² A Communication followed in April 2009, in which the Commission presented a set of biophysical criteria that might be used to designate Less Favoured Areas in the “other” category in future (see Box 3 below).¹³ It suggested that Member States be invited to simulate the application of the biophysical criteria on their territory, and send the resulting maps back to the Commission within six months. The Commission would then use those maps to assess how best to adapt the LFA designation system and to prepare a legislative proposal to that effect in due course.
26. In its Communication, the Commission also noted that eligibility rules applied after the process of designating Less Favoured Areas, but observed that many of the eligibility rules currently used by Member States are inessential to the main objectives of the measure. It suggested that their consistency with the objectives of the scheme and with the international commitments of the EU could be enhanced, and pledged to examine this aspect of the scheme further when preparing the legislative proposal. The latter is expected to be published no earlier than 2010
27. The Commission has indicated that LFA payments will in future be called Natural Handicap Payments. To avoid confusion, however, this report continues to refer to the LFA scheme and LFA payments.

¹¹ Council Regulation 1698/2005, Art. 37–1.

¹² The consultation document is available here:
http://ec.europa.eu/agriculture/consultations/lfa/consultationdoc_en.pdf

¹³ Communication from the Commission “Towards a better targeting of the aid to farmers in areas with natural handicaps” of 21 April 2009, COM (2009) 161.

CHAPTER 2: THE ROLE OF THE LFA SCHEME

Purpose of the LFA Scheme

28. The formal objectives of the LFA scheme have changed over time, following each redrafting of the legislation on which the scheme rests. The provisions of the 2005 Rural Development Regulation do, however, appear to reorient the scheme more dramatically than the changes that had gone before. By being placed under Axis 2 of that Regulation, the overarching objective of the LFA scheme became the improvement of the environment and the countryside. Article 36(a) stipulates that the measure should target the sustainable use of agricultural land. Meanwhile the provisions relating to the designation of “other” Less Favoured Areas specify that support should be targeted at areas “where maintaining extensive farming activity is important for the management of the land”.¹⁴
29. Among our witnesses, however, we found competing interpretations of the purpose of extending aid to farmers in Less Favoured Areas.

Witnesses' Views

30. Some witnesses, including the European Commission and the UK Government, regard the maintenance of farming activity in some disadvantaged areas as instrumental to the delivery of certain environmental and landscape benefits, and justify public aid accordingly.
31. The European Commission suggested that the role of LFA payments was to allow farmers to continue farming under difficult circumstances (due to natural handicaps) and in doing so to maintain land management and the countryside (Q 32). The UK Government warned that while the LFA measure is often perceived as providing compensatory payments similar to Pillar 1 support payments, the scheme is an Axis 2 measure, and should therefore be targeted at maintaining and promoting sustainable farming systems that deliver environmental and landscape benefits that would not otherwise be provided by the market. Farmers should not be paid “simply for economic disadvantage” (Department for Environment, Food and Rural Affairs Memorandum, p.163, Q 1).
32. The Royal Society for the Protection of Birds (RSPB) suggested that the LFA scheme has a unique role to play in supporting the kind of extensive, livestock-based farming systems that produce a range of environmental public benefits, such as habitats for wildlife, and environmental services like water catchment and carbon storage (Q 93). On behalf of the English National Parks Authorities Association (ENPAA), Peter Barfoot emphasised the importance of continued land management for the uplands landscape, whose value to the tourism business in the National Parks should not be underestimated (Q 94).
33. By contrast the farming unions (e.g. Farmers’ Union of Wales Memorandum, p.16, Para. 51), some other Member States (e.g. Poland Q 296, Bulgaria Q 394, Finland Q 466), and some of the devolved administrations (Scottish Executive Memorandum, p.149, Paras. 10.1–10.2; Welsh Assembly Government Memorandum, p.208, Q 1) view the LFA

¹⁴ Council Regulation 1698/2005, Art. 50–3(a).

scheme as a means to support farming activity in disadvantaged areas in return for socio-economic, as well as environmental, benefits to rural communities and the wider public. The prevention of rural depopulation was the socio-economic objective most widely cited by our witnesses. From this perspective, the primary purpose of the LFA scheme is to contribute to the financial viability of farms in disadvantaged areas, so that they can continue providing the desired public benefits as a by-product of their farming activity.

34. NFU Scotland (NFUS) noted that delivery of wider non-market benefits is dependent on active land management, which will only continue if the core agriculture business is viable. It took the view that LFA support is “essential to ensuring continued viability, by off-setting the real costs of farming in disadvantaged areas and thereby enabling the delivery of a host of rural development benefits” (NFUS Memorandum, p.26, Para. 9; see also Peter Morris, National Sheep Association, Q 137). The National Farmers’ Union (NFU) argued that LFA designation allowed Member States to channel support to areas facing “the harshest farming conditions in Europe”, yet where farming is “central to maintaining food production, the landscape, traditional skills and preventing depopulation and land abandonment”. More specifically, the NFU viewed the scheme as a mechanism for sustaining characteristic hill farming systems and the public benefits of farming these areas (Memorandum, p.19, Paras 8, 10, 11). Dai Davies, President of NFU Cymru, warned that individual public benefits could not be targeted in isolation, so that trying to keep people in the hills, trying to keep villages in the hills, and trying to keep schools open in certain marginal areas all have to be seen as inter-connected (Q 80).
35. The IEEP observed that a gap had arisen between the evolution of the policy as expressed in the 2005 Rural Development Regulation and how it is perceived by beneficiaries on the ground (Q 188). It argued that the purpose of this particular scheme is no longer socio-economic, and that keeping people on the land is no longer part of the logic of the measure. Instead, the LFA scheme should be viewed as an environmentally-driven measure, aligned with the new rural development package, which is less concerned with the number of farmers, and more concerned about the type of agriculture to be supported, ensuring that it is sustainable and delivers public goods in return for the money spent (QQ 188–191). It pointed out that there are other rural development measures available that target the objective of keeping people in rural areas and maintaining a dynamic rural economy much more precisely (Q 215).

Committee’s Views

36. We endorse the European Commission’s stance on the purpose of support for farms in Less Favoured Areas: **payments should help farmers in marginal areas to continue farming where their farming activity generates public benefits in the form of positive impacts on the environment and the landscape.**
37. We emphasise the importance of continuing to assess the public benefits obtained in exchange for this type of aid: society does not owe unconditional support to farmers wishing to farm in areas affected by natural handicaps. **Indeed, we anticipate that as climate change begins to take its toll on parts of Europe, support may need to be reassessed.** In some instances, currently non-handicapped areas may require additional support, while in

other instances, for example where water scarcity becomes particularly acute, land may become so severely handicapped that support should be withdrawn.

38. **We are conscious that by maintaining farming activity in place in marginal areas, the LFA scheme also makes a de facto contribution to preserving food production capacity, which could become increasingly important if climate change reduces production capacity elsewhere.**
39. We recognise that farming activity in marginal areas often brings social, economic and cultural benefits to local communities and the wider public. **However, measures available under the other axes of the Rural Development Regulation—see Box 1 above—offer more targeted and cost-effective ways of addressing socio-economic objectives in rural areas.**
40. We also consider it important to recognise that neither the LFA payment nor the wider package of financial aid available to farmers in Less Favoured Areas will necessarily be sufficient to prevent a decline in farming activity in marginal and remote areas of the EU. LFA payments may exert a moderating influence, but would-be farmers' career choices are likely to be influenced by cultural and lifestyle factors as well as economic incentives. **We view this as an emerging policy challenge that merits consideration as part of the wider review of the CAP post-2013.**

Relationship to other CAP instruments

41. The role of the LFA scheme must be considered in context: the measure is one among a suite of policy instruments available under the Common Agricultural Policy. We asked our witnesses to set out what they saw as the distinction between the LFA scheme and other, related CAP instruments, notably Single Farm Payments under Pillar I, and agri-environment schemes under Pillar II.

Witnesses' Views

42. There was considerable consensus among our witnesses that the LFA scheme should not overlap with agri-environment schemes: aid recipients should not be asked to deliver environmental benefits over and beyond basic land management obligations. The European Commission emphasised that the LFA scheme should in principle offer compensation to farmers operating under more difficult circumstances than a normal farmer in a region which is not handicapped. Although the scheme is driven by environmental objectives, it must not necessarily include any specific requirements to respect additional environmental obligations (Q 32). Indeed, the Commission warned that if this were to be the case, LFA farmers would be put at a disadvantage relative to farmers in non-handicapped regions (Q 34). The RSPB and the IEEP seconded this, arguing that payments made through the LFA scheme should simply seek to retain the type of land management that is already in place (Q 120 and Q 217).
43. Several witnesses argued that LFA support should be viewed as the underpinning for agri-environment schemes in disadvantaged areas: without LFA support, continued land management might be jeopardised, and without continued land management, the authorities would not be able to

commission the delivery of additional environmental services from farmers through agri-environment schemes. The Scottish Executive, for example, argued that “it is only through sustaining farming and crofting activity and by retaining land managers in Less Favoured Areas that there can be effective uptake of agri-environment measures” (Memorandum, p.149, Para. 10.2). The Scottish Crofting Foundation (SCF) echoed this view, casting the LFA as “the instrument which maintains that level of activity upon which you can then build more targeted agri-environment responses for specific habitats” (Q 155). The Welsh Assembly Government also concurred (Memorandum, p.208, Q 1).

44. The relationship between Single Farm Payments under Pillar I and the LFA scheme appears to be more complex. NFU Scotland saw LFA payments as “more akin to a Single Farm Payment, more like a Pillar I payment” than other rural development measures because of their income support function, thus bridging the gap between the two Pillars of the CAP (QQ 47, 57). The European Commission offered a similar interpretation, presenting Single Farm Payments as an income support instrument, and LFA payments as a hybrid, offering compensation to farmers for operating in more difficult regions where, for environmental reasons, it is considered important to maintain farming activity (Q 32). The SCF stressed that in the most marginal areas, the most cost-effective way of maximising returns from the Single Farm Payment would be to cease doing anything at all beyond meeting minimum cross-compliance conditions.¹⁵ It argued that LFA payments should target these types of farming systems, where it would otherwise be uneconomical to continue farming actively, but where it is deemed important to preserve such activity for other reasons (Q 156).
45. A number of witnesses (RSPB, Q 97; ENPAA Q 105; SCF Q 156) pointed out that where Single Farm Payments are calculated on the basis of production during a historic reference period, farms in disadvantaged areas—which are typically less productive—receive lower payments than their counterparts in non-LFA areas. Those farms then become proportionately more reliant on LFA support as a means of topping up their income. This can be exacerbated where the pattern of LFA payment distribution maps onto the pattern of Single Farm Payment distribution, as some witnesses suggested was the case in Scotland. The RSPB argued that while one would expect a pattern of LFA payments that was the reverse of that for Single Farm Payments in historic-based systems—as the former rewards and the latter penalises productive disadvantage—the two maps in fact mirror each other in Scotland (Q 96). The SCF also raised this issue, warning that LFA payment distribution in Scotland “does not sufficiently support the most marginal farms in the most difficult areas” (Q 138).
46. Meanwhile the IEEP suggested that the cross-compliance conditions¹⁶ attached to Single Farm Payments tend to be more onerous for farms in Less Favoured Areas, for three reasons: first, their profit margins are lower; second, they tend to be livestock farms and both types of cross-compliance

¹⁵ In order to be eligible to receive their full Single Farm Payment, farmers must meet a number of Statutory Management Requirements (SMRs) and maintain their land in good agricultural and environmental condition (GAEC). SMRs reflect the provisions of relevant EU legislation. GAEC is defined by each Member State, based on a common EU-wide framework. Taken together, SMRs and GAEC are the two elements of cross compliance.

¹⁶ See footnote 15 above.

conditions bear slightly more heavily on livestock farmers than on arable farmers; and third, they tend to be more extensive and are therefore more susceptible to scrub invasion which could lead to breaches of cross-compliance (Q 217).

Committee's Views

47. The evidence we received suggests that LFA payments are partly being used to plug a gap created by the way in which Pillar I subsidies are delivered. The productive potential of a holding is either disregarded or, in historic-based systems, positively rewarded. Single Farm Payments also fail to reflect variation in the magnitude and significance of the public benefits delivered by continued farming activity in different settings. **For these reasons, we see a distinctive role for the Less Favoured Areas scheme, which offers a means of channelling support in a much more discriminating way, to those farms that are least able to earn compensation from the market, yet contribute most to the maintenance of the landscape.**

CHAPTER 3: THE CONTENT OF THE REVIEW

Designation criteria

48. The need to review the existing classification of Less Favoured Areas was at the heart of the Court of Auditors report on the scheme. In that report, the Court argued that the Commission should develop, in close collaboration with the Member States, a more appropriate set of indicators for identifying Less Favoured Areas that would be consistent and guarantee equitable treatment of beneficiaries.¹⁷
49. The Commission has proposed common biophysical criteria (see Box 3), with specific minimum thresholds applicable across the EU, which Member States would use to identify areas facing natural handicaps. In a first stage, an area would be designated as disadvantaged if at least 66% of its active agricultural land meets at least one single criterion at the fixed threshold. For example, an agricultural area presenting a slope above 15% would qualify, disregarding its other soil-climate characteristics.
50. By the end of October 2009, Member States will be required to have undertaken a simulation exercise involving the mapping of the areas that, according to the proposed criteria, would be designated as facing a natural handicap. This will allow the Commission to assess more comprehensively the possible impact of the proposals on designation criteria and to adjust them accordingly ahead of the publication of a new draft legislative framework.
51. It is further proposed that Member States (or the appropriate authorities depending on constitutional arrangements) then fine-tune the designation to ensure that only those areas where natural handicaps are actually affecting agriculture are designated as Less Favoured Areas. This second step would remove from the eligible areas those areas where the handicap has been overcome, based on the availability of irrigation systems, drainage control systems and production-related indicators above a certain ceiling, e.g. the average yield as compared to the national average or the average of relevant neighbouring regions.
52. This would be a move away from the current position, in which a wider range of designation criteria are tolerated, including socio-economic criteria such as economic performance and population density. The change would be in line with the 2005 Rural Development Regulation¹⁸ (see para. 23 above).

BOX 3

The proposed common biophysical criteria

Climate

- Short growing period due to low temperature
- Periods of at least 10 consecutive days with temperatures of 35°C or over.

Soil

- Poorly drained soil (areas waterlogged for a significant part of the year)

¹⁷ Court of Auditors Special Report No 4/2003

¹⁸ Council Regulation (EC) No 1698/2005

- Over 15% of clay, silt, sand, organic matter or coarse material in top soil, or boulder(s) within 15cm of the surface
- Short depth from the soil surface to hard rock
- Presence of salts, exchangeable sodium and gypsum in the topsoil

Soil and Climate

- Soil-moisture balance criterion: Applies if a lack of soil moisture limits crop growth

Terrain

- A slope greater than 15%

Further details on the criteria are available in the Technical Annex of the Commission's Communication¹⁹

Witnesses' Views

The principle of common biophysical criteria

53. The Commission noted that the Court of Auditors had criticised the system of delimiting Less Favoured Areas as exhibiting “a lack of coherence, comparability and of transparency”. The revised indicators should therefore be more transparent, based on scientific evidence, and more coherent, while allowing Member States the possibility to adapt them to their own circumstances (Q 2).
54. Among our witnesses, there was a general acceptance that some form of common criteria would be useful as a way of ensuring fairness and consistency (Scottish Natural Heritage para 10; DEFRA Q 568; Welsh Assembly Government para 2; COPA-COGECA Q 358; Finland Q 470). The Czech Presidency emphasised that, in adopting the Rural Development Regulation, Member States had acknowledged that there was a need for clear criteria and that these should correlate to natural handicaps (Q 435).
55. A minority of witnesses were sceptical about the concept of common biophysical criteria. The Farmers' Union of Wales and NFU Cymru both argued that Member States should choose their own set of criteria, which would then be presented to the Commission for assessment (Q 66).
56. Other witnesses were supportive in principle, but called for increased flexibility. Poland, for example, emphasised that each Member State should be able to determine for itself which criteria it wanted to apply, given differing climates and soil quality (Q 306).
57. The IEEP considered the proposed biophysical criteria to be accurate proxies of natural handicap but suggested that they were not sufficiently precise to identify those areas where environmental benefits are most prevalent (Q 220). It suggested that one of the advantages of clear biophysical criteria was to establish a transparent link between LFA payments and the severity of the handicap (Q 238).
58. Several witnesses were concerned that the availability of data across all Member States in order to apply the criteria may be a problem (IEEP Q 222;

¹⁹ SEC(2009)449 21.04.2009

Macaulay Institute, para 3; Scottish Rural Property and Business Association para 11; Country Land and Business Association para 3.4). The IEEP referred specifically to data issues that the IEEP had encountered in a recent report on the conservation of agricultural soils across Europe. Among the representatives of Member States' governments from whom we took evidence, only the Czech Republic expressed particular concern that collation of data for the purposes of mapping the Less Favoured Areas would be a problem (Q 448).

59. The European Commission took the view that the data are available in many cases, but that they are not always maintained in a consistent way or in a framework, suggesting that they “must be put together in a systematic way and then integrated into a coherent approach” (Q 20). The Commission was confident that Member States would co-operate in providing as much data as possible within the six month deadline it has set (Q 328). The Swedish government, on the other hand, warned that there is no consensus among Member States on the need to deliver the data to the Commission (QQ 530–532).
60. The UK Government stressed the importance of retaining regional flexibility to designate land as LFA at land parcel or (sub-) holding level where desired, and where the data to do so is available, rather than restricting designation to a higher administrative level or ward (Memorandum, p.164, Q 3) . The Scottish Executive also underlined this point (Memorandum, p.150, para. 10.10).

UK-specific concerns

61. Most of our UK witnesses pressed for the inclusion of biophysical criteria that would capture the impact of cool, wet maritime conditions. The ENPAA warned that Europe-wide criteria “could result in some very, very strange anomalies in England and Scotland and Wales because of our unique oceanic-type climate”, and so there may need to be additional country-based criteria (Q 117). Scottish Natural Heritage noted that the criteria in Scotland ought to relate to the climate (cool temperatures, a short growing season and high rainfall) and the soil (poor in nutrients, often naturally waterlogged and susceptible to peat erosion) (Memorandum, p. 200, para 12).
62. The Macaulay Land Use Research Institute, UK Government and Scottish Executive argued that the criteria should include “field capacity days”, a measure which reflects the wetness of the climate and the period of time that the field is at field capacity (the maximum amount of water that a particular soil can hold). This, in their view, would more effectively take into account the specificities of the UK and Irish maritime climate than the soil-water balance criterion proposed by the Commission (Memorandum, p.193, para 6; QQ 577, 553).

Fine-tuning of LFA designation

63. In considering how to take into account some of the national and regional specificities across the EU, there was broad agreement among our witnesses that national and regional authorities should be permitted a degree of fine-tuning of the LFA designation resulting from application of the common biophysical criteria (FUW, Q 66; National Beef Association, Q 159; NFU Cymru, para 11; NFU, para 17; Scottish Natural Heritage, para 11; National Sheep Association, pages 2–3; Welsh Assembly Government, Q 2; Commission, Q 14; IEEP, Q 222; COPA-COGECA, Q 358).

64. The Commission explained that there are circumstances where the handicap does not really lead to a difficulty in production because it has been overcome by technical progress or other forms of intervention, such as irrigation or drainage. Member States should therefore have the option to verify whether the natural handicap is still manifest, based on a framework set out in the legislation (QQ 13–14). Similarly, the UK Government identified the need to ensure that funding is provided to the right farmers in the right areas where there is severe disadvantage, but also where the environmental benefits and public benefits are being delivered (Q 579). They argued that fine-tuning should only be used to exclude areas that would otherwise be designated as LFA, not to include additional areas (QQ 577–579).
65. Some witnesses took the view that the fine-tuning should take place at a lower administrative level than the Member State (COPA-COGECA, Q 358; Germany, Q 262; DEFRA, Q 576). The Welsh Assembly Government emphasised the importance of sufficient regional flexibility to take into account differences in natural disadvantage (para 2).
66. The IEEP warned of the danger of “a whole suite of additional criteria” ensuing from the fine-tuning process (Q 222). The Bulgarian government stressed the importance of a level playing-field, suggesting that any discretion given to Member States in terms of taking on board the specificity of the country was acceptable as long as it did not distort the competitive environment (Q 398). In a similar vein, the UK Government emphasised the importance of monitoring: “we would certainly see a role for requiring the Commission or some independently verified scrutiny elsewhere of Member States’ designations, of the rules, and the payment rates” (Q 601).
67. Indeed the potential importance of monitoring was demonstrated by the rather disparate range of views on how biophysical criteria might be fine-tuned. The Government argued that the UK should be able to take into account summer rainfall, for example (Q 576), while COPA-COGECA considered that the fine-tuning should involve socio-economic considerations (Q 361). According to the Minister, the UK Government will be working with the Commission to resist the bolting on of socio-economic factors (Q 584).

Omission of socio-economic criteria from the set of indicators

68. A final consideration brought to the Committee’s attention was the proposed omission of socio-economic criteria from the set of indicators used to identify Less Favoured Areas. The Scottish Executive and the Commission pointed out to us that the new Rural Development Regulation demands an exclusive focus on natural handicaps, as Member States can draw on measures under the other two axes of the Regulation to target socio-economic objectives (QQ 10, 554). The Commission also argued that while natural handicaps were immutable, socio-economic handicaps such as remoteness or population density could change over time, requiring regular review of LFA designations (Q 10).
69. The UK Government were categorical in their rejection of the LFA scheme as a socio-economic tool: “The whole basis of LFA ... is that it is to reward those wider benefits that come from farming in disadvantaged areas, not to tackle issues around socio-economic factors”. Those, the Government considered, can be tackled in other ways (Q 580). The Swedish government

- noted the view of Swedish farmers that there is a need for a change in the criteria for payment “to make it clearer that this is a payment to compensate for natural handicaps and not for socio-economic reasons. We have other policy areas to deal with that” (Q 515).
70. The RSPB rejected the notion that socio-economic factors such as fragility and distance from markets and labour should be factored in, arguing that these were “all well and good when the support was there to deliver food production” (Q 118). But if the objective was to deliver a much wider range of public benefits, the RSPB did not see the relevance of socio-economic criteria. Scottish Natural Heritage considered that the exclusion of socio-economic criteria should lead to increased transparency and consistency (para 10).
 71. Other witnesses, on the other hand, considered that socio-economic indicators still had a role to play in identifying disadvantaged areas. The FUW argued that socio-economic criteria ought to be maintained because alternative economic options for farmers were often limited in less favoured areas. NFU Cymru disputed the Commission’s view that socio-economic factors change, arguing that key factors such as distance from market do not alter, an argument that was supported by the Scottish Crofting Foundation (Q 162). Remoteness was also an issue of concern to the National Sheep Association (Q 163) and to the European Forum on Nature Conservation and Pastoralism, which argued that distance should be seen as a physical or natural disadvantage (para 35).
 72. The Scottish Executive made the point that, although it too attaches importance to socio-economic indicators, the proposed biophysical indicators often serve as an adequate proxy because natural and socio-economic handicaps (such as remoteness and population density) tend to be correlated (Q 554). Finland also anticipated that it would not need to draw on socio-economic criteria as the same objective is achieved by using biophysical criteria (QQ 472–3).
 73. A distinctive perspective was provided by the Bulgarian government, which explained that Bulgaria was content with the omission of socio-economic criteria because it was not saddled with the “burden of the past”. Bulgaria’s LFA scheme only started in 2007 and deliberately omits socio-economic designation criteria because it was already anticipated that these would disappear (QQ 379, 420).
 74. A final twist in the debate was rehearsed by several of our Scottish witnesses. It was anticipated that application of the biophysical criteria could lead to the exclusion from the scheme of parts of Scotland, such as areas around Caithness and Orkney, which continue to face the permanent disadvantage of being situated far from their markets, and whose land, while of poor quality, is of less poor quality than most other land in Scotland (NFUS, Q 68). One solution, advocated by the NFUS, would be to apply socio-economic criteria (Q 68). Another option, highlighted by the NFUS, Scottish Executive, Scottish Crofting Foundation and Scottish National Heritage, would be to explore the possibility of using Article 18 of the Rural Development Regulation to designate mountain areas and Article 20 to designate islands as areas with specific handicaps (QQ 69, 555, 159 and SNH Memorandum, p.200, para 10). Whilst this would appear to solve the potential problem for Orkney, it might not be sufficient to capture all areas currently designated as LFA. The Scottish Executive also emphasised that its

budget resources, rather than the legislative framework, were likely to be the limiting factor (Q 556).

Committee's Views

75. The Court of Auditors was strongly critical of the existing designation system which has led to a proliferation of criteria across the European Union. In order to provide consistency and transparency, **a common set of biophysical indicators to identify disadvantaged areas based purely on natural handicap is welcome.**
76. The European Union is, however, geologically and meteorologically diverse, a diversity which leads to a range of handicaps that must be adequately captured in the common set of criteria. **The criteria proposed by the Commission in its Communication provide an adequate basis for Member States to map the areas with natural handicaps across the EU. When assessing the maps that result, it will be critical to examine whether the specific nature of the UK and Irish maritime climate is adequately captured by the proposed criteria. At that stage, it may be necessary to press for the inclusion of additional criteria such as field capacity days or a suitable proxy.**
77. The establishment of indicators and the requirement to map is meaningless, however, without the appropriate data. While some Member States may have all of the necessary data to hand, we note that extra efforts may be required of others to ensure that the mapping can be completed within the Commission's deadline. **We recommend that the Commission pays careful attention to the availability of data in each Member State and offers assistance to Member States where necessary. Mapping down to land parcel level should be encouraged where such data is available, as this will facilitate the very targeting of aid that the review is intended to promote.**
78. Diversity of national and regional circumstances is such that it will be necessary to fine-tune the designation that results from application of the common biophysical criteria, but we see a danger that Member States may seek to use the fine-tuning process to replicate existing LFA designations. **We therefore endorse the approach advocated by the UK Government, whereby national and regional authorities would be permitted to fine-tune designations only in order to exclude areas where handicaps have been overcome.**
79. **We see a role for the Commission in monitoring this process, and ensuring that the criteria used for fine tuning are related to the objectives of the scheme as laid down by the 2005 Rural Development Regulation.**
80. We recognise that in many parts of the EU, the LFA scheme is still used to pursue socio-economic objectives. It is our view, however, that the policy levers available under the other axes of the EAFRD—and indeed under other EU, national and regional schemes—are better suited to that task, and that the LFA scheme's implementation must be brought into line with its formal objectives. **We consequently support the proposed move away from socio-economic indicators of disadvantage towards designations based purely on natural handicap.**

Eligibility criteria

81. Receipt of aid is dependent both on being located in an LFA and on fulfilling eligibility criteria. Currently, there are three mandatory EU-level eligibility criteria (see para 9), which are supplemented by a range of additional eligibility criteria set at the national and, in some cases, regional levels. According to the Commission, around 150 different criteria are used around the EU.
82. The Commission's Communication states that appropriate farm level eligibility rules are a useful way of targeting the aid after the process of area delimitation. The Commission considers that the current range of eligibility rules used by Member States could be amended so as to enhance their consistency with the objectives of the scheme and with the international commitments of the EU. A sufficient margin of manoeuvre should be left for addressing local peculiarities, which would also respect the principle of subsidiarity. In its Communication, the Commission has opted to defer making any firm proposals on this component of the scheme until the Member States have simulated the application of the new biophysical criteria on their territories and returned the resulting maps.

Witnesses' Views

Harmonisation of eligibility criteria

83. The majority of our witnesses accepted the need for a framework set at the EU level, allowing Member States to select their own eligibility criteria within that framework as appropriate. Some, however, were keener than others to emphasise the need for a framework that would align the criteria with the objectives of the scheme. The UK Government argued that a "strong EU-wide framework" must be "underpinned by first principles about what this measure is about" (Q 593). More specifically, the European Forum for Nature Conservation and Pastoralism argued that the EU-level framework must be related to the Rural Development Regulation Axis 2 objectives (Memorandum, p.184, para 4). Further detail was provided by the RSPB, which suggested a series of EU-wide conditions including: irrigation and drainage limits; minimum and maximum stocking densities; field size limits; and maximum tree density (Memorandum, p.52, para 20).
84. The need to avoid poor quality criteria which diverge from the scheme's objectives was emphasised by others. The European Commission wished to avoid "the big number and diverse quality of eligibility criteria which we have today" (Q 21) and the Farmers' Union of Wales considered that a common framework should ensure that "the eligibility conditions are not open to abuse within Member States" (Memorandum, p.15, para 38). The National Sheep Association recognised that a harmonised framework at the EU-level would assist in ensuring that the objectives of the scheme were fulfilled (Memorandum, page 70).
85. The IEEP warned that establishing a clear set of rules without constraining Member States might prove challenging (QQ 230–231). This caution appeared to be borne out by the evidence received from other Member States and regional authorities, who were keen to maintain flexibility at the national and regional level. The German government warned against excessive harmonisation of eligibility criteria (Q 272). The Bulgarian government recognised the need for some harmonisation but emphasised that "specificity

should also be taken into account, so there should be discretion to add to the criteria” (Q 402). Both the Czech and Swedish governments were cautious in their support for harmonisation of eligibility criteria and stressed that flexibility should be retained (QQ 449, 521).

86. The Scottish Executive emphasised that the flexibility must allow them to take into account “contrasting situations” across Scotland itself (Q 557). The Scottish Environment Protection Agency (SEPA) cautioned against setting maximum and minimum stocking densities at the EU level (Memorandum, p.197, Q 4). The Welsh Assembly Government called for “objective and benign” EU-wide criteria that would preserve regional flexibility within each Member State to determine the most appropriate eligibility criteria locally (Memorandum, p.210, Q 4).
87. A minority of our witnesses rejected any form of common eligibility criteria. The NFU pointed to the current condition in the Rural Development Regulation requiring that any measures financed under Axis 2 (such as the LFA scheme) shall target the sustainable use of agricultural or forestry land. In the NFU’s view, this common condition is sufficient, particularly as each Rural Development Plan is then subject to a Commission process of approval (Q 75). Similarly, NFU Cymru argued that it is for the Member State or region “to work up eligibility requirements and submit them to the Commission for approval” (Memorandum, p.23, para 15). The Ulster Farmers’ Union did not consider it feasible to set common eligibility conditions that were in line with the scheme’s objectives (Memorandum, p.31, para 28).
88. Some witnesses dismissed the use of eligibility criteria entirely. The Finnish government considered it impossible to impose eligibility criteria in view of the restrictions imposed by the Finnish climate (QQ 474–475), while the National Beef Association argued that the imposition of eligibility criteria might restrict mixed farming (Q 165).

The purpose and type of criteria

89. Several witnesses stressed that the purpose of eligibility criteria is to target aid within areas delimited as LFA (Commission, Q 21; Scottish Natural Heritage Memorandum, p.201, paras 18–21). The European Forum on Nature Conservation and Pastoralism noted that “effective targeting of LFA payments is best achieved through farm-level eligibility criteria” (Memorandum, p.184, para 3).

Exclusion of intensive farming

90. The majority of witnesses emphasised that eligibility criteria must be tied to the objectives of the scheme and concluded that intensive farming systems²⁰ should therefore be excluded (SCF, Q 165; SNH Memorandum, p.201, paras 18–21; IEEP, Q 228; European Forum on Nature Conservation and Pastoralism Memorandum, pp.185-186, paras 6 & 22; Country Land and Business Association Memorandum, p.183, para 6.2). As the European Commission explained, the Rural Development Regulation explicitly indicates that the scheme should be used to support extensive farming

²⁰ For example, the raising of large number of animals on a small amount of land or the cultivation of crops by using substantial inputs of capital labour or technologies such as pesticides and fertilisers.

systems²¹ (Q 21). The UK Government asserted that the scheme was never intended to support intensive farming (Q 588).

91. The governments of most other Member States from whom we took evidence were equally supportive of excluding intensive farming systems. The German government explained that it is already excluding certain “intensive agricultural production areas” (QQ 266–267). The Czech government expressed support for eligibility criteria that allow LFA payments to be carefully targeted, for example on the basis of livestock density and the extent of grassland, with the aim of excluding intensive farming (Q 443).
92. The Commission pointed out, however, that some Member States were less discriminating, and were for example extending LFA aid to areas whose soil quality was poor on some criteria (e.g. stoniness) but where champagne production was viable and successful (Q 13). The Bulgarian government explained that their current eligibility criteria relate to environmental conditions, farm size and active farming (Q 402). This means that no differentiation is made among eligible farms in terms of the type of activity undertaken, which allows holdings such as vineyards to be included (Q 412).

WTO obligations

93. Both the European Commission and the UK Government were also keen to emphasise that eligibility criteria must respect WTO obligations (Commission, Q 21; UK Government, Q 594). In order to avoid challenge under WTO rules, the criteria would need to be “green box compatible”, which means that the resulting payments should not distort trade, or at most cause minimal distortion. Such payments must be government-funded and must not involve price support. Typically, this might allow direct payments not linked to production levels or payments for the delivery of environmental goods.

Part-time farmers and applicant’s residence

94. It was noted that some Member States currently exclude part-time farmers from receipt of aid, an exclusion criticised by most witnesses, particularly as such practices differ across the European Union (NFU, QQ 70–71; NFUS, Q 71; NFU Cymru, Q 72; Ulster Farmers’ Union, QQ 72–73; European Forum on Nature Conservation and Pastoralism Memorandum, p.184, para 4; Bulgaria, Q 402). The NFU explained, for example, that some farms may appear to be active full-time but they might be considered part-time when judged by their economic output. The European Commission rejected the exclusion of part-time farmers altogether, on the basis that as long as such farmers contribute to the objective of the measure, “we do not see a reason why they should not be compensated for the specific costs they have” (Q 21). Another criterion deemed irrelevant was the residence of the applicant (UK Government, Q 593)

Committee’s Views

95. If the objectives of the scheme as set out in the Rural Development Regulation are to be met, **a common EU-level framework for eligibility**

²¹ Extensive farming systems would generally include a large area of land with proportionately low levels of capital, labour or technologies.

criteria is in our view essential. Without such a framework, the scheme risks being undermined by the imposition of a multitude of additional and possibly irrelevant eligibility criteria.

96. The EU-level framework must strike a balance between enforcing the scheme's objectives and affording sufficient flexibility to Member States and regions. We welcome the Commission's recognition of the need to clamp down on the use of criteria deemed irrelevant to the objectives of the scheme or contrary to the international commitments of the EU.
97. **We regret the Commission's reluctance to propose an EU framework for eligibility criteria at this stage. We consider that the focus of such a framework should be on extensive farming systems, the exclusion of any restrictions irrelevant to the objectives of the measure, and WTO-compatibility. It should not rule out mixed farming. Reaching agreement among Member States on such a framework is, however, likely to prove challenging.**

Payment Formula

98. Where they are not already doing so, Member States will be required to calculate LFA payments using the new payment formula set out in the 2005 Rural Development Regulation, which stipulates that payments should "compensate for farmers' additional costs and income forgone related to the handicap for agricultural production in the area concerned."²² Regulation 1974/2006 lays down that calculations should only contain elements that are verifiable, and should be based on figures established by appropriate expertise.²³ The principle behind the formula is that the LFA payment should compensate for all or part of the additional costs incurred by farmers in LFA areas compared to their counterparts in non-LFA areas. Member States' average LFA payment levels would still have to fall within a range fixed by the Council. The formula is already used for CAP agri-environment payments and for state aid, and is a recognised formula in the context of the World Trade Organisation.

Witnesses' Views

99. A number of witnesses welcomed the additional transparency that the new calculation method would bring. The UK Government anticipated that implementation of the formula, and the requirement for it to be verified independently, would make an important contribution to the consistency and efficiency of the LFA measure (DEFRA Memorandum, p.165, Q 6).
100. The IEEP, which had concluded in its evaluation report that the link between the handicap creating the disadvantage, the consequences for farm profitability and the level of payment was often not sufficiently transparent under the current regime, expressed qualified optimism that the new payment formula would begin to redress this. Its Director explained that clearer and more objective criteria for measuring the level of disadvantage would make it easier to calibrate payments accordingly (Q 235). The new formula, while "pretty broad brush", would at least provide a framework whereby Member States would need to present their calculations in a slightly

²² Art. 37.

²³ Art. 53.

more consistent form and be slightly more easily cross-examined by the Commission. So while the IEEP did not view the formula as a guarantee of completely consistent or carefully calibrated payments, it did expect it to “reduce some of the level of inconsistency” (Q 235).

101. The Commission anticipated that the new system would prevent over-compensation—a problem raised in the Court of Auditors’ report (Q 28). Other witnesses were less confident: the ENPAA noted that payment calculations are “not a hard science” and could be made more generous, or less, depending on the figures put into them, yet remain “perfectly justifiable and verifiable” (Q 129).
102. Most witnesses did not expect that use of the payment formula would stimulate convergence in LFA payment rates across the EU, delivering consistency in that sense. The Commission indicated that it was not interested in bringing about harmonisation of payment levels (Q 340).
103. The IEEP anticipated that continued flexibility around eligibility criteria would maintain variation in payment levels (Q 237). It also expected that, as Member States would continue to operate within a fixed budget up to 2013, their ability to change payment rates radically would be quite constrained. In the next programming period, however, there could be more of a break with past levels of payment (Q 237).
104. The UK Government emphasised that it would be essential for Member States and regions to retain the flexibility to determine what proportion of “additional costs and income forgone” is payable, including the flexibility to pay small or zero payments in some areas. They argued that the LFA scheme is a discretionary measure that works alongside a variety of other measures to deliver rural development objectives, and that Member States must be able to determine their budget allocation for each scheme in that wider context (DEFRA Memorandum, p.165, Q 6). At the other end of the spectrum, the Finnish government explained it would be in Finland’s interests to remove the upper limit on payment levels, as an objective calculation of the handicap faced by Finnish LFA farmers would yield a higher payment level than is currently permissible (Q 479).
105. Some farmers’ unions highlighted what they saw as a muddle in the philosophy behind the new payment formula, and particularly its “income forgone” element. The NFUS argued that LFA payments were not about income forgone or doing something non-productive such as setting aside land, as would be the case in agri-environment schemes. Instead the payments should compensate for a permanent physical disadvantage that cannot be remedied (Q 57). The NFU pointed out that, in some situations, farmers in LFA areas would be making so little net profit that they would not be forgoing income at all when participating in the LFA scheme, a point echoed by the RSPB (QQ 81, 129). The ENPAA acknowledged that there might be no net income to forgo, but argued that compensation for the cost of management could still be delivered adequately through the new payment formula (Q 129).
106. The NFU and NFUS advocated the inclusion of an “incentive” element in the formula to reward farmers who could produce “a really good environmental product” (Q 82). The NFUS pointed out that payments under the new formula would be totally dissociated from outcomes, even though the logic of the payment should now be on delivering outcomes

(Q 82). By contrast the ENPAA argued that where full payment for the costs involved in doing a job was being offered, no additional incentive to do that job should be deemed necessary (Q 129).

107. The UK Government warned that the approach enshrined in the formula does not recognise all factors relating to disadvantage for which the market may have already compensated the farmer. They observed, for example, that there is no adjustment for the lower land and rental costs payable in an LFA compared to a non-handicapped area (DEFRA Memorandum, p.165, Q 6).
108. A critical issue highlighted by both the UK and Finnish governments was the benchmark to be used for calculating “additional” costs, and notably whether the point of comparison should be a national benchmark or an EU benchmark. The Finnish government argued that an EU average should be used, as countries like Finland would have no non-handicapped reference to draw on (Q 479). The Scottish Executive warned that if Member States assess handicap relative to a reference area in their country, it is likely that land facing the same handicaps would attract different payment levels in different parts of the EU (Memorandum, p.150, Para. 10.13). The UK Government suggested that guidance should be developed to ensure consistent reference points are adopted for comparison with non-disadvantaged areas (DEFRA Memorandum, p.165, Q 6).

Committee’s Views

109. We expect that the new method of calculating LFA support will improve transparency and facilitate scrutiny of Member States’ payment practices. However, we do not expect that adoption of the formula will eliminate over-compensation in and of itself. **In order to address the Court of Auditors’ concerns fully, the European Commission must take responsibility for monitoring Member States’ implementation of the formula, and for challenging their calculations where necessary.**
110. We recognise that there will continue to be considerable variation in LFA payment levels across and within Member States. Although this could be viewed as a distortion of the Single Market, it is in our view an inevitable corollary of allowing individual authorities to exercise discretion in how they deploy the rural development funding they receive through the EAFRD, including the freedom not to operate an LFA scheme at all. We believe that this level of discretion is justified on the grounds of subsidiarity²⁴, and that the minimum and maximum payment levels set by the Council should exert an additional moderating influence.

²⁴ The principle of subsidiarity is defined in Article 5 of the Treaty establishing the European Community. In this context, we use it to mean that these types of decisions are more appropriately taken at national, regional, or local level than at EU level.

CHAPTER 4: IMPLEMENTATION AND OVERSIGHT

Timing of reform

111. The current Czech Presidency of the EU has opened negotiations on the Commission's Communication in Council Working Groups and the Special Committee on Agriculture. It hopes that these discussions will pave the way for Council Conclusions to be adopted at the Agriculture and Fisheries Council meeting due to be held in June (Q 435). The subsequent Swedish Presidency will then inherit the dossier (Q 531), but a legislative proposal from the Commission is not expected until 2010 at the earliest (Q 324). On this timetable, a revised LFA scheme would be unlikely to be implemented before 2014, by which time the future of the Common Agricultural Policy as a whole is expected to be under discussion against the backdrop of a review of the EU budget. There could consequently be a case for rolling the LFA review into a wider review of the CAP, to avoid implementing a targeted reform of the LFA scheme that is quickly overtaken by a wider reform of the CAP, precipitating further changes to the scheme.

Witnesses' Views

112. Those advocating that reform of the LFA scheme should be postponed justified their stance in different ways. Natural England argued that there is overlap between the scope of the LFA scheme and agri-environment programmes in Pillar II and elements of Pillar I support. It made the case for using the next round of CAP reform to rationalise and, where appropriate, integrate these measures (Memorandum, p. 196, Paras. 23–24). The Country Land and Business Association suggested that there was “little point” in tinkering with LFA areas and measures any further until a more wide-ranging debate about the purpose and distribution of the whole support system, and the role of the LFA scheme within it, had taken place (Memorandum, p.184, Paras. 10.1–10.2). The Bulgarian government indicated that as it had only just begun applying its LFA scheme in 2007, it would wish to postpone any further reform until after 2013 (Q 397). The Swedish government, which is due to take on the EU Presidency in July, anticipated that finding support from all the Member States to press ahead swiftly with the LFA review would be difficult (Q 532).
113. By contrast the Commission, the current Czech Presidency and the UK Government cast the LFA review as a “technical exercise” which should not be affected by the budget review (Q 330, QQ 437–438 and Q 603 respectively). The Commission stressed that “what we are doing is not a reform”, but rather a technical exercise that would help Member States to target funds more efficiently (Q 330). The Czech government explained that the exercise had been planned for a few years and now was the time to “materialise the decision” (Q 455). It anticipated that the debate on the future of the CAP would centre on the role of Pillar I payments, rather than on rural development, and so did not expect that debate to hold up the LFA review. It also emphasised the “general consensus” on the importance of a response to the Court of Auditors' report of 2003 (Q 435).

Committee's Views

114. At its heart, the LFA review is a technical exercise that should be undertaken separately from any further reform of the CAP. However, it has a political dimension that Member States are unlikely to overlook. The review could bring unwelcome consequences in the form of areas that might no longer qualify for aid, in limits on national and regional authorities' discretion in awarding aid, and even in the administrative demands that closer oversight by the Commission might entail. We did not sense much appetite for reform among the Member States from whom we took evidence, and we anticipate that rallying consensus on the need to press ahead will take considerable coaxing on the part of the Commission and the Council Presidency.
115. **We nonetheless support a prompt execution of the review.** The deficiencies highlighted in the Court of Auditors' report cannot continue to be left unchecked. But just as importantly, a successful review should ensure that LFA funds are allocated more efficiently, benefiting not only the taxpayer but also the farms most deserving of support under this scheme.

Monitoring and evaluation

116. In its 2003 report, the Court of Auditors found that although the LFA scheme had been in operation since 1975, no overall evaluation of the impact of the measure had been carried out. It noted that beneficiaries believed that LFA aid had enabled them to continue farming in an area which they might otherwise have had to leave, but argued that in the absence of an overall evaluation, no definite conclusions could be drawn. The Court concluded that the Commission was insufficiently informed of the impact of the scheme, and that it could therefore not be guaranteed that resources were being used properly.²⁵
117. Following publication of the Court of Auditors' report, an evaluation of the LFA measure was commissioned from the Institute for European Environmental Policy, and published in 2006.²⁶ The IEPP concluded that the original goal of the LFA measure—preventing the abandonment of agricultural land—had been reached in the 'old' Member States of the EU²⁷, where relatively little farmland had ceased to be managed by agriculture. It suggested that the LFA measure is one of a number of policies that have contributed to this outcome, but that its exact contribution is not clear cut, partly because there is little evidence about how beneficiaries would have acted in the absence of a payment, partly because significant numbers of holdings in LFA areas continue to be farmed even though they do not attract LFA payments, and partly because the contribution of the LFA payment to farm incomes is often dwarfed by other CAP subsidies. The report emphasised that there is variation across farms and Member States in the extent to which LFA payments contribute to farm incomes and in the income level required to maintain farming, and that it is difficult to be confident that the LFA payments offered match these varying requirements,

²⁵ European Court of Auditors, Special Report 4/2003, para. III (f) and paras. 72–79.

²⁶ 'An Evaluation of the Less Favoured Area measure in the 25 Member States of the European Union', report prepared by the Institute for European Environmental Policy for the European Commission's DG Agriculture, November 2006.

²⁷ Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, Netherlands, Portugal, Spain, Sweden, UK.

suggesting that there is no uniform pattern of effectiveness. It nevertheless concluded that the measure had been most effective on livestock farms.

118. Articles 80 and 81 of the 2005 Rural Development Regulation stipulated that the Commission and the Member States should draw up a common monitoring and evaluation framework specifying common indicators on the basis of which the progress, efficiency and effectiveness of individual rural development programmes could be measured. It also mandated annual progress reports and ex ante, mid-term and ex post evaluations of rural development programmes by independent evaluators (Arts. 82 and 84). The common monitoring and evaluation framework was established by Regulation 1974/2006. That Regulation charges the Commission with drawing up guidance on the evaluation of each rural development measure, and with providing information sheets for each measure specifying the logic of intervention and the indicators against which progress is to be assessed.²⁸

Witnesses' Views

119. The Commission assured us that it had devoted close attention to the Court of Auditors' assessment of the LFA scheme and its deficiencies, and responded by introducing a number of changes, among them the common management and evaluation framework, accompanied by indicators to monitor the results delivered by the measure (QQ 28–29). It explained that Member States must report back to the Commission on an annual basis, and conduct mid-term and ex-post evaluations outlining the impact of the measure, and indicating how far the measure has helped to ensure continued agricultural land use in areas with handicaps (Q 29). However, some Member States had experienced difficulty in using the indicators to produce their first annual report in 2008 (Q 30). The Commission conceded that the submission of incomplete reports by Member States would not automatically halt the payment of aid. Instead, it pledged to work with Member States to ensure that all the information required for the process of justifying budget allocations was available (Q 31).
120. The UK farmers' unions were adamant that the LFA scheme had made a critical difference to the preservation of farming activity in disadvantaged areas. They pointed out that LFA payments could amount to anywhere between 13 and 33 per cent of net farm incomes, sometimes more in bad years, and that that contribution made a critical difference to whether a given farmer chose to continue farming in an LFA area (QQ 48–56, Q 87).
121. Among other Member States, however, we heard different accounts of the extent to which land abandonment presented a threat. The Polish and Bulgarian governments, for example, each identified land abandonment as a severe problem (Q 285 and Q 385, respectively). But the German government noted that while farmers did go out of business, the proportion of land being abandoned was very low in Germany, as it would be more common to seek alternative income sources outside agriculture (Q 252).
122. The UK Government noted that the demand to take over upland farms was still there (Q 575). The Scottish Executive also noted that anecdotal evidence about land abandonment was not borne out in the statistics, which

²⁸ Commission Regulation (EC) No 1974/2006 of 15 December 2006 laying down detailed rules for the application of Council Regulation No 1698/2005 on support for rural development by the European Agricultural Fund for Rural Development (EAFRD), Article 62 and Annex VIII.

showed a rise in the number of applications for LFA support in Scotland in 2008 compared to 2007. It explained that livestock numbers had been coming down in Scottish LFAs, not least as a result of decoupling (which brought headage payments to an end)²⁹, but argued that without LFA payments a greater decline would have been observed (QQ 546–547).

123. The IEEP explained that overall, the area of land under agriculture in LFA areas had been maintained over the period 1995 to 2003. It also drew to our attention the huge variation in the proportion of land designated as LFA that attracts aid—ranging from over 90 per cent in Ireland, Luxembourg and Finland, to less than 20 per cent in France and Portugal—and suggested that where LFA land continues to be farmed in the absence of LFA payments, the payment could not be regarded as essential for the continuation of agricultural activity. It also found significant variation in the proportion of farm income sourced from LFA payments, but concluded that, given the narrow profit margins under which LFA farms sometimes operate, even relatively small contributions—of 5 per cent or less in some southern Member States—might be significant (QQ 209–211).

Committee's Views

124. Many of our witnesses asserted their conviction that the measure has made a critical difference to preventing land abandonment by maintaining farming activity, pointing to the contribution that LFA payments make to the financial viability of farming businesses. However, this does not in itself establish that LFA payments are either necessary or sufficient to prevent abandonment. **Like the Court of Auditors before us, we have therefore been unable to draw firm conclusions about the effectiveness of the LFA scheme in meeting its objectives.**
125. **While we recognise that it will be difficult to disentangle the effect of the LFA scheme from other financial aid made available to farmers, we believe that the Commission and the Member States must commit to assembling the evidence base with which the scheme's effectiveness as a mechanism for protecting the environment and the landscape might be assessed and kept under review.** We anticipate that the scheme's performance against its objectives will need to be evaluated regularly, both by the Commission and at a local level, to establish whether environmental and landscape benefits continue to be delivered, and whether it is still appropriate to offer support where natural handicaps are either exacerbated or mitigated by climate change.
126. **We urge the Commission to ensure that the indicators used to assess the impact of the LFA measure reflect its objectives, and can be readily applied by Member States. While we recognise that some Member States may need time to develop systems for collecting the relevant data, we believe that in the medium term, the Commission should consider temporary suspension of payments where evaluation reports are unsatisfactory or not forthcoming.**

²⁹ Decoupling refers to the breaking of the link between CAP subsidies and production. Headage payments were one variant of this, whereby subsidies were linked to the number of livestock kept on a given holding.

CHAPTER 5: CONCLUSIONS AND RECOMMENDATIONS

The role of the LFA scheme

127. We endorse the European Commission's stance on the purpose of support for farms in Less Favoured Areas: payments should help farmers in marginal areas to continue farming where their farming activity generates public benefits in the form of positive impacts on the environment and the landscape.
128. We emphasise the importance of continuing to assess the public benefits obtained in exchange for this type of aid: society does not owe unconditional support to farmers wishing to farm in areas affected by natural handicaps. Indeed, we anticipate that as climate change begins to take its toll on parts of Europe, support may need to be reassessed. In some instances, currently non-handicapped areas may require additional support, while in other instances, for example where water scarcity becomes particularly acute, land may become so severely handicapped that support should be withdrawn.
129. We are conscious that by maintaining farming activity in place in marginal areas, the LFA scheme also makes a de facto contribution to preserving food production capacity, which could become increasingly important if climate change reduces production capacity elsewhere.
130. We recognise that farming activity in marginal areas often brings social, economic and cultural benefits to local communities and the wider public. However, measures available under the other axes of the Rural Development Regulation offer more targeted and cost-effective ways of addressing socio-economic objectives in rural areas.
131. We also consider it important to recognise that neither the LFA payment nor the wider package of financial aid available to farmers in Less Favoured Areas will necessarily be sufficient to prevent a decline in farming activity in marginal and remote areas of the EU. LFA payments may exert a moderating influence, but would-be farmers' career choices are likely to be influenced by cultural and lifestyle factors as well as economic incentives. We view this as an emerging policy challenge that merits consideration as part of the wider review of the CAP post-2013.
132. The evidence we received suggests that LFA payments are partly being used to plug a gap created by the way in which Pillar I subsidies are delivered. The productive potential of a holding is either disregarded or, in historic-based systems, positively rewarded. Single Farm Payments also fail to reflect variation in the magnitude and significance of the public benefits delivered by continued farming activity in different settings. For these reasons, we see a distinctive role for the Less Favoured Areas scheme, which offers a means of channelling support in a much more discriminating way, to those farms that are least able to earn compensation from the market, yet contribute most to the maintenance of the landscape.

The content of the review

133. The Court of Auditors was strongly critical of the existing designation system which has led to a proliferation of criteria across the European Union. In order to provide consistency and transparency, a common set of biophysical

indicators to identify disadvantaged areas based purely on natural handicap is welcome.

134. The European Union is, however, geologically and meteorologically diverse, a diversity which leads to a range of handicaps that must be adequately captured in the common set of criteria. The criteria proposed by the Commission in its Communication provide an adequate basis for Member States to map the areas with natural handicaps across the EU. When assessing the maps that result, it will be critical to examine whether the specific nature of the UK and Irish maritime climate is adequately captured by the proposed criteria. At that stage, it may be necessary to press for the inclusion of additional criteria such as field capacity days or a suitable proxy.
135. The establishment of indicators and the requirement to map is meaningless, however, without the appropriate data. While some Member States may have all of the necessary data to hand, we note that extra efforts may be required of others to ensure that the mapping can be completed within the Commission's deadline. We recommend that the Commission pays careful attention to the availability of data in each Member State and offers assistance to Member States where necessary. Mapping down to land parcel level should be encouraged where such data is available, as this will facilitate the very targeting of aid that the review is intended to promote.
136. Diversity of national and regional circumstances is such that it will be necessary to fine-tune the designation that results from application of the common biophysical criteria, but we see a danger that Member States may seek to use the fine-tuning process to replicate existing LFA designations. We therefore endorse the approach advocated by the UK Government, whereby national and regional authorities would be permitted to fine-tune designations only in order to exclude areas where handicaps have been overcome.
137. We see a role for the Commission in monitoring this process, and ensuring that the criteria used for fine tuning are related to the objectives of the scheme as laid down by the 2005 Rural Development Regulation.
138. We recognise that in many parts of the EU, the LFA scheme is still used to pursue socio-economic objectives. It is our view, however, that the policy levers available under the other axes of the EAFRD—and indeed under other EU, national and regional schemes—are better suited to that task, and that the LFA scheme's implementation must be brought into line with its formal objectives. We consequently support the proposed move away from socio-economic indicators of disadvantage towards designations based purely on natural handicap.
139. If the objectives of the scheme as set out in the Rural Development Regulation are to be met, a common EU-level framework for eligibility criteria is in our view essential. Without such a framework, the scheme risks being undermined by the imposition of a multitude of additional and possibly irrelevant eligibility criteria.
140. The EU-level framework must strike a balance between enforcing the scheme's objectives and affording sufficient flexibility to Member States and regions. We welcome the Commission's recognition of the need to clamp down on the use of criteria deemed irrelevant to the objectives of the scheme or contrary to the international commitments of the EU.

141. We regret the Commission's reluctance to propose an EU framework for eligibility criteria at this stage. We consider that the focus of such a framework should be on extensive farming systems, the exclusion of any restrictions irrelevant to the objectives of the measure, and WTO-compatibility. It should not rule out mixed farming. Reaching agreement among Member States on such a framework is, however, likely to prove challenging.
142. We expect that the new method of calculating LFA support will improve transparency and facilitate scrutiny of Member States' payment practices. However, we do not expect that adoption of the formula will eliminate over-compensation in and of itself. In order to address the Court of Auditors' concerns fully, the European Commission must take responsibility for monitoring Member States' implementation of the formula, and for challenging their calculations where necessary.
143. We recognise that there will continue to be considerable variation in LFA payment levels across and within Member States. Although this could be viewed as a distortion of the Single Market, it is in our view an inevitable corollary of allowing individual authorities to exercise discretion in how they deploy the rural development funding they receive through the EAFRD, including the freedom not to operate an LFA scheme at all. We believe that this level of discretion is justified on the grounds of subsidiarity, and that the minimum and maximum payment levels set by the Council should exert an additional moderating influence.

Implementation and oversight

144. Many of our witnesses asserted their conviction that the measure has made a critical difference to preventing land abandonment by maintaining farming activity, pointing to the contribution that LFA payments make to the financial viability of farming businesses. However, this does not in itself establish that LFA payments are either necessary or sufficient to prevent abandonment. Like the Court of Auditors before us, we have therefore been unable to draw firm conclusions about the effectiveness of the LFA scheme in meeting its objectives.
145. While we recognise that it will be difficult to disentangle the effect of the LFA scheme from other financial aid made available to farmers, we believe that the Commission and the Member States must commit to assembling the evidence base with which the scheme's effectiveness as a mechanism for protecting the environment and the landscape might be assessed and kept under review. We anticipate that the scheme's performance against its objectives will need to be evaluated regularly, both by the Commission and at a local level, to establish whether environmental and landscape benefits continue to be delivered, and whether it is still appropriate to offer support where natural handicaps are either exacerbated or mitigated by climate change.
146. We urge the Commission to ensure that the indicators used to assess the impact of the LFA measure reflect its objectives, and can be readily applied by Member States. While we recognise that some Member States may need time to develop systems for collecting the relevant data, we believe that in the medium term, the Commission should consider temporary suspension of payments where evaluation reports are unsatisfactory or not forthcoming.

APPENDIX 1: SUB-COMMITTEE D (ENVIRONMENT AND AGRICULTURE)

The members of the Sub-Committee that conducted this inquiry were:

The Earl of Arran
 Lord Brooke of Alverthorpe
 Viscount Brookeborough
 The Earl of Caithness
 Lord Cameron of Dillington
 The Earl of Dundee
 Baroness Jones of Whitchurch
 Lord Livsey of Talgarth
 Lord Palmer
 Lord Sewel (Chairman)
 Baroness Sharp of Guildford
 Viscount Ullswater

Declarations of Interest Relevant to this Inquiry

The Earl of Arran

*Married to a farmer and landowner in Devon
 Trustee of certain family trusts associated with farming*

Lord Brooke of Alverthorpe

Senior Strategic Adviser to Accenture plc—IT provider for Single Farm Payments for DEFRA

Viscount Brookeborough

*Farms LFA land in Northern Ireland (in receipt of LFA payments)
 Farms in Northern Ireland and received an EU grant several years ago for diversification
 Runs a farm-based tourist business*

The Earl of Caithness

*Trustee of a Trust that owns farmland within an LFA area. The farm owned by the Trust receives an LFA payment
 (Non-remunerated) Trustee of Fundatia Adept Ltd, a charity working to protect the countryside of Tarnava Mare in Southeast Transylvania. The trust receives EU grants*

Lord Cameron of Dillington

*Farmer and landowner and has commercial property interests in the countryside (not in an LFA area)
 Member of the National Farmers' Union
 Member of the Country Land and Business Association
 Member of the Campaign to Protect Rural England
 Member of the National Trust
 Director of the Royal Bath and West Society
 Trustee of the Lawes Agricultural Trust*

The Earl of Dundee

*Farmer, landowner and forester in Scotland
 Director of farming company in Scotland
 In receipt of Single Farm Payments*

Lord Livsey of Talgarth

No direct financial interests

Member of The Campaign for the Protection of Rural Wales
Adviser (unpaid) 'Prime Cymru'—Business start ups in Wales for 50+ year olds
Member of the Royal Welsh Agricultural Society
Vice President of the Brecknock Federation of Young Farmers Clubs
President of the Brecon and District Disabled Club—runs Dial-a-Ride Rural Bus Service Charity

Lord Palmer

Farmer (in receipt of Single Farm Payment and other rural Stewardship Scheme Payments)
Member of the National Farmers' Union Scotland
Member of the Scottish Rural Property and Business Association
President of British Association for Bio Fuels and Oils
President of Transport Division of the Renewable Energy Association
Residual beneficiary of banana growing estate in West Indies
Involved in rural tourism

Viscount Ullswater

Trustee of landed estates in Cumbria and Devon (Expenses)—Land owned by the Trusts attract LFA payments
Member of the Country Land and Business Association

A full list of Members' interests can be found in the Register of Lords Interests:

<http://www.publications.parliament.uk/pa/ld/ldreg.htm>

APPENDIX 2: LIST OF WITNESSES

The following witnesses gave evidence. Those marked * gave oral evidence.

- * Bulgarian Government
- * COPA-COGECA
The Country Land and Business Association (CLA)
- * Czech Government
- * Department for Environment, Food and Rural Affairs (DEFRA)
- * English National Parks Authorities Association (ENPAA)
- * European Commission
European Forum on Nature Conservation and Pastoralism
- * Farmers' Union of Wales (FUW)
- * Finnish Government
- * German Government
- * Institute for European Environmental Policy
- * Mr. Huw Irranca-Davies MP, Minister for the Natural and Marine Environment, Wildlife and Rural Affairs
Loch Lomond and the Trossachs National Park Authority
Macaulay Land Use Research Institute
- * National Beef Association
- * National Farmer's Union (NFU)
- * NFU Cymru
- * NFU Scotland
- * National Sheep Association
Natural England
- * Polish Government
- * Royal Society for the Protection of Birds (RSPB)
- * Scottish Crofting Foundation (SCF)
Scottish Environment Protection Agency (SEPA)
- * Scottish Executive
Scottish Natural Heritage (SNH)
Scottish Rural Property and Business Association
- * Swedish Government
Tenant Farmers Association
- * Ulster Farmers' Union
Welsh Assembly Government (WAG)

APPENDIX 3: CALL FOR EVIDENCE

Introduction

The House of Lords European Union Committee will be conducting a short inquiry, through its Environment and Agriculture Sub-Committee (Sub-Committee D), into the planned review of the Less Favoured Area support scheme, which is to be the subject of a European Commission Communication in Spring 2009.

Aid to farmers in Less Favoured Areas (LFAs) is part of the EU's Rural Development Policy. Following criticism by the European Court of Auditors in 2003³⁰, the policy objectives of the LFA scheme were amended to align them more closely with the sustainable land management objectives of Axis 2 of the new Rural Development Regulation³¹. However, the Council of Ministers failed to reach agreement on how to bring the modalities of the scheme into line with the new policy objectives. The European Commission was consequently charged with leading a review of the LFA measure.

Early in 2008, the Commission launched a public consultation³² as part of the review process, looking at how the scheme should be amended in light of its revised objectives. A Communication setting out the Commission's proposals is expected in Spring 2009. A legislative proposal could follow either late in 2009 or early in 2010.

The Committee is seeking evidence from stakeholders and other interested parties, on the basis of which it will formulate conclusions and recommendations designed to inform the House of Lords and assist the UK Government and the EU institutions in taking the review forward in the course of 2009 and 2010. The primary focus of the inquiry will be the EU-wide revision of the Less Favoured Areas scheme. Views on current developments in the way the scheme is delivered in the UK are welcome, but should where possible draw out the connection to the EU policy framework.

The issues

Against this background, the Committee hereby invites you to submit written evidence to its Inquiry. The Committee would find it helpful if, in addition to any general issues you may wish to raise, you would focus on a number of specific issues, listed below. It is recognised that those submitting evidence will not necessarily have an interest in all the questions and may therefore wish to be selective. Views are sought on the following:

The past: strengths and weaknesses of the LFA scheme

- (1) The strengths and the weaknesses of the LFA scheme thus far.

The current review: common biophysical criteria

- (2) Whether it is appropriate to set common, EU-wide biophysical criteria for delimiting LFA areas, as suggested by the Commission in its consultation paper.

³⁰ ECA Special report No 4/2003 concerning rural development: support for less favoured areas (OJ C151 27.06.2003, p. 1–24)<http://eca.europa.eu/portal/pls/portal/docs/1/173294.PDF>

³¹ Articles 36 (a)(i) & (ii), 37 and 50 of Council Regulation (EC) No 1698/2005 of 20 September 2005 on support for rural development by the European Agricultural Fund for Rural Development.

³² http://ec.europa.eu/agriculture/consultations/lfa/index_en.htm

- (3) Whether the common biophysical criteria set out by the Commission in its consultation paper are appropriate and effective in identifying disadvantaged areas. Are there any omissions, whether in the form of further biophysical indicators or other indicators?

The current review: eligibility conditions

- (4) What degree of harmonisation of eligibility conditions (for determining access to LFA payments), if any, is needed.
- (5) What the basic rules and criteria for eligibility for LFA aid should be, if the scheme is to meet its new objectives.

The current review: payment calculation

- (6) How practicable is the new payment formula (based on additional costs and income foregone related to the handicap in the area concerned)? Is it likely to help reduce wide discrepancies in payment levels across Member States?

The impact of the review

- (7) To what extent would common biophysical criteria and amended eligibility criteria address the deficiencies of the LFA scheme as identified by the Court of Auditors in 2003, and in particular:
 - guarantee equitable treatment of beneficiaries
 - facilitate monitoring, control and audit of the measure
 - facilitate evaluation of the impact and effectiveness of the measure

The future development of the LFA scheme

- (8) What is the role of the LFA scheme in the context of the current Rural Development Regulation, and the reformed, post-Health Check CAP. What should the LFA scheme deliver in the short term (pre-2013) that other policy instruments affecting farm viability, environmental protection and agricultural land use cannot deliver?
- (9) The future evolution of the scheme, post-2013, within the context of the EU budget review, the EU's cohesion policy and further reform of the Common Agricultural Policy.

APPENDIX 4: RECENT REPORTS

Recent Reports from the Select Committee

Session 2008–09

Priorities of the European Union: evidence from the Ambassador of the Czech Republic and the Minister for Europe (8th Report, Session 2008–2009, HL Paper 76)

Enhanced scrutiny of EU legislation with a United Kingdom opt-in (2nd Report, Session 2008–2009, HL Paper 25)

Session 2007–08

Annual Report 2008 (32nd Report, Session 2007–2008, HL Paper 191)

Priorities of the European Union: evidence from the Ambassador of France and the Minister for Europe (24th Report, Session 2007–08, HL Paper 155)

The Commission's Annual Policy Strategy for 2009 (23rd Report, Session 2007–08, HL Paper 151)

Priorities of the European Union: evidence from the Minister for Europe and the Ambassador of Slovenia (11th Report, Session 2007–08, HL Paper 73)

The Treaty of Lisbon: an impact assessment (10th Report, Session 2007–08, HL Paper 62)

Recent Reports prepared by Sub-Committee D (Environment and Agriculture)

Session 2007–2008

The Revision of the EU's Emissions Trading System (33rd Report Session 2007–2008, HL Paper 197)

The Progress of the Common Fisheries Policy (21st Report Session 2007–2008, HL Paper 146)

The Future of the Common Agricultural Policy (7th Report Session 2007–2008, HL Paper 54)

Session 2006–2007

European Wine: A Better Deal for All Final report with evidence (39th Report, Session 2006–2007, HL Paper 184)

European Wine: A Better Deal for All (30th Report Session 2006–2007, HL Paper 144)

Water Framework Directive: Making It Work (27th Report Session 2006–2007, HL Paper 136)