

Multi-Annual Subsidy Decoupled from Surface Area *- a Romanian proposal for the future of European small farms -*



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Which small farms is the Commission's communication talking about?

In November 2010, European Commissioner Dacian Cioloş released "the Common Agricultural Policy (CAP) towards 2020" – a document outlining the broad strokes of the reform of the European agricultural policy. The communication will be followed in 2011 by a legislative proposal by the Commission. Thus, we are currently in the stage between general principles and concrete measures. In this context, CRPE proposes a subsidy scheme for small farms that would facilitate:

- a) giving small farmers access to funds - for those with economically viable commercial operations*
- b) encouraging the sale of land to those will small holdings without commercial potential.*

The communication announces the Commission's intention to introduce a simple scheme specifically for small farmers that is meant to replace the existing regime of direct payments, thus

Romania's Ministry of Agriculture and Rural Development (MADR) has repeatedly expressed its support for the introduction of a support scheme for small farmers, including in its presentation, "Romania's Position on the Future Common Agricultural Policy After 2013".

reducing bureaucracy. The current procedures only take into account historical or land area criteria, no matter the size of the farm in question, and small and mid-sized farmers clearly have a harder time bearing the administrative costs related to application for the subsidy.

Easier said than done. Because the current system implies a certain level of automatization: EU agricultural land areas are included in digital maps, and farmers receive certain sums annually, following their requests. The system is relatively difficult to set up (drawing maps, registering parcels of land), but once done it largely functions automatically. It is true that there are large administrative costs; for instance, the maps are updated at certain intervals. So, how could a scheme that distributes money for many farmers and many parcels of land look simpler than the current system? In the following sections, we will present CRPE's proposal. We will first define the desired beneficiaries.

What does "small farm" mean?

With its large number of rural households, Romania has a very obvious interest in this question. We need to specify that, *as the European Commission has it, "small farms" are not generally subsistence households.* Moreover, a large part of the latter are not included in the Common

Agricultural Policy – those with less than 1 ha do not receive European subsidies.¹ Even if, at this stage of formulating the new policy for small farms, the criteria for delimiting them have not yet been defined, it is likely that the term will not refer to those farms that do not currently receive direct subsidies.

The difference is rather substantial if we consider the number of farms. EU countries have 13,7 million agricultural operations², but direct CAP payments were only made to 7,8 million beneficiaries (2009 numbers). It is subsistence farms that make up the difference. A stricter definition of subsistence farms by Eurostat, using the concept of the economic dimension³ of the operations, considers subsistence farms to be those with less than 1 ESU (= a value added of 1200 euro / year). These farms (approx. 6,3 million) represent 47% of agricultural operations, 23% of the agricultural workforce, and 7% of the total agricultural surface area of the EU. That is why, should the historical criterion for allocating direct payments ever be rejected, Romania ought to consider the possibility of also taking these areas into consideration in a possible redivision of direct payments on the basis of surface area at the EU level, even if their owners are not currently beneficiaries of the direct payments. The main argument in favor of this approach is that these surface areas could be considered a kind of reservoir for the consolidation of the operations that currently benefit from direct payments.

The (probably more realistic) alternative to this proposal would be for the surfaces occupied by subsistence operations to constitute one of the criteria for allocating funds for the Second Pillar, considering the fact that subsistence farms have an incontestable role in maintaining the vitality of the rural space, or at the least the chances for revitalizing it. Otherwise, Romania's main efforts surely must be directed at the future situation of the current beneficiaries of direct payments, which in Romania are not few (in 2010 approximately 1 million requests were submitted.)

How payments for small farms can be simplified

In a relatively recent interview for newspaper *Adevărul*, Commissioner Cioloș announced the direction in which the Commission's plans for supporting small farms was headed: "For small farms, we intend to establish a lump sum payment under much simpler conditions than those for mid-sized and large farms. Small farmers will probably no longer have to submit a request every year, and there will not be as many verifications. And in the program for rural development we will have measures for the facilitation of investments in small farms."⁴

¹ We have explained Romania's reason for opting for 1 ha as the minimum in our previous report, "One Country and Two Agricultures", CRPE Policy Paper no. 4, 2009.

² Structural Agriculture Investigation in 2007

³ The economic dimension of an operation is given as the gross value added that could potentially be produced by an operation, and the unit of measure for this in the EU is the ESU (European Size Unit), which is equivalent to a value added of 1200 euro.

⁴ *Adevărul* Europa Interviews. Dacian Cioloș: "Romanian farmers will receive more money, but not as much as the French".

CRPE's proposal is exactly along the lines sketched by Commissioner Cioloş. Romania even has an obligation to make a proposal for the practical application of this idea, one which would prove crucial to the restructuring of the agricultural sector.

How do we define "small farms"?

To get past the complicated problem of definitions and minimums, we propose the application of a simple principle: *Small farms are those currently receiving small direct subsidies.*

If we consider the categories for beneficiary allocation currently used by the Commission, we may propose that the limit for small farms be 1250 euro. This means that, in practice, "small farm" = European farm currently receiving under 1250 euro / year in European funds.

Of the 7,8 million farms in the EU currently receiving direct payments, approximately 5 million fall

CRPE's Proposal

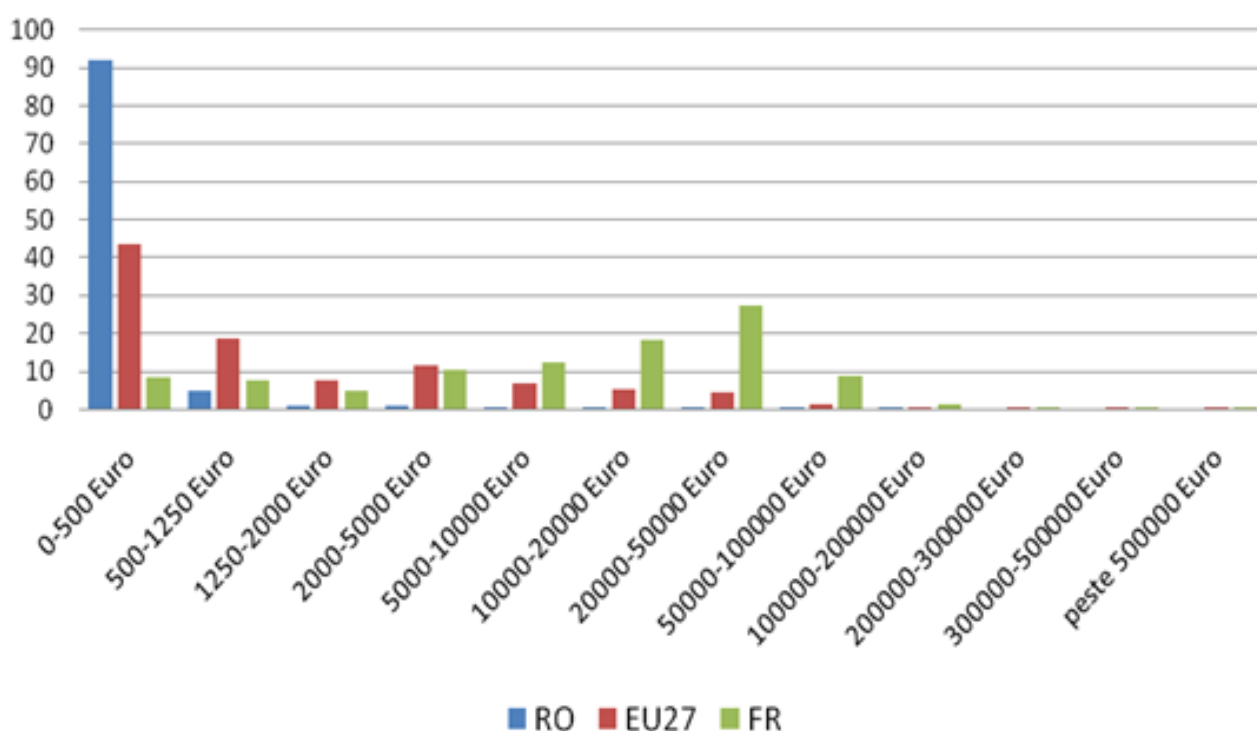
- *small farms = those that now receive small sums of money*
- *a multi-annual system of payment not tied to surface area*

under the 1250 euro threshold. Thus, our proposal applies to 5 million European farmers. In the case of Romania, the impact would be dramatic: 90% of Romanian farmers that currently receive direct payments fall below this threshold.

Of course, the impact differs from country to country – see Fig. 1. While 90% of Romanian farms currently receiving payment, for France the figure is just 15%, which is still not little.

Fig. 1.

Percent of total direct payment beneficiaries by payment size category



What would change for small farmers?

At the moment, the payment system is the same for a farmer with 5 ha as it is for one with 5000 ha. Every farmer submits an annual request and passes through certain verification procedures. Obviously, the administrative costs disproportionately affect small farmers, and at a national level states with more small farms.

In Romania's case, annual payment of the subsidy, which is indirectly tied to land ownership (because the amount of land under lease is relatively small), inhibits the sale of fragmented plots.

A peasant with 2 ha of land makes an annual payment to the Romanian state of approximately 10 euro / year⁵ and receives a subsidy of approximately 100 euro; the subsidies are growing, thanks to Romania's program for the equalization of mid-sized subsidies in the EU. In this context, a peasant's rational choice is not to sell his land but to instead wait for subsidies.

In CRPE's proposal, farmers would sign up to receive a subsidy only once, at the beginning of the European financial programming period. As this period is currently seven years, farmers would submit a single request in the first of the seven years and would subsequently receive the same subsidy for the following seven years. The subsidy would only be tied to the surface area of the land under cultivation (the agricultural property) at the beginning, when the request is made. This would allow a peasant to sell his land and continue receiving the subsidy for seven years. This, in turn, would eliminate the tendency for farmers to hold onto unworked land in order to receive the subsidy through annual requests. Though the change might appear minor, it would

Our proposal would produce different effects for two different categories of farmers:

- farmers with small holdings would be encouraged to sell, while still benefitting from the subsidy for 7 years (or 5, if the European financial programming period changes)
- for farms defined as mid-sized by Romanian standards (e.g. over 10 ha) it would create growth opportunities by bringing onto the market small pieces of land from the immediate vicinity of currently existing operations. Given the extreme fragmentation of the holdings, it is to be expected that mid-sized farmers would take advantage of this opportunity more than small farmers

have the potential to create a major effect on the structure of agricultural property in Romania and other EU states with fragmented agricultural land.

If a peasant sells his land because he will receive the subsidy for another 7 years, the new owners will be able to use the land and declare it, but they will not receive direct payments until after the expiration of the period for which the old owners receive the support. The effect could be similar to that for the "lifelong annuities" program, but on a much larger scale, over a shorter time span, and with greater chances of helping mid-sized farms consolidate (potentially also with the help of certain specific rural development measures).

If our proposal is considered, Romania would need to rethink the support mechanism for mid-sized farms in the CAP's second pillar (rural development). Farmers who wish to modernize their operations currently may receive 1500 euro / year after the submission of an application file, as part of measure 141 for the support of semi-subsistence farmers who wish to restructure their holdings. Romania ought to come up with a policy to encourage the expansion of mid-sized farms, including through facilities accorded by the state to these farms, in order to reduce sale and lease transaction costs for land.

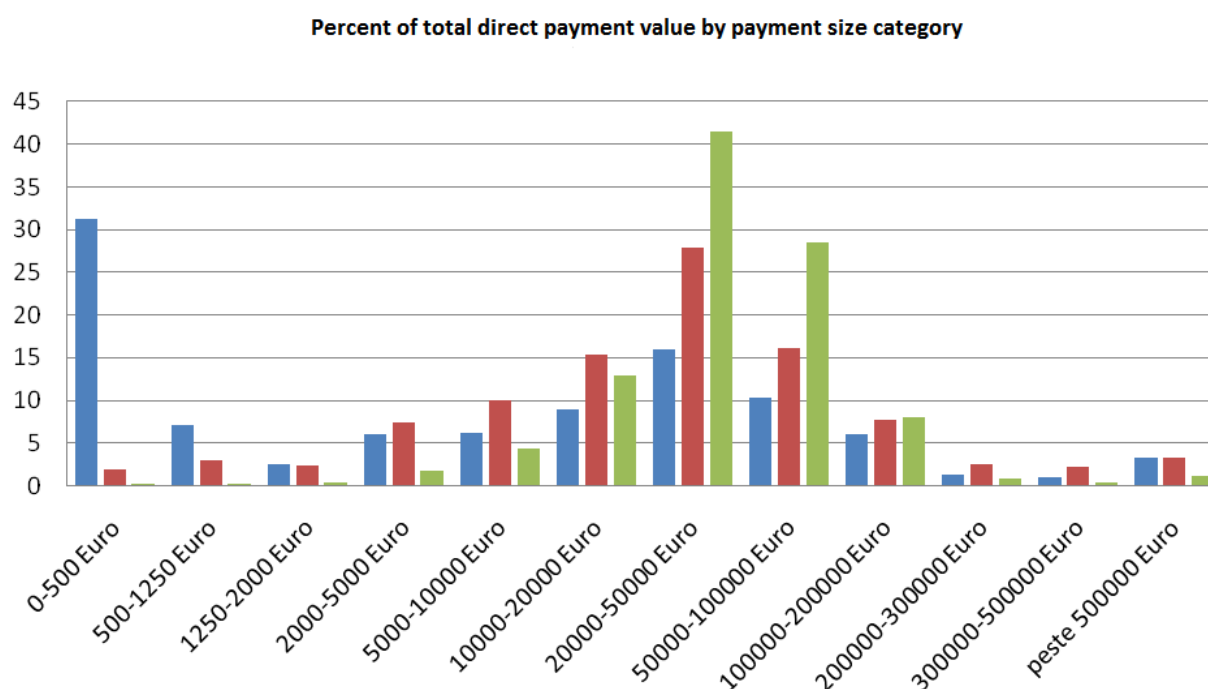
⁵ Fees differ on the basis of the nature of the land and positioning, such that we will greatly simplify matters by using an average reference value.

The effect on administrative costs ought to be spectacular in Romania's case, as long as applications for payments are only submitted by large farmers, among whom many apply online (in 2010 there were already 237,000 applications submitted online for 5,2 ha). Reducing the risk of incorrect declarations would simply be the welcome consequence of introducing this system, and it is reasonable to expect that in the future not only the costs of administering the direct payment system would be reduced but it would also eliminate most of the causes that generated the application of penalties for defective administration of payments (as happened to Romania for payments corresponding to the first year, 2007).

The Commission's searches seem to point to a new paradigm for the small European farm, such that the definition of the small farm used to grant direct payments (from the first pillar) can also be applied to the measures for rural development (from the second pillar).

Our proposal would shift the center of gravity of small farms toward farms that today – in Romania, as in other new member states – benefit from transitional measures⁶ to support semi-subsistence farmers in restructuring, that is, for farms between 2 and 8 ESU in Romania.

Fig. 2.



Maintaining farmers' incomes with direct payments

Just as CAP objectives, ample from the outset, have been supplemented by new challenges over the course of half a century of existence, direct payments today are also tied to objectives that are difficult to reach with a single instrument. Nevertheless, the EU still considers direct payments to play a key role in reducing discrepancies between the incomes of those engaged in

⁶ Of the set of transitional measures for new member states, those that are not part of the menu generally accepted by all states will probably disappear, because it is natural not to have transitional measures for agricultural operations when you require equal treatment in the distribution of direct payments.

agriculture and the incomes of those occupied in other branches of the national economy, especially industry.

Direct payments made up 27% of total agricultural incomes in the EU-27 over 2006-2008. Despite this, income per unit of labor in agriculture remained at less than half the average salary per unit of labor for the 27 members of the EU.

However, as far as direct payments are concerned, in Romania the dominant interpretation appears to be that granting financial compensation for agricultural production is justified by the goal of maintaining low food prices, in light of reduced consumer purchasing power. That is why in Romania large firms are considered by political decisionmakers to be the most entitled to benefit from direct payments. And this is probably why Romania's official position has constantly been one of opposing proposals for capping direct payments to large farmers, without taking into consideration the fact that the resulting savings at the EU level could pay for support for more small farms.

The allocation between farmers of the direct payments, according to the regulations that define the current CAP, calls into question the equitability of the distribution, as 20% of beneficiaries currently receive 80% of direct payments⁷, according to different possible analyses. For example, an analysis of the data collected by FADN⁸ for 2006, when Romania and Bulgaria were not yet members, shows that 20% of EU-25 farmers received 76% of direct payments⁹. The directional data for 2009 payments from a more recent report¹⁰ arrives at the same results: approximately 20% of farms receive approximately 80% of direct payments in the EU-15 (old member states) as well as in the EU-12 (states that have joined since 2004). Judging through the lens of the 20/80 principle, the situation is similar in Romania: an analysis of the distribution of beneficiaries and corresponding land areas eligible for payments by surface area (from European funds), according to the requests submitted in each of the years over 2007-2009, shows that 19% of farmers receive approximately 77% of direct payments.

Returning to the data for 2009 payments at the member state level, Romania's extreme model is conspicuous when it comes to beneficiary distribution, with a giant number of farmers (almost 1 million) receiving under 500 euro in direct payments from European funds, a figure surpassing Poland, which has approximately 700,000 thousand beneficiaries in this category. As the direct payments equalize (Poland has a head start of 2 years in this process), a part of the Romanian beneficiaries will pass into the category of those with payments between 500 and 1250 euro, according to the current classification. Fig. 2 shows how big the difference in distribution of direct payments by category of beneficiaries is in a country with a structure that is currently undergoing

⁷ In this context, we mention Pareto's 20/80 principle. Vilfredo Pareto observed at the end of the 19th century that, in the case of many countries, the distribution of incomes followed a cumulative law, whereby 20% of the population received a cumulative 80% of the total income.

⁸ Farm Accountancy Data Network, organized by each state and coordinated by DG AGRI.

⁹ Direct payments distribution in the EU-25 after implementation of the 2003 CAP reform based on FADN data, DG AGRI, 2008.

¹⁰ http://ec.europa.eu/agriculture/funding/directaid/distribution_en.htm

adjustment – as in Romania’s case – compared to one with a stable structure – like France –, which gives the EU-27 average limited relevance.

If the solution of a more equitable distribution is chosen, this will probably affect large farms, with small farms benefitting. However, the effects of this redistribution on the agricultural sector will only show where the number of farms is large enough (as in some new member states and in some Mediterranean countries).

Romania would be an exemplary case, because, while the 20/80 principle is also respected in the concentration of payments in Romania, the difference between the average EU-27 level (the 20% of beneficiaries that receive 80% of payments receive 5000 euro and up) and that of Romania (where the starting point for the upper 20% is around 500 euro) must be noted. In addition, while in old member states a concentration of payments exists, in Romania these are also polarized: over 90% of beneficiaries (with payments under 500 euro) receive around a third of the volume of payments, while at the other end 1% of beneficiaries (with payments over 50000 euro) also receive around a third of payments. Thus, a redistribution of direct payments in Romania would automatically become an instrument for stimulating the appearance and development of mid-sized farms.

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Areas of expertise:

- * Common Agricultural Policy
- * Internal Agricultural Policies

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