EconPol
WORKING PAPER

17
2018

September
Vol. 2

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EUROPE
econPOL
European Network for Economic
and Fiscal Policy Research

headed by

EconPol Working Paper
A publication of EconPol Europe
European Network of Economic and Fiscal Policy Research

Publisher and distributor: ifo Institute
Poschingerstr. 5, 81679 Munich, Germany
Telephone +49 89 9224-0, Telefax +49 89 9224-1462, Email Dolls@ifo.de
Editors: Mathias Dolls, Clemens Fuest

EconPol Europe: www.econpol.eu

The EU Budget and Common Agricultural Policy Beyond 2020: Seven More Years of Money for Nothing?

Friedrich Heinemann[*] *and Stefani Weiss*[**]

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Abstract

At the outset of European integration, farming featured high on the political agenda for good reason: the food security of postwar Europe was at stake. But by the 1980s, subsidies to agriculture still accounted for two-thirds of the EU budget. Today, the Common Agricultural Policy (CAP) accounts for roughly 38 percent of spending, the largest single expenditure in the Multiannual Finan-cial Framework (MFF). According to the new Commission proposal for the MFF 2021–2027, this will change only slightly. Direct payments to farmers will still constitute the largest item in the CAP budget.

This analysis looks into the two main arguments for legitimizing CAP: income protection and European public goods. Our proposal for reform starts from the premise that income protection cannot justify the current level of direct payment from the EU budget. Likewise, the public good justification, which gained substantial rhetoric importance in the MFF 2014–2020, has not come to fruition. Evidence indicates that "greening conditions", set up to protect the environment, have been largely non-binding, unproductive, and thus an un-justifiable expense. Against this backdrop, the Commission's June 2018 pro-posal on CAP's future is disappointing. We conclude that the current proposal is not in line with a sound public goods approach. Without substantial modifi-cation, direct payments will remain an ineffective incentive for the provision of agricultural services in the fields of environment, climate policy, and animal protection. In the Commission proposal, the instrument of "eco-schemes" comes closest to a model of public goods-

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related direct payments. In coming months, there are still opportunities to improve the draft. We recommend that in the future budget a certain share of direct payments – up to 50 percent of national envelopes – is spent on eco-schemes that should reflect a strict “val-ue-for-money” rationale. Eco-schemes would then define compensation for the verified provision of public goods at well-defined unit prices.

Acknowledgement: This research has been supported by the Bertelsmann Stiftung. The authors thank Christoph Harendt for his comments and suggestions.

1 Introduction

In recent months, the likely contours of post-2020 Common Agricultural Policy (CAP) have emerged. Following a first communication in November 2017 (European Commission 2017b), in June 2018 the Commission published its proposals for CAP beyond 2020 (European Commission 2018a). These cautious reform ideas have set the parameters for the coming negotiations: CAP will continue to have a two-pillar structure of direct payments and rural development, with a seven-year budget of €365 billion (current prices). As before, almost three-quarters of the budget is reserved for direct payments to farmers (€265 billion). This translates into a 5 percent cut in current prices, respectively 12 percent in constant prices (accounting for inflation), according to Commission figures.

Even with these cuts, the money allocated to CAP is still much higher than that to other budgetary items – items that better reflect Europe's urgent challenges. In this sense, opportunity costs remain immense (see Heinemann, 2017, for more CAP opportunity cost calculations). For example, in the MFF proposal the ratio between the CAP budget and all of the resources foreseen for migration and border management is 11:1, and the ratio of CAP to the total budget for security and defence is 14:1. It is thus plainly evident that the new CAP must justify its contribution to European objectives.

In fact, with the Commission´s June proposal, comprehensive reforms of the overall CAP envelope are off the table. This holds, in particular, for the phasing out of direct payments and the introduction of a national co-financing share as discussed in the June 2017 Commission Reflection Paper on the EU budget (European Commission 2017a; Heinemann 2017). Instead, the new CAP model closely resembles the current one. However, given the harsh criticism of direct payment's fairness, administrative burden, and low environmental impact, the Commission suggests modifications for direct payments including their degression according to farm size as well as capping above a certain threshold. Also, it proposes more flexibility for member states in using conditionality and incentives for "higher ambitions on environmental and climate action" while funding their farmers.

In this report, we evaluate the recent proposals for direct payments. Our perspective is based on the consensus in the scholarly discourse, namely that direct payments can only be legitimate if they effectively finance goods and services for European society that the market would not otherwise provide. We argue that Europe is currently running the risk of losing a once-in-seven-years opportunity to employ CAP instruments to foster a European agricultural sector that delivers on more ecological, climate-oriented, and animal-friendly production. Moreover, we provide arguments as to why size-dependent caps and degressive direct payments are fundamentally wrong and may be counter-productive in the light of the public goods approach.

Despite these faults, it is wishful thinking that the Commission could be send back to the drawing board. The June proposal is on the table and has significantly narrowed the leeway for reform. Still, the Commission proposal leaves room for its improvement. Thus, we set out in this paper how in the coming months the effectiveness of public good provision can be increased at least to a modest but significant extent. The eco-schemes have the potential to become the key vehicle for a public goods orientation of direct payments. Some specifications on the contents and spending shares of these schemes could offer a powerful lever to incentivize farmers to produce a verifiable quantity of public goods. If that opportunity is lost, however, Europe is about to waste a budget of €265 billion and spend enormous amounts of money for virtually nothing in terms of European added value.

In the following, we provide a brief refresher on CAP and discuss the two legitimizing arguments for direct payments – income support and public good compensation – before we discuss in more detail the Commission proposal and make suggestions for the EU budget negotiations.

2 CAP and the Emerging Public Good Legitimization

In terms of budget, CAP is the most prominent policy field at the European level. Established in 1962 by the six founding member states (European Commission 2012), today Article 39 (TFEU) defines CAP's objectives. These are to increase productivity and efficiency in the farming sector, ensure a fair standard of living for farmers, stabilize markets, ensure the availability of supplies, and ensure that this supply is provided for EU citizens at reasonable prices (see also Burrell 2009; European Commission 2012). Initially, it was intended to balance power between then industry-focused Germany and agriculture-based France. But CAP gradually evolved as enormous productivity increases and changing societal preferences led to substantial modifications over the course of time (Tangermann and von Cramon-Taubadel 2013).

Since its establishment, expectations of CAP have clearly changed. For instance, the initial idea of a self-sufficient European agricultural sector has become largely obsolete due to Europe's deep integration in diversified global food markets. Diversification of import sources has proved a more compelling guarantee for a reliable food supply than self-sufficiency, which would not protect Europe against domestic production shocks. In addition, the food preferences of European citizens have changed. Typical diets now contain substantial amounts of food types not produced in Europe (Boulanger and Messerlin 2010). Hence, self-sufficiency or targeting the balanced trade of agricultural commodities would not only result in reduced gains in trade, but it would also deprive European consumers.

Several trends create challenges for the European agricultural sector, just as they do for competing regions (Anania 2009). These include a continuing increase in demand for agricultural commodities in combination with climate change, more binding limitations on natural resources, and increasing societal sensitivities concerning animal protection (OECD 2011b). For example, agriculture is increasingly held responsible for reducing biodiversity. The effects of climate change on agriculture are unclear, but farming needs to adapt to changing climate conditions (Anania 2009). Climate change will also affect the availability of natural resources. But even without climate change, intensified farming influences the availability of natural resources, such as soil (Wall 2012) and water (Sakadevan and Nguyen 2015). The global increase in demand for agricultural commodities is driven by global population growth. Besides the growing demand for quantity, there is increasing demand for better (ecological) quality (Boulanger and Messerlin 2010).

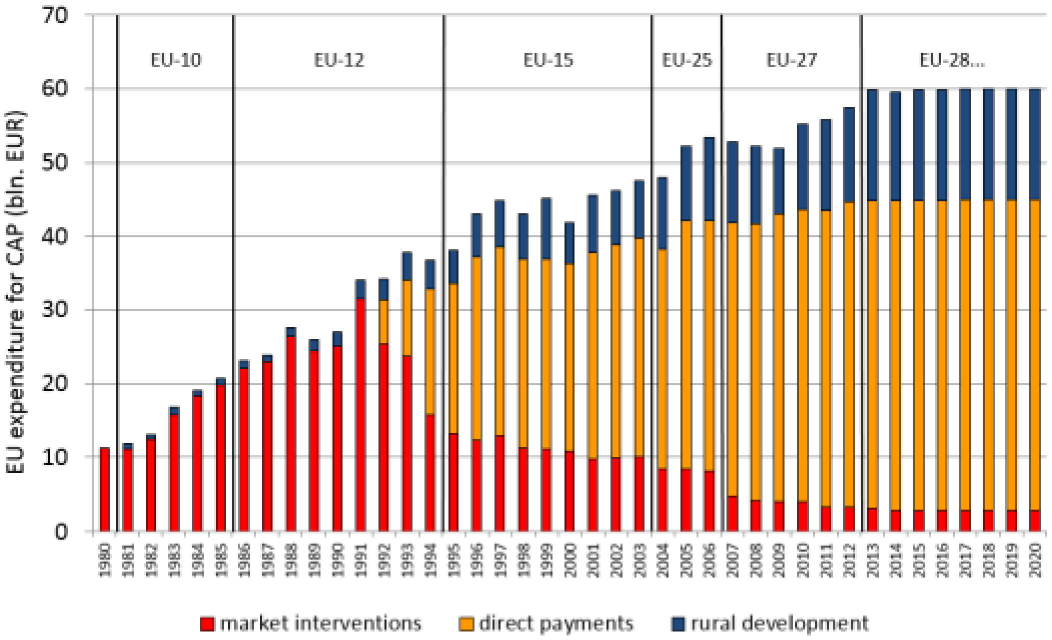
When originally introduced, CAP aimed to control commodity prices through price support, including export subsidies. This resulted not only in mismatches in demand and supply – including the infamous excess supply of commodities such as milk and butter – but also in international resistance and pressure for reform. In the course of the negotiations for WTO's General Agreement on Tariffs and Trade (GATT), the incompatibility between free trade and the CAP design become quite clear (see e.g. Weyerbrock 1998). This resulted in several reforms of CAP that sought to align it with market economy principles and improve the efficiency of its design. The most notable revisions were provided by the MacSharry reform implemented in 1992, Agenda 2000 (introduced in 1999), and the Fischler reform that took effect in 2003 (see, e.g, Ackrill 2000; Burrell 2009; Greer 2013; OECD 2011a).

The MacSharry reform was a major breakthrough in integrating the European internal market for food production into the global market: tariffs on imports were abolished, price support was cut, and quotas for suppliers were phased out. Instead of efficiency-distorting market interventions, CAP's focus was shifted to direct payments to compensate farmers for income losses. In addition, CAP's scope was broadened to include rural development. Agenda 2000 strengthened and expanded the focus on rural development. The Fischler reform ceased product support almost completely[1] and installed a decoupled system of direct payments as income support for farmers, independent of the type and amount of commodity farmed.

Figure 1 shows the transformation from the highly protectionist market-intervention system towards a system of less distortive direct payments. While the major share of CAP funding was for price-supporting measures until 1994, this has fundamentally changed with direct payments now dominant in the CAP budget.[2]

Today, CAP consists of two pillars. About three-quarters of CAP funding is dedicated to pillar one with its decoupled direct payments for farmers. Since the latest amendment to CAP in 2013, 30 percent of direct payments have been dedicated to so-called "greening" conditions for payments based on the fulfilment of environmental efforts. This pivot is clearly meant to accentuate the public good character of farming (European Commission 2013b; Matthews 2013).

Figure 1: Development of Composition of CAP Expenditures



Source: Tangermann and von Cramon-Taubadel (2013) (based on European Commission (2013a)); own calculations.

[1] A longer transition period was granted for some quotas. For example, the milk quota was only abolished for dairy farmers in 2015 and for sugar beets in 2017 (Sorrentino, Henke and Severini 2016).

[2] Since 2013, market interventions have been reduced to a negligible 5 percent of total expenditures. Market intervention now happens only exceptionally, in times of crisis (European Commission 2013b).

The new environmental public good rationale uses a combination of sticks and carrots. The sticks are embedded in “cross compliance” rules, which foresee transfer cuts for farmers who do not comply with good agricultural and environmental practices. The carrot component is greening payments. A further public good component has been installed in pillar two (rural development), where farmers are rewarded for services that benefit the environment and climate based on a contract approach with pricing for additional costs incurred by farmers (This direct pricing logic is currently absent in the greening payments of pillar one). Pillar two targets rural development and, unlike pillar one, is co-financed by member states (Cantore, Kennan and Page 2011).

In the analysis to follow, we focus on direct payments, which are the main element of CAP funding. In particular, we shed more light on the two main legitimizing arguments that refer to the social objective of appropriate income support and the view that direct payments are the price that farmers pay for the provision of public goods.

3 The Uncompelling Case for Pure Income Support from Europe

A welfare state-related argument would describe EU income support to farmers as a social policy that aids a particularly needy or deserving group in society. It is true that the share of farmers in the European workforce has dramatically declined (to just 4.25 percent of the workforce in 2017, according to World Bank data). But are farmers in comparison to other professional groups so particularly needy that they merit: a) direct income support on top of the usual welfare state income support, and b) if so, then having this additional social welfare financed from the EU budget?

The answer to the first part of this question is subjective. And, indeed, in many countries there is special emotional attachment to the farming sector and its people. But we can leave those value judgements aside and turn to the second part of the question. Even if one accepts privileged income support to farmers, should this be a European task or should we leave the responsibility to the member states and their budgets? Or to use current popular terminology: can the EU create European added value by providing income support to farmers in a way that the member states cannot?

The answer can be based on the criteria of European added value as developed in detail and applied to several policy fields by Weiss et al. (2017). Inter alia, the test applies the following criteria to judge the appropriate assignment of policies either to the national or to the European level:

- Existence of crossborder externalities: would national income support to farmers have substantial positive spill-overs to other member states so that freeriding occurs in the absence of European centralization?
- Economies of scale through European provision: could Europe provide income support to farmers at lower costs than do member states?
- Preference homogeneity of voters across member states: do Europeans across member states have similar views about the desirability of income support to farmers?
- Conflicts between national responsibility and a well-functioning internal market: would national income support to farmers constitute an obstacle to an open and undistorted internal market for agricultural products?

The more these questions can be answered in the affirmative, the clearer the case would be for European income support. However, closer scrutiny points to the opposite conclusion.

Externalities

Direct payments understood as pure income protection do not create significant cross-border spill-overs. Insofar as these payments alleviate the social problems of those in the agricultural sector, this is predominantly a benefit to the member state in terms of social and political stability.

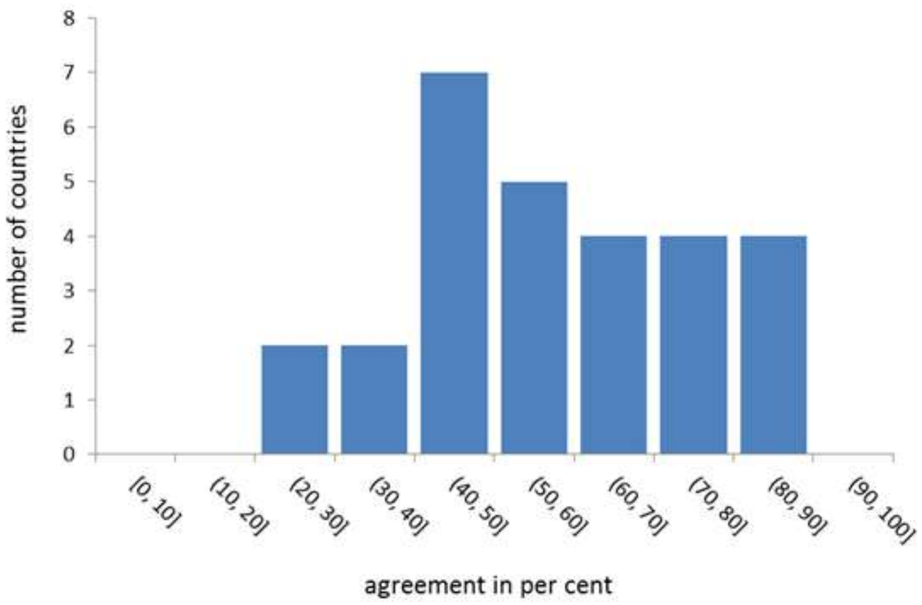
Economies of scale

EU direct payments are highly imprecise in terms of social targeting. They lack an individual income test that takes account of a farmer's full income – from all sources. Moreover, the amount of payment is determined only by the farm's size in hectares. Weiss et al. (2017) provide calculations that compare the size of average direct payments per farm with a country-specific level of income support that takes account of the (large) income differentials across member states. The results show that for the majority of member states, direct payments to the average farm are either too high or too low. Hence, it is impossible to argue that the European approach saves costs through economies of scale. Member states, with their welfare-state expertise and infrastructure, could provide much better targeted income support that corresponds to the actual income of farmers relative to income level in the specific national labour market. Hence, direct payments constitute a case of European diseconomies of scale with cost advantages for policy-making at the national level.

Member state preferences

Figure 2 (adapted from Weiss et al., 2017) investigates the acceptance of income support to farmers across member states. It relies upon the Special Eurobarometer 440 entitled "European, Agriculture and the CAP", published in October 2015. The graph illustrates the number of countries across different classes of support for higher payments to farmers. It reveals that views are very heterogeneous across member states. Popular support for an increase in financial aid to farmers differs widely between member states. The lack of agreement on the priority for special income support to farmers again points to the value of national rather than EU-level policies.

Figure 2: Eurobarometer Preferences for Higher Support to Farmers Across Member States



Source: Weiss et al. (2017); Eurobarometer question EB84.2 QC11: "And over the next 10 years, would you like to see an increase, decrease or no change in the EU financial support to farmers?" (percentage values for "increase" per country). The X axis denotes the share of answers with "increase" in the country.

Internal Market

A shift of responsibility for purely welfare-oriented direct payments from the EU level to the national level would be unlikely to create significant problems for the internal market for agricultural products. The European internal market has proven to function well despite the member states' highly diverse welfare systems. Moreover, it is a defining characteristic of direct payments since the MacSharry reforms that they are decoupled and largely non-distortive (i.e. they no not induce overproduction). Current European competition policy and state aid surveillance is sufficient to guarantee that national responsibility for farmers' income support would not degenerate into new distorting instruments.

The welfare-state argument for EU-financed income support to farmers is thus not convincing. If this is really the dominant motivation behind direct payments, then Europe should shift this responsibility to member states sooner rather than later.

4 Greening in the CAP 2014–2020 and the Failed Public Good Legitimacy

Since income protection is hardly sufficient to legitimize direct payments to farmers from the EU budget, ever more emphasis was placed on the public good rationale which now constitutes its main line of defence. Accordingly, direct payments should deliver European added value if they incentivize farmers to produce public goods that market incentives alone would not otherwise provide.

One might argue that the cross compliance conditions constraining all direct payments provide a public good dimension to direct payments as a whole. However, these conditions largely refer to the legal obligations of agricultural production, and thus do not incentivize a particularly ecological (and costly) production above current EU standards (Lünenbürger et al. 2013, S. 31). Hence, cross compliance amounts to a particularly problematic construction where farmers receive monetary compensation for respecting the law. In other sectors, the standard means to ensure compliance with legal obligations is to penalize the lawbreakers.

The greening component in the current pillar one regime, at least in principle, corresponds better to the public good logic: farmers who participate in CAP direct-payment schemes have to apply for green payments (small farms and organic farmers are considered green by definition, and are thus excluded). Farms are eligible for green payments if they fulfil conditions for crop diversification, maintenance of permanent grassland, and ecological focus areas that are conducive to biodiversity. The greening component in direct payment amounts to approximately 30 percent.

The greening approach certainly corresponds to the public good rhetoric – but not the substance. There are already limits in the way the approach is set up. If only 30 percent of payments have to be "earned" through a particular effort, this implies that 70 percent still follow the old transfer logic. The next crucial question is to what extent the 30 percent greening share of direct payments can be seen as a price for a particular contribution of farmers to the mitigation of climate change, the preservation of biodiversity, the improvement in the quality of water and soil, or animal protection above the legal minimum standards.

The bulk of independent research points in one disappointing direction:

- European Court of Auditors. In a special report, the European Court of Auditors (2017) concludes that greening conditionality has virtually no measurable environmental impact. The Court concludes (p. 6/7) that "greening, as currently implemented, is unlikely to significantly enhance the CAP's environmental and climate performance"; that the European Commission failed to "set clear, sufficiently ambitious environmental targets that greening should be expected to achieve"; that the "budget allocation for greening is not justified by the policy's environmental content"; that "greening led to changes in farming practices on only around 5 percent of all EU farmland"; "that the policy's likely results do not justify the significant complexity which greening adds to the CAP"; and that "green payment remains, essentially, an income support scheme."
- Overview of Scientific Studies. BirdLife Europe, European Environmental Bureau, and NABU have initiated a meta-analysis conducted by independent researchers (Pe'er et al., 2017) that condenses insights from 450 studies. The study concludes that greening's conditionality is seen as "insufficient to reverse negative trends due to broad exemptions, low requirements for crop diversification, lack of management criteria and the inclusion of ineffective options for Ecological Focus Areas …. Climate measures are insufficient, hardly targeting livestock production and nitrogen fertilizer use as the main sources of greenhouse gas emissions. Effects on soil and water are partly positive, partly negative". Moreover, efficiency is poor: for example, "the largest investments are made into the least effective measures from a biodiversity perspective".
- The Scientific Council of the German Federal Ministry of Food and Agriculture. The ministry's scientific council arrives at a similar conclusion: in its current form, greening is "largely ineffective with respect to the induced environmental benefit" (Wissenschaftlicher Beirat, 2018, p. 39) because there are too many exceptions. It also criticizes the greening conditions' modest goals as well as overcompensation: greening premia far exceed the burden induced through higher costs of production with higher ecological standards.

Thus, for the CAP 2014-2020 overwhelming evidence paints a clear picture of largely ineffective greening conditionality. This means that, like the income protection argument, the second possible legitimization – farmers "earn" at least some part of direct payments through environmentally friendly public goods – is deeply flawed. In fact, the political function of greening was to provide a new alibi for transfers to farmers (and landowners). In the light of the empirical evidence, it simply is not the case. Greening payments have not been effective in changing agricultural production to a degree that could justify their cost.

5 Assessing the CAP Proposal for 2021-2017

With its May 2018 proposal for the next MFF and the further specifications on CAP in June 2018, the European Commission has effectively created facts for the continuation of direct payments with limited cuts. In its financial table, the proposal foresees €265 billion (current prices) for direct payments over the years 2021–2027 with precisely defined national envelopes. This amount will be fully financed from the EU budget: no change towards national co-financing is foreseen.

This is a risky early decision. Europe continues to devote a significant part of its budget to a programme possibly without significant European added value. This would be the case if the post-2020 direct payments' conditionality is not more effective than before. According to the June 2018 package, the "new" CAP includes the following relevant features for the future of direct payments (European Commission 2018a):

– At the EU level, common objectives are defined together with a common "toolkit" which member states may take advantage of.
– Member states will have more freedom than before as to how to meet CAP's common objectives. In comprehensive national "CAP strategic plans", countries will set out how they use the tools for their own specific needs in order to meet the common objectives. These plans will also set the targets for the objectives, and the plans require approval from the Commission. Member states will assess progress on these targets through their own annual monitoring followed by a review conducted by the Commission.
– Direct payments shall be concentrated on smaller farms. There will be degression for payments in excess of €60,000 and a capping above €100,000. However, payments received are adjusted for salaries paid ("labour costs will be taken fully into account"). Matthews (2018) points out that with realistic assumptions on labour costs per hectare, the capping formula might not be binding. His empirical argument is that for most member states, labour costs per hectare are above the direct payment level (of around €250/hectare). The adjustment implies that labour costs are subtracted from the hectare premium. In most cases, the result is zero or less. Hence, the thresholds will rarely constrain payments.

- The terminology of "greening" and "cross compliance" will no longer be used. However, there are conceptually similar new conditions and instruments: direct payments remain conditional on "enhanced environmental and climate requirements," which resemble the old cross compliance rules. And member states must offer "eco-schemes" to support farmers in going beyond mandatory requirements. These eco-schemes must be funded from national direct payment allocations but farmers' participation is voluntary. However, so far there is no hint of a minimum share of direct payments to be used for the eco-schemes. The only binding number so far is that 40 percent of overall CAP "is expected to contribute to climate action" and that 30 percent of pillar two rural development is devoted to environmental and climate issues.
- Member states can no longer only transfer 15 percent between pillars (modulation). In addition, they can transfer another 15 percent from pillar one to pillar two for spending on environment and climate measures.

In the eyes of the Commission, "the new CAP will require farmers to achieve a higher level of ambition" on environmental and climate action (European Commission 2018b, p. 1). However, with the disappointing greening experience it is hard to understand the grounds for optimism. With respect to the earlier 2017 communication on the future of CAP, Matthews had already commented: "There is a huge disconnect in the Communication between the insistence that environmental and climate objectives will be given greater priority in the new CAP and the lack of any specific commitments in this section of the Communication which might deliver on this aspiration" (Matthews 2017). This criticism is hardly rebutted by gist of the June 2018 package. On the contrary, the following aspects in the proposal point to an even weaker link between direct payments and environmental public goods than before:

- Increasing flexibility: member states shall become more flexible with their use of direct payments. Flexibility relates to choice and the adjustment of tools from the common toolkit, but also to the greater leeway to shift money between CAP pillars. This hardly sounds like binding conditions on the provision of (uniformly defined) European public goods. Rather, this could invite member states to cherry pick those tools that are easy for their farmers to apply for and to maximize windfall gains for their own agricultural sector.
- Race to the bottom: increasing flexibility for member states has severe potential consequences. It might induce a race to the bottom of member states' environmental ambitions. Truly ambitious member states that use all of the available triggers to force farmers towards environmental and animal protection standards above the EU average will impose a competitive disadvantage on their domestic farmers (Wissenschaftlicher Beirat, 2018, p. 20). Farmers in member states with an ambitious "public goods regime" (direct payments as compensation for higher costs due to binding

environmental conditions) would then have to compete against farmers from member states with a "windfall gain regime" (direct payments without effectively binding conditions and lower production costs). To avoid this detrimental outcome, CAP needs to take precautions against this abuse of subsidiarity.

- Downside of "simplification": although it is desirable to cut red tape, the Commission's promise of "simplification" is ambiguous. To some extent, agricultural interest groups might simply have been successful in denouncing binding environmental conditions as a useless bureaucratic exercise (which was true with respect to the non-binding greening conditions). But an effective public good conditionality must impose a costly adjustment burden on farmers. It is precisely the existence of that burden for which farmers earn payments. From this perspective, the Commission's promise to simplify could, in part, be interpreted as a surrender to lobby pressure for unconditional transfers.
- Degression and caps on direct payments: the idea to concentrate direct payments on smaller or family-owned farms is problematic. The size of a farm is not a reliable indicator for the needs of farmers (and their employees). If direct payments should really be transformed into a welfare-state benefit (on top of national benefits) an individual means test on the comprehensive income and wealth of the receiving farmer must be introduced. Only this could identify farmers in need. But also in terms of the public good rationale, the size degression does not constitute a step forward. There is no evidence that smaller farms function in a more environmentally or animal-friendly way than larger farms (Wissenschaftlicher Beirat 2018, p. 37). Concentrating direct payments on small farms effectively promotes small and less productive farms. Taxpayers would thus compensate small firms for their lower productivity and hence give incentives for the splitting up of farms. This will not foster higher ecological standards. On the contrary, lower productivity implies higher production costs and less leeway for regulators to lift environmental standards. There is another, more subtle argument why degression further weakens reform and the movement of CAP towards the provision of societal goods (Wissenschaftlicher Beirat 2018; p. 38): namely, degression will strengthen the (false) narrative that direct payments advance fairness by assisting the needy, which makes it politically more difficult to demand something in return. This will also hold if the degression and capping turns out to be actually non-binding, as argued by Matthews (2018).

In sum, the current state of affairs does not give cause for optimism about a move towards real European added value in direct payments. If no substantive corrections occur in the ongoing legislative process, the post-2020 CAP will constitute a step backwards, making direct payments even less effective in incentivizing public good provision.

6 Triggers for Improvements in the Commission Proposal

The Commission proposal has set the stage, yet there is still time to improve the design of the new CAP. There are several levers available that could strengthen the link between direct payments and European public goods: these levers relate to instruments, verifiable conditions (above legal obligations) with adequate pricing, and binding budgetary shares.

Eco-schemes with public good potential

Conceptually, the eco-schemes put forward in the Commission proposal are one instrument in the toolkit that could bolster the public good legitimacy of direct payments. The draft regulation describes this instrument as such: “Eco-schemes voluntary for farmers … should be defined by the Member States as a payment granted either for incentivising and remunerating the provision of public goods by agricultural practices beneficial to the environment and climate or as a compensation for the introduction of these practices. In both cases, they should aim at enhancing the environmental and climate performance of the CAP and should consequently be conceived to go beyond the mandatory requirements already prescribed by the system of conditionality” (European Commission 2018c, p. 23).

This follows the logic of compensating farmers for services that they provide to society. Explicitly, compensation is only paid for services above the mandatory requirements.

Eco-schemes could provide relevant incentives, for example, by financing greenhouse-gas-reduction technologies in agricultural production, improving animal protection (e.g. through more space, higher quality of life) above the legal requirement, or the provision of ecological focus land.

Verifiable conditions above legal obligations with adequate pricing

For the public good rationale, financial compensation to farmers must correspond to the additional value that farmers provide in exchange for a payment. Eco-schemes should be used to further develop this pricing logic, which attaches a price tag to a well-defined public good provision.

It must no longer be sufficient to make a qualitative and vague argument about a more ecological form of production to qualify for a payment. Instead, eco-schemes must be derived from a “value-for-money” logic: a payment for an eco-scheme should correspond to the additional costs (or earnings foregone) induced by a change in production or – even better – to the “value” of the resulting public good.

For many types of related public goods, it is difficult to determine the value to society, such as animal quality of life or biodiversity. At least for greenhouse-gas-emission reductions, however, reference prices do exist from European emission trading, and provide a hint for an adequate price that aligns agricultural climate policies with that of other sectors in an efficient way (see Lünenbürger et al. 2013, for the possibilities of quantifying greenhouse gas reduction in agriculture). For other public goods – such as caring for higher quality animal life or for ecologically sustainable use of farmland – the unit price could be based on the costs function of farms producing at the efficient frontier or stated preference surveys. This member state flexibility should be reconsidered and limited. A uniform European definition of public outputs and a uniform pricing is highly desirable to prevent freeriding and other inefficiencies that result from national price differences for a European public good.

Necessarily, the public good approach requires extensive reporting requirements and verification. The provision of contractual environmental services to society must be evidenced as in any other field of public procurement. As explained, “simplicity” of direct payments in the sense of cutting back bureaucracy is not an objective in itself from the public good perspective. However, with effective incentives for public goods there is a fundamental difference to the current situation. Since today’s greening conditions are largely ineffective, the related bureaucracy constitutes a deadweight burden. This would change once farmers start to provide a service to society in return. The remaining bureaucratic costs must then be seen as transaction costs that are unavoidable in order to realize important European added value.

Binding national budgetary shares for eco-schemes

The voluntary introduction of eco-schemes for farmers makes sense given the logic of incentivization: farmers have the opportunity to earn money for the provision of a public good, if they choose to. However, member states should not be allowed to determine the share of direct payments invested in eco-schemes. This is an inefficient type of subsidiarity that would prompt a race to the bottom. Farmers in ecologically ambitious countries would be disadvantaged against competitors in countries that largely transfer direct payments as unconditional lump sums. Moreover, public goods financed from eco-schemes are of a European if not global dimension. If the decision on the amount of European public good is left to member states this will result in freeriding and the underprovision of these goods. Consequentially, European law must set two types of binding rules for member states:

First, there must be a binding share of the national direct payment envelope used for eco-schemes. The obvious best possible share would be 100 percent, which might not be politically feasible for the upcoming seven-year period given the farm lobbies' strongly entrenched sense of entitlement and their power to influence decision making in the EU. A lesser goal is the original greening share of 30 percent. There is a large consensus to increase the share of European public goods in the budget under the new MFF so that there should be a significant increase above 30 percent. Fifty percent could be appropriate for 2021-2027 with increasing shares after that.

Second, this minimum share must be earned in each member state through a verified contribution to a quantifiable amount of public good outputs according to the price list developed before. This might still make cherry picking possible in so far as some member states would concentrate on greenhouse gas reductions while others might see an easier way towards better conditions for animals or biodiversity. The European legislator would be free to make further conditions of minimum contributions in each of these dimensions per member state. But a certain division of labour along comparative advantages in the provision of these different types of societal services could be acceptable.

7 Conclusion

It is not too late to modify the June 2018 Commission proposal on direct payments in a way that would underscore the provision of environmental, climate, and animal-related public goods. Unfortunately, the political economy of CAP reform renders this unlikely.

The Commission's unconditional quantification of the new CAP's financial envelopes, both in aggregate and per member state, has only further strengthened the recipients' sense of unconditional entitlement. With minimum budgets fixed in an early stage of negotiations, receiving countries, farms, and their lobby groups will not be inclined to accept conditions more binding than before. This is a perfectly rational reaction from their side: windfall gains from lump sum transfers create greater welfare for them than payments in exchange for the costly provision of public goods. Furthermore, it is difficult to identify serious advocates of fundamental reforms given the overwhelming power of agricultural interest groups in all relevant national and European institutions (including the European Parliament, see Swinnen 2015).

Unfortunately, the likely outcome is that Europe will spend more than €250 billion on direct payments in 2021–2027 without significant provision of public goods in return. This would become another striking case in which European added value rhetoric stands in sharp contrast to the facts on the ground. In this sense, seven more years of money for nothing is a wasteful though realistic outcome of the coming final negotiations on CAP direct payments.

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