



Agriculture – Single Farm Payment Scheme

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This note describes the Single Farm Payment Scheme now in force for agriculture in England. Farmers now receive payments whether or not they produce anything.

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A. Background

The reform of the Common Agricultural Policy (CAP) brought about a separation between financial support and the level of production. The original CAP was based upon high support prices. The more the farmer produced the greater benefit he received from the policy. The result was over-production and huge surpluses that could only be sold abroad by means of large export subsidies. EU hopes of reaching agreement in World Trade Organisation (WTO) negotiations have led to pressure to end that system. A partial separation of subsidy from production had already been achieved in the 1992 reform that introduced Arable Area Payments. That concession allowed international agreement to be reached in the Uruguay round of trade talks. The 2003 CAP reform extended that principle to livestock farming, where support had previously been based upon the number of animals. All farmers now receive a Single Farm Payment (SFP) each year, rather than a collection of payments from individual schemes.

From the point of view of farmers the reform is considerable. However, from the trading point of view the change may be less important because the total money spent on the CAP has been guaranteed to remain at the same level from 2007 until 2013. Partly for that reason, the Doha round of world trade talks remains unresolved.

The basis for these requirements and standards and their enforcement is Council Regulation (EC) No 1782/2003 (OJ L 270, 21.10.2003) and Commission Regulation (EC) No 796/2004 (OJ L 141, 30.4.2004).

The latest information about scheme details for 2005/6 was published in October 2005.¹

B. Historic Payments or Regional Average

The Agriculture Commissioner, Franz Fischler, had intended that the SFP would be based upon the individual farmer's receipts during the reference period 2000-2002. However, at a late stage in the negotiations, the option was introduced of allowing payments to be averaged across a region. The choice of option was devolved, in the case of the UK, to individual countries. England, Scotland, Wales and Northern Ireland have each chosen a slightly different option.

England opted for the regional average. The National Farmers Union had favoured historic payments, but only managed to have the changeover period extended to eight years. Thus, for eight years SFP depends upon a combination of historic and regional average payments, with the regional average component increasing each year. Support for regional average payments came from environmental groups and from those farmers whose sectors had not benefited from the traditional CAP – notably vegetable farmers.

Originally SFP in England was to have been paid in two bands, with England divided into two areas: Severely Disadvantaged Areas (SDAs) and the rest. However, that formulation would have led to considerable redistribution of subsidy towards moorland areas from the rest of the SDAs. In April 2004, Margaret Beckett announced a three-tier system: the moorland within the upland SDA; the rest of the upland SDA; and all land outside the upland SDA.

In the short-term, there are numerous problems of detail in establishing either version of SFP. Historic payments rely upon the reference period, so that decisions had to be taken on farmers whose circumstances had changed during that reference period.

¹ Defra Press Release, *Single Payment Scheme – Defra announces arrangements for set-aside and ten month rules for 2006*, 3 October 2005
<http://www.gnn.gov.uk/content/detail.asp?ReleaseID=171567&NewsAreaID=2&NavigatedFromSearch=True>

In the longer term, the SFP will easily be incorporated into land prices. Land will be sold on the basis of what it can produce and what it will earn in SFP. The ease with which SFP can be capitalised means that the benefits go only to current farmers. Future farmers will simply have to pay more for their land in order to obtain SFP.

C. Dairy Farmers

Dairy farmers presented particular problems for the regional average payments approach. The CAP reform agreement included a 25% reduction in milk prices over four years, to be partly compensated by dairy premium payments. Dairy premium was paid to dairy farmers in England in 2004. However, Defra decided that in subsequent years that money should be included in the regional average single farm payment. That is not the position in Wales or Scotland where dairy farmers receive the dairy premium because their SFP is based on historic payments. Indeed, some English farmers have leased out their dairy quotas to Scottish or Welsh farmers with an agreement to share the dairy premium.² The Defra decision was controversial, since many dairy farmers believe that they lost their entitlement to a payment that had been intended for them. The Government explained its reasons in reply to a PQ in April 2005:

Mr. Clifton-Brown: To ask the Secretary of State for Environment, Food and Rural Affairs why the (a) dairy payment and (b) additional dairy payment are being redistributed to all farmers entitled to the single farm payment; and whether she plans to reconsider the decision to make such payments.

Alun Michael: My right hon. Friend, the Secretary of State, announced in a statement to the House on 12 February 2004, Official Report, columns 1585-1602, that all possible CAP direct payments, including the dairy premium and additional payment, would be decoupled in the UK at the earliest possible stage--that is in 2005--and that the flat rate model of the Single Payment would be adopted in England.

Those decisions were taken after very careful consideration of the arguments put forward in response to our consultation exercises on these matters. Those responses revealed a significant body of support for decoupling payments, recognising that the more fully support is decoupled, the greater the degree of freedom farmers will be given in respect of their business decisions.

A wide variety of often conflicting views were offered in respect of the Single Payment model, but our decision was ultimately guided by several key principles, namely: coherence with the Curry Commission report and our own Sustainable Farming and Food Strategy launched in 2002, in particular with the emphasis in both on bringing the industry closer to the market and on the increasing importance of environmentally-sensitive farming; consistency with our wider objectives for the Common Agricultural Policy, including greater simplicity, transparency, minimal bureaucracy and as few deductions as possible from the basic payment available; and

² "England loses milk quota", *Farmers Weekly Interactive*, 2 March 2005

the need to attract the widest possible support of the stakeholder community, for ongoing payments to farming which, we believe, requires us to move towards a system in which public money is delivering public goods. We recognise the special circumstances the dairy sector is in, but remain of the view that its long-term interests are best served by the decisions I have referred to.³

D. Cross-Compliance

The justification for paying SFP is no longer to maximise food production as it was for the high support prices in the years after the CAP was founded. Much of the political justification nowadays is based upon farmers preserving the environment. All farmers need to comply with certain basic environmental requirements in order to receive SFP, whether or not they are producing anything. That is known as cross-compliance. The Defra *Cross-Compliance Handbook 2005* gives an overview of requirements:

7. Cross compliance is divided into three sets of requirements (listed below), all of which you must meet in order to receive your single payment and other direct payments in full. You will need to comply with these three sets of requirements in respect of the whole agricultural area of the holding, regardless of the amount of land entered into the scheme.

- Maintenance of your land in Good Agricultural and Environmental Condition (GAEC). The CAP Regulations...set out a framework for GAEC standards within which each Member State decides its own detailed rules. The GAEC standards are set out in section C of this handbook. This includes a phased introduction of the requirements for soils... It is possible that further standards may be introduced – for example, Ministers have agreed to further work developing a proposed standard for undergrazing and considering the possible protection of additional landscape features. Further details will be published.
- Member States are required to maintain 2003 levels of permanent pasture. Certain measures have been put in place to ensure that England meets this requirement.
- Statutory Management Requirements (SMRs). These are domestic provisions derived from those EC directives and regulations listed in Annex III to the Council Regulation. They are already law in England so you should not have to do anything different in order to comply...⁴

³ HC Deb 21 March 2005 c540W

⁴ Defra, *Single Payment Scheme: Cross Compliance Conditions for England*, 2005 Edition
<http://www.defra.gov.uk/farm/capreform/pubs/pdf/Cross-compliance-3011.pdf>

E. Modulation and Environmental Stewardship

SFP will be reduced by a certain percentage each year to fund environmental projects under compulsory EU modulation. In addition, as part of the CAP reform deal the UK secured agreement to enable an additional national modulation rate to be levied, if a Member State chose to do so. The UK Government will make use of this flexibility to modulate for England at a higher level than the compulsory EU rate. In England this will be used to fund agri-environment spending, as part of the Government's sustainable farming and food strategy, and in particular the introduction of a new agri-environment scheme, Entry Level Stewardship (ELS). That scheme will be available for all farmers to enter. In other words, it will give them a chance to get back some of the money that they would otherwise lose because of modulation.

In 2005 the EU rate of modulation will be 3% and the additional UK rate 2%, making 5% in all. In 2006, the EU rate will be 4% and the additional UK rate 6% making 10% in all. The EU modulation rate will be at 5% in 2007 and following years. The rate of UK modulation has not been announced for years after 2006.

Environmental stewardship will be administered by “Natural England”, a new body being created by a merger of English Nature and Defra’s Rural Development Service.

According to the Defra website:

Environmental Stewardship is a new agri-environment scheme which provides funding to farmers and other land managers in England who deliver effective environmental management on their land.

The scheme is intended to build on the recognised success of the Environmental Sensitive Areas scheme and the countryside Stewardship Scheme. Its primary objectives are to:

- Conserve wildlife (biodiversity)
- Maintain and enhance landscape quality and character
- Protect the historic environment and natural resources
- Promote public access and understanding of the countryside
- Natural resource protection

Within the primary objectives it also has the secondary objectives of:

- Genetic conservation
- Flood management
- Environmental stewardship has three elements:

Entry Level Stewardship (ELS) is a 'whole farm' scheme open to all farmers and land managers who farm their land conventionally. Acceptance will be guaranteed provided you can meet the scheme requirements. If you have a mix of conventionally and organically farmed land, or if your land is farmed organically, you should apply for OELS.

Organic Entry Level Stewardship (OELS) is a 'whole farm' scheme similar to ELS, open to farmers who manage all or part of their land organically and who are not receiving aid under the Organic Aid Scheme (OAS) or the Organic Farming Scheme (OFS)

Higher Level Stewardship (HLS) which will be combined with ELS or OELS options, aims to deliver significant environmental benefits in high priority situations and areas.⁵

F. Prospects for farming

Although overall Government spending on farming is not to decline before 2013, individual farmers may find their incomes sharply reduced. That will particularly be the case if the rate of modulation is increased in later years.

In May 2005, NFU President Tim Bennett warned that small family farms could disappear:

The farmers' leader blames cheap food prices and the changes to the way European subsidies are calculated. Mr Bennett told BBC News generations of agricultural experience could be lost, and the change could be devastating for the countryside. European subsidies are moving in emphasis towards environmental stewardship and away from production. Wildflower meadows and cover for ground-nesting birds are among the habitats that will be encouraged by Brussels.

But Mr Bennett and many others in farming are warning that only big farms can make a profit in an economy based around cheap food. Organic and selling direct to the consumer through farmers' markets may offer possibilities for some farmers to make money, but there is only a limited amount of room, Mr Bennett says.⁶

That view might seem surprising in view of the public perception that farmers are being paid to do nothing and that that money is guaranteed for the foreseeable future. However, many farmers are already losing money. Their annual SFP will be lower than their payments under the previous regime because regional average payments include payments to some farmers who did not previously receive them. Further reductions will come from modulation. If world prices decline or if foreign producers gain more access into the EU market, then income from sales will also decline.

On the other hand, large competitive farms might perhaps thrive in a more competitive setting. The overall effects on the level of output and on the countryside remain unclear.

⁵ <http://www.defra.gov.uk/erdp/schemes/es/default.htm>

⁶ "Small family farms may vanish", *BBC News Online*, 17 May 2005

G. Tax Implications of Single Farm Payment Scheme

The attached Tax Bulletin Special Edition from HM Revenue & Customs sets out their views on the main points arising from Single Farm Payment Scheme
<http://www.hmrc.gov.uk/bulletins/tb-se-june05.pdf>.

H. The UK Government position on further CAP changes

The EU budget negotiations in Jun 2005 failed to reach agreement, partly because of differences over the UK rebate. The UK Government argued that further CAP reform was required. Many farmers may have been surprised by the prospect of further changes within a few months of adopting single farm payments. Margaret Beckett, the Secretary of State, explained the Government's position on 4 July 2005:

"This is not about destroying the CAP or changing it overnight but no one believes it can continue forever in its present form. It must continue to evolve through a process which respects the needs of farming and rural communities. The current debate about reform of the sugar regime is an important aspect of this evolution. The negotiations in the WTO are also a factor that will determine the CAP's future development. We also need to spend less money on the CAP. And what money we currently spend on agriculture could be better targeted on driving economic growth and competitiveness; delivering environmental progress; and boosting the rural economy. English farming can be rightly proud of the contribution it makes: in producing high-quality food; in its ability to innovate and adapt to change; and in managing the landscape for the benefit of us all.

"The dramatic take-up of new environmental management schemes by farmers is evidence of their commitment to sustainable farming. Some 4,000 applications have already been received from farmers keen to take part in the new Environmental Stewardship scheme. And the new £1 million programme I am announcing today will allow Defra to monitor the environmental impact of England's changing farming sector."⁷

I. Land Prices

People often suggest that changes to farm support will mean that farmers leave the land, so that some of it will not be farmed. That may happen in certain specific areas, notably the hills. However, one would expect any general move of that type to be reflected in land prices. The latest information does not show any decline. One would expect the figures to reflect the assured income from Single Farm Payment and that might contribute to the increase in prices in 2004:

⁷ Defra Press Notice, *UK at the forefront of CAP Reform – Beckett praises English farmers as leading the way in responding to change*, 4 July 2005

Jim Knight: The following table shows estimated agricultural land prices in England for the last 10 years. These are derived from data for all sales of agricultural land in England and give an indication of the trend in land values. They exclude land sold for non-agricultural purposes and sales of less than five hectares.

England agricultural land prices

	£ per hectare
1995	4,788
1996	6,058
1997	6,448
1998	6,134
1999	6,673
2000	7,082
2001	7,406
2002	6,896
2003	7,023
2004	7,745 ⁸

J. The EU Budget Settlement likely to reduce Single Farm Payments

An article in *Farmers Weekly* suggests that the EU Budget Settlement of December 2005 is likely to reduce Single Farm Payments by over a third:

Under the agreement, spending on direct payments and market supports (Pillar 1) will be frozen at current levels, as agreed by EU leaders in 2002. But for rural development, funding is being reined in substantially, with just 69bn (47bn) earmarked for the next seven years, compared with the 89bn (61bn) the EU Commission was originally after.

Controversially, the UK also succeeded in its plan to allow member states to apply voluntary modulation of up to 20% as a means of shifting more money from Pillar 1 to Pillar 2. This will not have to be match-funded by government.

"It seems highly likely this option will be used in the UK, but not in other member states, leading to major competitive distortions," said NFU chief economist Carmen Suarez. "The UK is the only country that currently has national modulation. Germany tried it, but then abandoned it."

If used to the full, UK farmers could see 20% of their SFPs taken by national modulation, on top of the 5% by compulsory EU modulation.

But it does not end there.

⁸ HC Deb 19 October 2005 c1017W

While the new budget fixed Pillar 1 spending at 293bn (199bn) for the next seven years, this will have to be shared out among 27 member states, not 25 as originally intended. The EU Commission estimates that the accession of Romania and Bulgaria will cost around 8bn (5.4bn). "That will take about 7% or 8% off EU15 farmers' payments due to the financial discipline mechanism," said Ms Suarez. "Combined with a 3% cut for the national reserve, farmers could be looking at a total cut in their SFPs of 36%." ⁹

The article also pointed out that the UK was likely to receive a smaller share of total development funds than before because half the money was reserved for new Member States and other money already committed to other States. The NFU estimated the decline at €20m compared to existing payments of €80m, further increasing the incentive for national modulation

⁹ "EU budget could take a third off British farmers' single payment", *Farmers Weekly Interactive*, 23 December 2005