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**COMMUNICATION FROM THE COMMISSION TO THE EUROPEAN
PARLIAMENT, THE COUNCIL, THE EUROPEAN ECONOMIC AND SOCIAL
COMMITTEE AND THE COMMITTEE OF THE REGIONS**

Towards a better targeting of the aid to farmers in areas with natural handicaps

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1. CONTEXT

In place since 1975, the aid scheme to farmers in Less Favoured Areas (LFA) provides a mechanism for supporting the continuation of farming and thus maintaining the countryside in mountain areas, in less favoured areas other than mountain (the so-called '*intermediate LFAs*') and in areas affected by specific handicaps.

Mountain areas cover nearly 16% of the agricultural area of the EU and are designated according to a limited number of physical indicators¹. Approximately 31% of the agricultural land of the EU is classified as intermediate LFA, on the basis of a wide range of criteria whose diversity throughout the EU was spotlighted by the European Court of Auditors as a possible source of unequal treatment². Only a limited proportion of farms in these areas, corresponding to 7% of total EU farms, receive an LFA payment and the average amount of the allowance significantly varies among the Member States, from 16 euro per hectare in Spain to 215 euro per hectare in Belgium.

The logic of intervention of the LFA scheme was revised in 2005. To enhance the contribution of the rural development policy to the EU sustainable development strategy, it was decided to clearly focus the objectives of the scheme on land management.

The removal of socio-economic objectives from the main aims of LFA payments - now called Natural Handicap Payments (NHP) - should be seen in the light of the availability of more targeted measures for supporting farmers' income and competitiveness as well as the wider rural economy. In a market oriented context, farmers' income is mainly sustained by decoupled direct payments and by rural development aids enhancing farms' competitiveness. The economic and social development in rural areas is mainly promoted by rural development and cohesion policy³ measures supporting the diversification into non-agricultural activities, the development of micro and small&medium sized enterprises and tourism activities, the provision of basic services.

Article 50.3 (a) of Regulation (EC) No 1698/2005⁴ provides a new definition of areas with natural handicaps other than those which are mountainous in character and than those with specific handicaps, i.e. '*areas affected by significant natural handicaps, notably a low soil*

¹ Altitude, slope, or a combination of these two factors. Areas north of the 62nd parallel are also regarded as mountain areas.

² European Court of Auditors (2003), *Special Report No 4/2003* - OJ C 151, 27.6.2003.

³ Council Regulation (EC) No 1083/2006 of 11.7.2006 laying down general provisions on the European Regional Development Fund, the European Social Fund and the Cohesion Fund and repealing Regulation (EC) No 1260/1999 - OJ L 230, 24.8.2006, p. 1.

⁴ Council Regulation (EC) No 1698/2005 of 20.9.2005 on support for rural development by the European Agricultural Fund for Rural Development (EAFRD) - OJ L 277, 21.10.2005, p. 1.

productivity or poor climate conditions, and where maintaining extensive farming activity is important for the management of the land'. However in 2005 the Council did not achieve an agreement on a possible Community wide system for classifying these areas in line with the new definition and the policy objectives. It was therefore decided to maintain the previous system in force for a limited period of time and the Commission was asked to undertake a review of the LFA scheme with a view to presenting a proposal for a future payment and designation system applying from 2010.

Despite the process of intense cooperation with national authorities and stakeholders and the scientific consultations carried out by the Commission since 2005, the limits resulting from the scale of pan-European data do not allow the Commission to present a legislative proposal underpinned by thorough analysis of a possible new delimitation system. The information necessary to assess the outcome of a new delimitation approach at detailed scale is only available – or can be collected – at national level.

With this Communication the Commission is therefore reporting on the state of play of the LFA review exercise and seeking to further involve the Member States in the analysis in order to elaborate on solid ground a proposal for an area delimitation system consistent with the EU objectives for NHP and stable over time.

2. AN OLD MEASURE WITH A MODERN RATIONALE

According to the evaluation carried out on behalf of the Commission and completed in 2006⁵, the LFA scheme has been effective in maintaining land use in marginal areas of the EU.

Whilst being a relatively old measure, the fundamental objectives of the natural handicap scheme as cast in Council Regulation (EC) No 1698/2005 remain relevant to the needs of substantial areas of the farmed countryside in the EU: continued agricultural management in areas where the intensification has not occurred because of physical constraints, supports in general the maintenance of valued open landscapes, semi-natural habitats and biodiversity; it can assist in the control of forest fires and contribute to good soil and water management.

Within the overall architecture of the Common Agricultural Policy (CAP), NHP have a distinctive role alongside other policy instruments, while being evidently interlinked with other land-based aid schemes.

Whereas the Single Payment Scheme (SPS) introduced in 2003⁶ aims in the first instance to sustain farmers' income by providing direct income support, NHP aim at preventing farmland abandonment in areas particularly exposed at the risk of marginalisation by providing compensation for the specific disadvantage causing this risk.

The SPS includes the obligation to keep agricultural land in Good Agricultural and Environmental Conditions (GAEC) to prevent under-management and abandonment.

⁵ IEEP (2006), *An evaluation of the Less favoured Area measure in the 25 Member States of the European Union*, http://ec.europa.eu/agriculture/eval/reports/lfa/index_en.htm.

⁶ By Council Regulation (EC) No 1782/2003 of 29 September 2003, repealed and replaced by Council Regulation (EC) No 73/2009 of 19 January 2009 establishing common rules for direct support schemes for farmers under the common agricultural policy and establishing certain support schemes for farmers, amending Regulations (EC) No 1290/2005, (EC) No 247/2006, (EC) No 378/2007 and repealing Regulation (EC) No 1782/2003 - OJ L 30, 31.1.2009, p. 16.

Complying with GAEC is potentially more onerous for farms in the LFA because of low yields and returns per hectare. However, the single payment per hectare is generally lower in LFA than on farmland outside the LFA, because of historic yields. In these areas, where progressive abandonment is more probable than elsewhere and farming is most important from an environmental perspective, NHP provide a specific instrument for supporting continued agricultural management.

The scope of NHP is also quite distinct from that of agri-environment payments which cover the income foregone and costs incurred linked to specific environmental commitments going beyond the mandatory baseline. NHP only compensate the natural disadvantage by covering the additional costs and income foregone related to the natural handicap. They therefore provide a basic form of support to appropriate forms of agriculture to remain in activity.

Despite this structural distinction from the agri-environment measure, NHP clearly contribute to environmental objectives. They fall under Axis 2 of the rural development policy and aim at contributing, through continued use of agricultural land, to maintaining the countryside and to maintaining and promoting sustainable farming systems.

Finally, it should be pointed out that this review exercise has limited scope; it does not include an in-depth assessment of NHP position within a modernized CAP and of the interplay with other land-based payments to farmers; these issues may be further addressed within the discussion on the future development of the CAP.

3. WEAKNESSES IN THE IMPLEMENTATION

Against the strengths mentioned above, a number of significant weaknesses in the LFA implementation were highlighted by the above mentioned report of the Court of Auditors in 2003, casting a shadow over the effectiveness and the efficiency of the scheme, namely as regards the delimitation of intermediate LFAs.

Several critical points raised by the Court have already been addressed. Regulation EC (No) 1698/2005 revised the approaches for calculating the payment and for classifying intermediate LFAs, and linked them both unequivocally to natural handicaps for agriculture, minimising the risk of overcompensation. It also introduced the requirement for NHP beneficiaries to respect cross compliance⁷, with a view to provide a simpler and more coherent approach compared to the good farming practices previously applied. A reinforced monitoring and evaluation of the measure was set up within the Common Monitoring and Evaluation Framework applying to all rural development interventions for the programming period 2007-13, while Regulation (EC) No 1975/2006⁸ provided more specific rules on controls and sanctions.

⁷ Regulation (EC) No 1782/2003 established the principle that farmers who do not comply with certain requirements in the areas of public, animal and plant health, environment and animal welfare are subject to reductions of or exclusion from direct support. This 'cross compliance' system, maintained under Regulation (EC) No 73/2009, applies also to rural development payments linked to land or animals.

⁸ Commission Regulation (EC) No 1975/2006 of 7 December 2006 laying down detailed rules for the implementation of Council Regulation (EC) No 1698/2005, as regards the implementation of control procedures as well as cross-compliance in respect of rural development support measures - OJ L 368, 23.12.2006, p. 74.

The problems that remain to be tackled within the current review exercise are the lack of transparency of the systems used by the Member States for classifying intermediate LFAs, the insufficient targeting of the aid on sustainable land management, notably by targeting on the situations most in danger of land abandonment and the need to achieve the common area classification approach.

4. MAKING THE LFA DELIMITATION SYSTEM MORE EFFECTIVE

4.1. Shortcomings of the present classification of intermediate LFAs

The current classification of intermediate LFAs, based on the three typologies of indicators listed in Article 19 of Regulation (EC) No 1257/1999⁹, raises serious questions about the effective and targeted use of the funds allocated to the scheme, for two main reasons.

It is partially based on socio-economic criteria that no longer reflect the core objectives of NHP and have been inherited from the original approach of the scheme which is now out of date. Furthermore, the evolution of the demographic and economic data used has not been taken into account to up-date the delimitation.

In addition, it has occurred with reference to a wide range of national criteria often not comparable at a European level. This diversity significantly reduces transparency and may lead to an insufficient targeting of the aid in the light of the objectives of the measure.

In 2005 the legislator redefined the areas with natural handicaps other than those which are mountainous in character and than those with specific handicaps as areas affected by significant natural handicaps, as mentioned in section 1 above. Starting from the new definition, the Council intended to set up a number of objective common criteria for designating the eligible area, as mentioned in the recitals of Regulation (EC) No 1698/2005.

The discussions preceding the adoption of the regulation showed that it was not possible to reach an agreement on an area classification method based on a number of proxies reflecting poor soil qualities and unfavourable climatic conditions (e.g. average cereal yields, % of permanent grassland, livestock density). The need for an in-depth technical cooperation with the Member States in order to identify objective and scientific-based delimitation criteria became evident.

In a first step, the Commission departments tasked the Joint Research Centre (JRC) to derive a set of common soil and climate criteria which could support a new delimitation of intermediate LFAs. In order to carry out this task, a panel of soil, climate and land evaluation high-level experts was established and its work was co-ordinated by JRC. The expert panel identified eight soil and climate criteria indicating, at a certain threshold value, severe limitations for European agriculture. They are listed in the technical annex to this Communication which includes also some technical details regarding their definition and justification.

⁹ Poor productivity of the land; economic performance in agriculture appreciably lower than the average; a low or dwindling population predominantly dependent on agricultural activity (Council Regulation (EC) No 1257/1999 of 17 May 1999 on support for rural development from the European Agricultural Guidance and Guarantee Fund (EAGGF) and amending and repealing certain Regulations - OJ L 160, 26.6.1999, p. 80) .

The biophysical criteria identified by the expert group of scientists through the JRC network can be used anywhere in Europe to discriminate land presenting severe limitations for agricultural production on the basis that soil and climate data of sufficient spatial and semantic detail are available.

They can be applied to designate areas affected by natural handicaps for agriculture in a relatively simple way: an area is considered affected by significant natural handicaps if a large part of its utilised agricultural land (at least 66%) meets at least one of the criteria listed in the table at the threshold value indicated therein. The biophysical criteria are therefore not cumulative. Any indicator can trigger the classification provided that the characteristics related to such criterion are observed and appropriately measured in the area, at the associated threshold value.

The thresholds should be considered as a minimum level of handicap to be met for classifying an area as constrained; the Member States would have the possibility to raise the threshold level if this is not discriminatory and justified by national circumstances.

4.2. Preliminary assessment of the biophysical criteria and data limits

The biophysical criteria mentioned above represent a promising approach for setting up an objective and transparent system for designating areas according to Article 50.3(a) of Regulation (EC) No 1698/2005. They have been therefore used as a basis for the area delimitation envisaged in three out of four options for reviewing the LFA system submitted to public consultation on 22 May 2008 and described in the impact assessment report accompanying this Communication.

They have been extensively discussed in over one hundred meetings held by the Commission departments and the Member States since November 2007. The investigations made until now in cooperation with the national experts suggest that they are robust, based on sound science and allow classifying land homogeneously throughout the EU. They provide a simple and comparable system for LFA designation, unambiguously linked to soil and climate handicaps for agriculture and implementable by all the Member States in a relatively short period of time, although requiring administrative effort to be put in place.

The assessment of the common criteria made until now cannot however be regarded as exhaustive, because of the lack of adequate data at EU level. The pan-European data available are not adapted for an application of the criteria at a detailed territorial scale and for an assessment of its impact at such detailed scale. For that reason and in order to avoid anomalous results, the active involvement of the relevant Member States' authorities in further analytical work is envisaged as a necessary intermediate step before tabling a legislative proposal.

The cooperation required from the Member States aims, on the one hand, at simulating the application of the common criteria on the basis of sufficiently detailed soil and climate data.

On the other hand, the simulation should include adequate elements ensuring that the areas where the natural handicaps have been offset are not granted LFA status, as discussed in the following section.

5. TARGETING THE AID TO EXTENSIVE FARMING SYSTEMS IMPORTANT FOR LAND MANAGEMENT

5.1. Excluding areas where farming has overcome natural handicaps

The intensity of farming systems is often a reflection of natural conditions: areas where natural handicaps have not been offset by human intervention and technological progress are in general characterized by low-input, low-output farming systems due to the physical constraints farmers face.

Thanks to technical progress and human intervention, farmers have in several cases managed to overcome successfully the natural handicaps and are able to carry out profitable agriculture in areas where the natural conditions were at the origin quite unfavourable. In such cases, the intrinsic natural characteristics of the area remain unchanged, so on the pure basis of the biophysical criteria the area would be designated as severely constrained for agriculture. However, the handicap does not impact on agricultural productivity and there is no justification for classifying the area as affected by natural handicaps. As an example, many wet areas were artificially drained and are now highly fertile; however the artificial drainage has not changed the intrinsic character of the soil type, which will still classify as poorly drained.

It is therefore necessary, for the cases where the natural handicaps can be overcome, to fine-tune the area delimitation by applying the biophysical criteria in combination with appropriate production-related indicators.

The handicaps resulting from poor drainage, soil texture, stoniness, rooting depth and chemical properties, as well as soil-moisture balance are those most commonly offset by farmers thanks to investments, farming techniques and appropriate crop choices. The simulations made on the basis of these criteria should therefore systematically exclude:

- (a) artificially drained areas when applying the poor drainage criterion;
- (b) areas with high proportion of irrigated land when applying the soil-moisture balance criterion;
- (c) areas for which soil problems (soil texture, stoniness, rooting depth and chemical properties) are clearly overcome and where relevant production-related indicators (average cereal yield or livestock density or standard gross margin per hectare) are comparable to the national average (excluding, where appropriate, mountain areas).

The technical annex accompanying this Communication provides more details about the required fine-tuning of the area delimitation in relation with the different types of natural handicap and the associated biophysical indicators.

5.2. Eligibility rules at farm level

Limiting the eligible zones to those actually suffering from natural handicaps is a *sine qua non* for targeting the aid to areas at risk of marginalisation and land abandonment and where extensive farming is important for land management.

Beyond the area delimitation, appropriate eligibility rules applied after the process of area delimitation within the zone designated as disadvantaged, in order to target the aid to the farms complying with the objectives of the scheme are a useful tool for directing the aid to areas for which the hazard of abandonment is greatest. Different agricultural practices may in fact coexist in the same area, where some farming systems have overcome the natural handicap through intensification processes.

Eligibility rules at farm level are already widely used by the Member States today, although according to the evaluation many of these are inessential to the main objectives of the measure and reflect a wide variety of objectives and administrative requirements. Their consistency with the objectives of the scheme and with the international commitments of the EU can be enhanced, while leaving a sufficient margin of manoeuvre for addressing local peculiarities, in respect of the principle of subsidiarity.

The use and definition of eligibility rules at farm level is discussed in the options identified within the ongoing impact assessment and described in the report accompanying this Communication. The examination of this component of the payment system will be further developed when preparing the legislative proposal, taking also into account the impact of a possible new delimitation system based on the simulations carried out by the Member States in response to this Communication.

6. SIMPLIFICATION POTENTIAL

Establishing a common set of delimitation criteria would simplify the implementation of the NHP scheme at EU level, as the almost 100 indicators currently applied by the Member States at different threshold values, would be replaced by 8 criteria clearly defined and associated with the same minimum thresholds all over the EU territory.

The transparency resulting from this simplification should provide more efficiency in the implementation, in terms of transposition and compliance with the objectives.

One biophysical indicator would be sufficient for classifying an area as affected by natural handicap, while in the current system an area needs to exhibit all the three types of handicaps mentioned in Article 19 of Regulation (EC) No 1257/1999 for being designated (see footnote 9).

It is clear however that the application of common biophysical criteria requires start-up costs that will be different among the Member States depending on the quantity and the quality of the soil and climate data available.

At present 13 Member States use 'index systems' for designating intermediate LFAs. These are methodologies based on several indicators combined for calculating an index used for classifying the areas according to specific thresholds or classes. There are, in a number of cases, similarities between the index systems used in different Member States. However it is difficult to compare these systems against each other, since even when they are based on the same type of information, different weighting methods or classifications are then used to calculate the index.

The degree of complexity of the 'index systems' is variable, but is in general higher than the biophysical indicators considered for this review. Many of the index methodologies include the biophysical criteria identified by the experts and listed in the technical Annex

accompanying this Communication. In some cases the 'index systems' can be considered more sophisticated than the biophysical criteria and therefore able to better capture the presence of handicaps in an area. However, setting up a common index system to be applied consistently by all the Member States would require a huge effort in terms of design, data collection, analysis and implementation. Therefore, the establishment of a pan-European index system as a means of well capturing the presence of natural handicaps would neither be efficient nor realistic.

In the Member States where the current LFA delimitation is based on proxies of poor land productivity, an area designation process based on common biophysical criteria would probably require an effort for collecting and harmonizing soil and climate data at the appropriate scale.

In the light of these scale data issues, trade-off between simplification and effectiveness of new delimitation methods could be identified by the Member States when simulating the application of the biophysical criteria. If significant, they should be considered in the impact assessment preceding the legislative proposal of the Commission.

7. BUDGETARY IMPACT

This review exercise is neutral as regards the EU and the national budgets, since the financial allocation of the LFA scheme, composed of the contribution of the European Agricultural Fund for Rural development and of national co-financing, is decided in the framework of each Rural Development Programme, within the limit of the overall appropriations attributed to the Member State to support rural development in a given programming period. A change in the financial need resulting from a better targeting would move the resources available to other measures within the programme.

8. CONCLUSIONS AND TIMETABLE

The aid scheme to farmers in areas with natural handicaps needs to be reviewed in order to adapt the intermediate LFA delimitation and payment system to the land management objectives decided in 2005, to improve its transparency and objectivity while giving due weight to national and regional peculiarities, and to promote the targeting of the aid to the situations for which the hazard of land abandonment is greatest.

Setting out a common framework for classifying areas with natural handicaps, other than those which are mountainous in character and those with specific handicaps, on the basis of common objective criteria would enhance the transparency, the robustness and the coherence of the area delimitation system throughout the EU.

The data available to the Commission at pan-European level are not sufficient for carrying out a simulation at detailed scale of the application of possible common criteria identified during the impact assessment, which should underpin a legislative proposal to make the NHP scheme more effective.

In order to facilitate the achievement of the Community's tasks, and in particular to provide a solid basis for elaborating the required legislative proposal, the Commission suggests that Member States be invited to simulate the application on their territory of the biophysical criteria listed in this Communication and to produce maps of the areas that would result

eligible under such simulations. The simulations should show the area that would be delimited according to the biophysical criteria appropriately fine-tuned, when necessary and according to the indications provided in the technical annex accompanying this Communication, in order to exclude the areas where the natural handicap has been overcome.

The simulations should be carried out at a sufficiently detailed territorial level, e.g. LAU 2 in the nomenclature of territorial units for statistics.

They will not be considered as a new LFA delimitation but will constitute a valuable means of gauging the feasibility of the review options identified and eventually underpin a future legal proposal setting up the framework for a new LFA delimitation in a long-term perspective.

The Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions are invited to discuss the main lines of this Communication. The Member States should be invited to carry out the above simulations and send the resulting maps to the Commission services during the six months following the adoption of the present Communication.