Partial Business and Regulatory Impact Assessment

Title of Proposal
Common Agricultural Policy (CAP) – Direct Payment Regulation

Purpose and intended effect

- **Background**

  The Common Agricultural Policy (CAP) is an EU Policy that was created in the 1957 Treaty of Rome and has undergone several reforms since to address the needs of a changing world.

  The 'Agenda 2000' reforms divided the CAP into two 'Pillars': production support (Pillar 1, Direct Payments) and Rural Development (Pillar 2).

  A new rural development policy was then introduced to support rural initiatives while also helping farmers to diversify, improve their product marketing and re-structure their businesses.

  The emphasis of the CAP has gradually changed from a principle focus on productivity to gradually include a focus on competitiveness and sustainability. The reforms in 2003 took this forward with the introduction of the Single Farm Payment Scheme (SFPS) and the decoupling of support payments from the level of production.

  Much of the funding remains in Pillar 1, and is paid out to farmers and land managers in decoupled direct payments, the Single Farm Payment (SFP).

  The CAP is currently undergoing reform in Europe with significant changes being introduced for future Direct Payments (Pillar 1).

  The SFP is being replaced by the Basic Payment Scheme (BPS) which is supplemented by top-up payments such as the mandatory “Greening” and Young Farmer Payments and optional payments as decided by Member States such as Voluntary Coupled Support, Redistributive payment, etc., to give a total direct payment for each business.

  The UK Direct Payments (Pillar 1) allocation (National Ceiling) from Europe for the 2013 – 2019 scheme years is €25.061 billion, of which Scotland’s allocation (Scottish Ceiling) for the period is €4.096 billion.

This is broken down into annual ceilings as per the table below.

Scheme Year	UK	Scotland
2013	3,650,000,000	596,600,000
2014	3,548,576,000	580,014,747
2015	3,555,915,000	581,214,307
2016	3,563,262,000	582,415,174
2017	3,570,477,000	583,594,466
2018	3,581,080,000	585,327,526
2019	3,591,683,000	587,060,586
Total €	**€25,060,993,000**	**€4,096,226,806**

- **Objective**

  Scottish Government objective is to ensure the CAP reforms help deliver a sustainable and vibrant agriculture sector in Scotland that delivers on the Wealthier & Fairer and Greener Strategic Objectives of the Scottish Government's National Performance Framework.

  In particular, a sustainable and vibrant agriculture sector will help deliver the following National Outcomes;
  - We realise our full economic potential with more and better employment opportunities for our people,
  - We value and enjoy our built and natural environment and protect it and enhance it for future generations,
  - We reduce the local and global environmental impact of our consumption and production.

- **Rationale for Government intervention**

  The rationale for the CAP is determined at a European level. The Direct Payment regulation refers to the document that sets out the challenges the CAP seeks to address: "The CAP towards 2020: Meeting the food, natural resources and territorial challenges of the future". In the document the European Commission expresses a rationale for CAP support:

  "Together, the present set of policy measures results in what is the main contribution of the CAP – a territorially and environmentally balanced EU agriculture within an open economic environment. Delivering more public benefits in future will require a strong public policy because the goods provided by the agricultural sector cannot be adequately remunerated and regulated through the normal functioning of markets.
  Withdrawing public support would lead to greater concentration of agricultural production in some areas with particularly favourable conditions, using more intensive farming practices, while the less competitive areas would face marginalisation and land abandonment. Such developments would result in increased environmental pressures and the deterioration of valuable habitats with serious economic and social consequences including an irreversible deterioration of the European agricultural production capacity".

The section on the policy orientation is more specific in relation to the rationale underpinning the European policy instruments for direct payments:

"The necessary adaptations of the direct payment system relate to the redistribution, redesign and better targeting of support, to add value and quality in spending. There is widespread agreement that the distribution of direct payments should be reviewed and made more understandable to the taxpayer. The criteria should be both economic, in order to fulfil the basic income function of direct payments, and environmental, so as to support for the provision of public goods".

However, as the final Pillar 1 regulation is the result of collective deliberation between the European Commission, the European Parliament and the European Council, there are other interpretations of the role of Direct Payments have emerged.

The European Commission's rationale for intervention reflects some of the conditions faced by Scottish agriculture. Scotland has a very diverse agriculture sector with a large proportion (85%) of our agricultural land being classified as Less Favoured Area (LFA). Europe defines LFA as areas that are in danger of abandonment of agricultural land-use and where the conservation of the countryside is necessary.

The CAP plays a vital role in ensuring that many of Scotland's farms survive financially and is therefore hugely important in sustaining not just agriculture but our rural communities that depend on agriculture. Agriculture is important to Scotland. It directly generates an income of around £635 million and supports a workforce of around 65,000.

The reformed CAP Direct Payment Regulation allows a degree of flexibility in how it may be implemented. This is essential to enable Scottish Government develop a CAP that works for the whole of Scotland.

Scottish Government, after consultation with stakeholders, will use some of the flexibilities permitted to tailor the CAP to the needs of Scottish agriculture.

Consultation

- **Within Government**
  Within Government consultation on the policy has involved the following teams;
  CAP Reform and Crop Policy
  Rural Development Policy
  Natural Heritage Management Policy
  Livestock Policy
  RESAS (Rural Science and Analysis Unit)

RPID (Rural Payments and Inspections Directorate)
SGLD (Scottish Government Legal Directorate – Rural Affairs Division)

Project teams including representatives from the areas listed above were set up to consider various aspects of the Direct Payment Regulations i.e. the move to area based payments, voluntary coupled support, greening, etc.

The work of the project teams has been used in the development of the Scottish Government position on the CAP and to inform stakeholders.

- **Public Consultation**
  Public Consultation will take place from 16 December 2013 for 12 weeks.

  There has been an on-going informal consultation throughout the policy process via the Scottish Government's CAP Stakeholder Group. The Stakeholder Group meets regularly and minutes of the meetings along with papers, reports, etc., prepared for the meetings are posted on the CAP pages of the Scottish Government website and can be viewed at; http://www.scotland.gov.uk/Topics/farmingrural/Agriculture/CAP/regulations

  There has also been 2 conferences on the CAP and several meetings with stakeholder bodies during the process.

- **Business**
  During the consultation period it is planned to have face to face discussions with farmers and crofters in different geographical areas and from the various sectors in Scottish Agriculture, including arable, beef, dairy, sheep, crofting, etc.

OPTIONS

<u>Option 1 – Do Nothing</u>

- This option would mean not implementing the EU reforms to CAP.

- **Sectors and groups affected**
- The Sectors and Groups primarily affected would be the agriculture sector, farmers, crofters, land managers, suppliers to the agriculture sector, the food processing industry, rural communities, etc.

- **Benefits**
- The benefit of this option would be a reduction in the administrative burden on the industry in terms of not having to complete and submit forms such as IACS (Integrated Administration and Control System) and a reduced number of inspections.

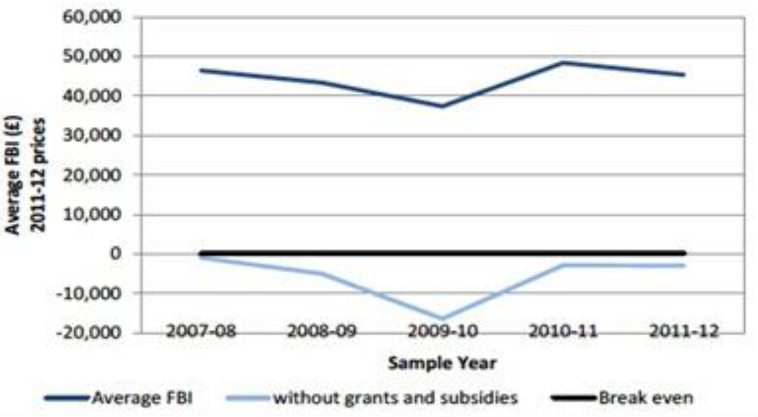
- For Government there would also be a reduction in administration costs through not having to process claim forms, carry out inspections and make payments.

- **Costs**
- The cost to the industry would be the loss of direct payments which are crucial to the survival of many businesses in the agriculture sector.

- For Government the cost would take the shape of financial penalties imposed from Europe for failing to implement Regulations.

- The Chart below, from the Economic Report on Scottish Agriculture 2013 Edition, shows the overall impact of grants and subsidies on the average income of farm businesses. The trends of Farm Business Income (FBI) remain largely unchanged, with the exception of the latest year (2011-12), when FBI without grants and subsidies showed no change on the previous year. In all of the last five years, average FBI (in 2011-12 prices) has been below zero when grants and subsidies are removed.

Average FBI of Scottish farms without grants and subsidies, 2007-08 to 2011-12



<u>Option 2 – Implement CAP Reform</u>

- Implementing the reformed CAP Direct Payment Regulation is a regulatory requirement and places certain mandatory obligations on Member States / Regions but also contains a degree of flexibility in how it may be implemented by including several optional measures for Member States / Regions to consider.

- Two of the biggest decisions for Scotland in implementing the CAP are Regional allocation of the CAP and Flexibility between Pillars.

- **Regional allocation of National Ceilings** – The Regulation states that Member States **<u>may</u>** decide to apply the Basic Payment Scheme at regional level.

- The UK Government has already indicated that as at present the National

Ceiling will be split into regions England, Scotland, Wales and Northern Ireland. Details of Scotland's direct payment ceiling is included in the Background section above.

- UK Government has said it is up to Scottish Government how to implement the CAP in Scotland. Scottish Government can choose to create sub-regions within Scotland based on objective and non-discriminatory criteria and on how to split its budget ceiling between the different payment regions. Cabinet Secretary has intimated he is minded to create 2 or 3 payment regions in Scotland based on land type.

- Several scenarios for payment regions have been modelled by the James Hutton Institute and Scottish Government analysts. The modelling process is on-going and stakeholders are kept informed of progress through the CAP Stakeholder Group. Modelling and other information is available on the CAP Reform pages of the Scottish Government website and can be viewed by following the links below.
- http://www.scotland.gov.uk/Topics/farmingrural/Agriculture/CAP/regulations/Meetings-2013

- **Flexibility Between Pillars** – The Regulation provides that Member States/Regions **<u>may</u>** transfer up to 15 % of their Pillar 1 Ceiling to Pillar 2 for use in relation to Rural Development measures. The Regulation also includes a provision for some Member States, including UK, that they **<u>may</u>** transfer up to 25% of the Pillar 2 ceiling to Pillar 1 to be used for Direct Payments.

- Cabinet Secretary has intimated that because of Scotland's very low Pillar 2 budget allocation it is likely that Scotland will transfer funding from Pillar 1 to Pillar 2 but not from Pillar 2 to Pillar 1.

- A decision on the percentage transfer has to be notified to Europe by the end of 2013. A mini consultation by Scottish Government is proposing a transfer of 9.5% from Pillar 1 to Pillar 2.

- Once the final decision has been taken and notified, Europe will calculate the amount to be transferred for the duration of the CAP up to 2019 and issue revised annual national/regional ceiling's for each Member State. In the case of a transfer from Pillar 1 to Pillar 2, it means that the amount transferred is no longer available for direct payments and all further decisions have to be made in line with the revised national/regional ceiling.

- If Scotland were to transfer 9.5%, it would result in transferring around €55m to €56m, a year. A transfer of the maximum 15% would result in transferring roughly €88m a year.

- *<u>Figures used in this BRIA assume a transfer of 9.5% from Pillar 1 to Pillar 2.</u>*

- **Mandatory obligations - Where there is a degree of flexibility this has been highlighted**.

- **Agricultural Activity** – Scottish Government has argued that future direct payments should only go to active farmers, closing the loophole that currently allows so called “slipper farmers” to claim subsidies on land that naturally meets the GAEC (Good Agricultural and Environmental Condition) requirement without carrying out any activity.

- The Regulation requires Member States/Regions to establish a minimum activity on areas naturally kept in a state suitable for grazing or cultivation, the so called “Scottish Clause”, Article 4 (1)(c) of the Regulation. The European Commission will set out what constitutes a minimum activity level and the type of land it should be applied to in Delegated Acts.

- At this point in time it is not clear what the Commission view as an acceptable level of activity. The latest position in the draft Delegated Acts suggests that the activity shall not require any production, rearing or growing of agricultural products. This would make implementation of the Scottish Clause very difficult.

- It is difficult to clarify how much direct support goes to inactive farmers, the Brian Pack Inquiry estimated around €30 million per year, or just over 4% of the current budget. This equates to approximately 4.4% of the area currently used to activate entitlements.

- **Active Farmer** – Under the Regulation no direct payments are to be granted to persons whose agricultural area is mainly an area naturally kept in a state suitable for grazing or cultivation and who do not carry out the minimum activity established by the Member State / Region.

- In addition no direct payments are to be granted to persons who operate airports, railway services, real estate services, permanent sports and recreational grounds.

- Member States / Regions **<u>may</u>** on basis of objective and non-discriminatory criteria add to the list of businesses that are to be excluded from receiving direct payments and **<u>may</u>** also decide that no direct payments are granted to persons whose agricultural activities form an insignificant part of their overall economic activity and/or whose principal company objectives do not consist of exercising an agricultural activity.

- The exclusion of certain businesses, etc., does not apply to farmers whose direct payments in the previous year do not exceed an amount to be decided by Member States /Regions, but that amount shall not exceed €5000.

- **Minimum Requirement for receiving direct payments** - Member States / Regions shall decide not to grant direct payments where total amount in a given calendar year is less than €100 or where the eligible area of the holding for which direct payments are claimed is less than 1 hectare.

- Member States / Regions **may** adjust those thresholds to take account of structure of their agricultural economies within certain limits, For UK those limits are €200 or 5 hectares.

- The current threshold in Scotland is 3 hectares, if this were increased to 5 hectares, around 2% of businesses currently receiving direct payments and 1% of land currently used to claim direct payments would be excluded. In the consultation n document Scottish Government do not propose to change the threshold.

- **Reduction of the Payment (Degressivity)** – A reduction of at least 5% shall be made on Basic Payments exceeding €150,000 with the money going to Pillar 2.

- The reductions do not apply to Greening Payments, Young Farmer Payments or to any of the optional types of direct payments such as coupled support. Salaries can also be excluded from these reductions.

- Member States / Regions **may** set a higher level of degressivity including an overall cap on payments above a certain limit.

- It is difficult to estimate how much the reduction would generate since no decisions on the number and make up of payment regions for Scotland or the budget allocations to those regions have been taken.

- Based on the value of current Single Farm Payments, we estimate that if the move to area-based Basic Payments is phased in up to 2019, then the 5% degressive reduction on Basic Payments over €150,000 might yield about €1 million per year. If a total cap on Basic Payments over €500,000 was imposed, then this could initially generate in the order of €5-10 million per year.

- **First allocation of Payment Entitlements** - Payment entitlements shall be allocated to farmers who meet the Active Farmer criteria and apply for an allocation of entitlements by a specific date in 2015 (Likely to be 15 May 2015).

- Member States / Regions **may** also allocate payment entitlements to farmers;
    - Who did not receive direct payments in 2013 and produced fruits, vegetables, ware potatoes, seed potatoes, ornamental plants and/or cultivated vineyards,
    - Were allocated entitlements from the National Reserve in 2014,
    - Never held entitlements established under the previous Direct Payment Regulations (EC 73/2009 and EC 1782/2003) provided they produced reared or grew agricultural products in 2013.

- This will allow Scotland to award entitlements to new entrants and previously unsupported sectors such as deer farming which were excluded from the current SFP.

- The number of entitlements allocated in 2015 shall be equal to the number of eligible hectares the farmer declares in his application.

- Scotland currently has around 4.559m hectares of agricultural land claimed under the current SFP. It is estimated that there is around an additional 1m+ hectares of land that could be eligible for payments. If all this land were claimed it would severely reduce payment rates across Scotland.

- Member States / Regions **may** apply specified limitations on the number of entitlements to be allocated and there are various methods for doing this through reduction coefficients, etc. Scottish Government does not propose to use reduction coefficients but no decisions will be taken until after the consultation is complete.

- **Value of payment entitlements and convergence** – The Regulation stipulates that the unit value of payment entitlements shall be calculated by dividing a fixed percentage of the national / regional ceiling for each year by number of payment entitlements in 2015, excluding those allocated from the National Reserve in 2015.

- The Regulation also allows for a Member States /Regions on the basis of objective criteria, to introduce a windfall tax of the increase, or part of the increase, in the value of payment entitlements, on farmers who have benefited in cases of sale or grant or expiry of all or part of a lease of agricultural areas after 15 May 2014 and before the date fixed for this Regulation (15 May 2015). The proceeds of the windfall tax would revert to the National Reserve. Scottish Government propose to use the windfall tax in cases where the termination or ending of a lease leads to a windfall for the farmer/land owner concerned.

- Member States can also place a siphon on sales of entitlements transferred without land whereby a part of the payment entitlements transferred shall revert to the National Reserve. Scottish Government proposes to use the siphon on entitlements transferred without land.

- It is not possible to estimate how much could be raised by the windfall tax or the siphon on entitlements at this time.

- As of claim year 2019 at the latest, all payment entitlements in a Member State or, in case of application of Article 20, in a region, shall have a uniform unit value.

- By way of derogation Member States / Regions **may** decide that entitlements whose initial unit value is lower than 90 % of the national or regional unit value in 2019 shall have, for claim year 2019 at the latest, their unit value increased at least by one third of the difference between their initial unit value and 90 % of the national or regional unit value in 2019, the so called “Irish Tunnel”.

- Member States **may** decide to set that percentage at a level higher than 90% but not above 100%.

- Member States shall provide that, at the latest for claim year 2019, no payment entitlement shall have a unit value lower than 60% of the national or regional unit value in 2019, unless this results in a maximum decrease above a 30% threshold. In such a case, the minimum unit value shall be set at a level necessary to respect that threshold.

- The national or regional unit value in 2019 shall be calculated by dividing a fixed percentage of the national ceiling or regional ceiling, for calendar year 2019, by the number of payment entitlements in 2015, excluding those allocated from the national or regional reserve in 2015.

- In order to finance these increases in the value of payment entitlements, the payment entitlements having an initial unit value higher than the national or regional unit value in 2019 shall have the difference between their initial unit value and the national or regional unit value in 2019 decreased on the basis of objective and non-discriminative criteria to be determined by Member States. Such criteria **may** include the fixing of a maximum decrease of the initial unit value of 30%.

- When differentiating the value of entitlements, the move from the initial unit value of payment entitlements and their final unit value in 2019 shall be made in equal steps starting from 2015.

- In 2015, Member States shall inform the farmers of the value of their payment entitlements for each year of the period covered by the direct payment Regulation.

- It is not possible to accurately calculate entitlement values at this time until decisions, on payment regions and their budget allocations, and on what optional schemes will be used, i.e. VCS, Redistributive payment etc., are made

- **National Reserve** - Member States shall establish a national reserve and in the first year of the basic payment scheme, make a linear percentage reduction of the Basic Payment Scheme ceiling at national level in order to constitute the national reserve. The linear reduction shall not be higher than 3% except, if required, to cover the allocation needs.

- Member States that decide to regionalise the CAP **may** establish regional reserves, with the linear reduction being made from the regional ceiling.

- Member States shall allocate payment entitlements from the national reserve or the regional reserves in accordance with objective criteria and in such a way as to ensure equal treatment between farmers and to avoid market and competition distortions.

- Payment entitlements shall only be allocated to farmers who meet the Active Farmer requirements.

- As a matter of priority, Member States / Regions shall use the national or regional reserves to allocate entitlements to young farmers and farmers who commence their agricultural activity (new entrants).

- Member States / Regions **may** use the national or regional reserves to;
    - Allocate entitlements to farmers to prevent land from being abandoned, including areas subject to restructuring and/or development programmes relating to a form of public intervention, and/or to compensate farmers for specific disadvantages,
    - Allocate entitlements to farmers who were prevented from being allocated entitlements as a result of force majeure or exceptional circumstances,
    - Linearly increase on a permanent basis the value of all payment entitlements under the basic payment scheme at national or regional level if the national or regional reserve exceeds 0.5% of the annual national or regional ceiling for the basic payment scheme, provided sufficient amounts remain available for allocations under the reserves.

- When making allocations to young farmers , new entrants, to prevent land abandonment, etc. Member States / Regions **may** either allocate new entitlements or increase the unit value of all existing entitlements of a farmer, up to the value of the national or regional average.

- The Basic Payment Scheme Ceiling is dependent on the deductions from the National Ceiling. The mandatory deductions from the national ceiling are 32% (30% Greening and 2% Young Farmer Payment) the optional deductions could be up to around 48% (8% VCS, 15% Redistributive Payment, 5% ANC, 10% Small Farmer Scheme)

- This means the Basic Payment Scheme ceiling could range from as little as 20% to a maximum of 68% of the National ceiling. The amount of funding for the National Reserve, a 3% reduction from the BASIC Payment ceiling, is entirely dependent on the decisions on which optional schemes should be implemented along with the mandatory schemes.

- For the first year of the new CAP it will be possible to make a linear reduction of the value of payment entitlements under the basic payment scheme to cover the allocation needs of the National Reserve.

- In the event that the national or regional reserve is not sufficient to cover young farmer or new entrant allocations in future years, it will be possible to make a linear reduction of the value of payment entitlements under the basic payment scheme.

- It is estimated that there are around 700 existing new entrants that are likely to claim entitlements through the National Reserve or to have the value of entitlements increased. Although difficult to predict it is estimated that there could be up to 200 new entrants per year.

- **Payment for agricultural practices beneficial for the climate and the environment (Greening)** - - 30% of the Pillar 1 ceiling must be set aside for greening measures, this equates to approximately €159 m –in 2019 scheme year.

- This will be paid to farmers in the form of a greening payment provided they meet the requirements of the greening measures.

- The greening measures include Crop Diversification, Maintaining Permanent Grassland and the creation of Ecological Focus Areas (EFA).

- Member States / Regions **may** consider using equivalent practices that yield an equivalent or higher level of benefit than the standard greening measures.

- Member States / Regions **may** also decide from a list of options what should be included in the EFA.

- Decisions on how to implement the greening measures in Scotland will be taken after the consultation process has been completed.

- The value of greening payments will depend on the decisions on how Scotland is divided into payment regions and how the greening measures are to be implemented.

- **Payment for Young Farmers** – Member States / Regions shall grant an annual payment to young farmers who are entitled to a payment under the basic payment scheme.

- Young Farmers means natural persons setting up for the first time an agricultural holding as head of the holding or who have set up such a holding in the 5 years preceding first submission of an application to the basic payment scheme, and are no more than 40 years of age in the year of submission of that application.

- Member States / Regions **may** define further objective and non-discriminatory eligibility criteria for young farmers applying for the payment as regards appropriate skills and/or training requirements.

- The regulation allows up to 2% of the national ceiling to be allocated for the Young Farmer payment, using the maximum for this would be the equivalent of around €11m per year

- There are 4 options for calculating the payment which are included in the consultation document.

- **The following optional measures may be considered.**
- **Redistributive payment** - Member States **may** decide to grant an annual payment to farmers who are entitled to a payment under the basic payment scheme.

- The payment shall be granted annually upon activation of payment entitlements by the farmer and shall be calculated by multiplying a figure to be set by the Member State, which shall not be higher than 65 % of the national or regional average payment per hectare, by the number of payment entitlements that the farmer has activated.

- The number of such payment entitlements or hectares shall not be higher than 30 hectares or the average size of agricultural holdings in the Member State concerned (UK 54ha).

- The Regulation allows for up to 30% of the national ceiling for direct payments to be used for the redistributive payment.

- It is estimated that using the maximum payment across Scotland would require around €123m per year, or around 23% of Scotland's ceiling .

- If a decision is made to use the redistributive payment, payment rates for individual farmers depend on the decision to be taken in relation to how the payment is to be implemented i.e. across the whole of Scotland or only in a particular payment region. It will also depend on the decision in relation to payment regions.

- **Payment for Areas with Natural Constraints (ANC)** - Member States **may** grant a payment to farmers entitled to a payment under the basic payment scheme and whose holdings are fully or partly situated in areas with natural constraints designated by Member States in accordance with Article 33(1) of the new Rural Development Regulation (EU) No […] [RDR].

- Member States **may** decide to grant the payment to all areas falling within the scope of areas designated with natural constraints and/or on the basis of objective and non-discriminatory criteria, to restrict the payment to some of the areas designated by the Member State.

- The Regulation allows for up to 5% of the National ceiling to be used for the ANC payment. Scottish Government do not propose to use the ANC payment as it would require wholesale change to the Less Favoured Area (LFA) support structure.

- **Voluntary Coupled Support (VCS)** - Member States **may** use up to 8% of their annual national ceiling to grant VCS to farmers in the following sectors and productions: cereals, oilseeds, protein crops, grain legumes, flax, hemp, rice, nuts, starch potato, milk and milk products, seeds, sheepmeat and goatmeat, beef and veal, olive oil, silk worms, dried fodder, hops, sugar beet, cane and chicory, fruit and vegetables and short rotation coppice.

- VCS may only be granted to those sectors or to those regions of a Member State where specific types of farming or specific agricultural sectors undergo certain difficulties and are particularly important for economic, and/or social and/or environmental reasons.

- Coupled support may only be granted to the extent necessary to create an incentive to maintain current levels of production in the regions or sectors concerned.

- Scotland currently uses 4.5% of its direct payment ceiling for coupled support through the Scottish Beef Scheme which delivers an annual budget of €29.8m.

- Using 8% of Scotland's ceiling for 2014 – 2019 would deliver an annual budget of around €42m.

- Decisions on how VCS would be implemented in Scotland, i.e. should it be for beef sector only as per the current scheme or should there be a scheme for sheep,etc., will be taken after the consultation process is completed.

- **Small Farmer Scheme** - Member States **may** establish a scheme for small farmers in accordance with the conditions laid down in Regulation and farmers holding payment entitlements and fulfilling the minimum requirements for receiving direct payments may opt to join the scheme.

- Payments under the small farmers scheme replace all other direct payments.

- The annual payment for each farmer participating in the small farmers scheme shall not be lower than €500 and not higher than €1 250 and is calculated by one of the following methods:
  - an amount not exceeding 125% of the national average payment per beneficiary;,
  - an amount corresponding to the national average payment per hectare multiplied by a figure corresponding to the number of hectares with a maximum of three five.

- There are different methods for Member States to fund the Small Farmers Scheme up to a maximum of 10% of the national ceiling.

- The main benefit for farmers participating in the scheme would be that they are exempt from the greening practices and provided they only claim Pillar 1 payments, they would also be exempt from cross-compliance penalties. This would greatly reduce the administrative burden on small farmers

- However, the reality is that many of Scotland's small farmers are livestock farmers in the Less Favoured Area and likely to be claiming LFA support through Pillar 2. They will also be mainly grassland farms and so exempt from the greening measures anyway. Scottish Government does not therefore propose to introduce a Small Farmer Scheme as it is unlikely to deliver any additional simplification for small farmers.

- **Sectors and groups affected**
- The Sectors and Groups primarily affected will be the agriculture sector, farmers, crofters, land managers etc.

- **Benefits**
- The main benefits to industry is that there is a level playing field in terms of consistency of regulation on the sector across the rest of the UK and Europe. Businesses will know what level of support they will receive each year up to 2019. This will create a degree of certainty for businesses giving them confidence for planning ahead.

- The benefits for Government of implementing the CAP reforms ensures that Scotland meets its regulatory requirements and significantly lessens the risk of penalties being applied from Europe for non-compliance.

- **Costs**
- The European Commission has estimated that implementing the CAP reforms will incur an increase in administration costs of around 20% for Governments/Administrations.

- For businesses there will be an additional cost in terms of greater complexity/administrative costs for measures such as greening, voluntary coupled support , etc.

Scottish Firms Impact Test

- Details of the results of face-to-face interviews with individual businesses will be included in the final BRIA.

- **Competition Assessment**

  The new CAP addresses anomalies in the present system that prevents some farm businesses, including new entrants to farming, deer farmers, etc., from accessing the current CAP.

  Using the Office of Fair Trading's Competition Filter questions we have concluded that the proposals will neither directly or indirectly limit the number or range of suppliers, limit the ability of suppliers to compete or reduce suppliers' incentives to compete vigorously.

- **Test run of business forms**
  This will happen as part of the RPID Futures programme which is a customer focussed IT programme to support and deliver the systems required to implement the CAP Reforms for 2015.

Legal Aid Impact Test

- A person appealing against a decision on eligibility for CAP payments, etc., can claim Legal Aid to assist them pursue an appeal. This will continue in the new CAP.

- However, the rules for receiving payments in the new CAP are different to the current rules so there will need to be changes to the appeals process to address changes in the CAP legislation.

- The current appeals process is designed to try and resolve issues without recourse to the legal system. The Land Court also takes a flexible approach, not always requiring an appellant to be represented by Legal Counsel.

- Scottish Legal Aid Board (SLAB) does not expect there to be additional impact on the Legal Aid Fund.

Enforcement, sanctions and monitoring

- The CAP will be enforced through a robust regulatory framework set out in the Regulation of the European Parliament and of the Council on the financing, management and monitoring of the common agricultural policy (The Horizontal Regulation) and in implementing rules.

- The Horizontal Regulation has still to be formally adopted by the Council and is expected to be adopted at the Agriculture and Fisheries Council on 16 December 2013. The European Parliament formally adopted the Regulation on 20 November 2013, text available at; http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//NONSGML+TA+20131120+SIT-04+DOC+WORD+V0//EN&language=EN

- The implementing rules are still being discussed in Europe and are yet to be published.

- Scottish Government's Rural Payments and Inspection Division (RPID) will monitor and enforce the CAP in conjunction with delivery partners such as SEPA and AHVLA through administrative checks and on the spot checks including the use of aerial photography, GPS equipment, livestock and record checks.

- The sanctions for non-compliance includes a range of penalties as laid down in the European legislation. The penalties applied can range from warning letters in the event of very minor breaches to 100% reductions and exclusion from schemes in the event of extremely serious or repeated breaches or over declarations.

Implementation and delivery plan

- The reformed CAP will be implemented in a manner consistent with the robust implementation process in place for the current CAP, i.e. submission of application forms, inspections and where necessary penalties applied for non-compliance.

- There is a regulatory requirement for the reformed CAP to be implemented from 1 Jan 2015.

- **Post-implementation review**
  A post implementation review will be carried out, it is possible that as with the previous CAP Europe will seek to have a mid-term review of the CAP.

Summary and recommendation

Option 1 – It is not possible to adopt a do nothing option.

There is a regulatory requirement for Member States to implement European Regulations and a failure to do so would lead to very substantial penalties. It is also a requirement of Section 57 of the Scotland Act 1998, that Scottish Government do not act in a way that is incompatible with EU Law.

Option 2 – Implementing the CAP is a regulatory Requirement for Scottish Government and is the recommended option.

There are many elements within the direct payments regulation some mandatory and some optional. The various measures are interlinked with varying outcomes depending on the combination of measures to be adopted.

Decisions on what measures are to be adopted to deliver a final direct payment package for Scotland will be taken after the consultation has taken place. A final more detailed BRIA will be prepared once those decisions have been taken.

- **Summary costs and benefits table**
  This will be completed when the final BRIA is prepared.

Declaration and publication
I have read the impact assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options. I am satisfied that business impact has been assessed with the support of businesses in Scotland.

Signed:

Richard Lochhead

Date: 12/12/2013

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