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THE SELECT COMMITTEE ON THE EUROPEAN UNION
(SUB-COMMITTEE D)

INQUIRY INTO THE REVISION OF THE LESS FAVOURED AREAS SCHEME

WEDNESDAY 21 JANUARY 2009

MS JOSEFINE LORIZ-HOFFMAN, MR ALEXANDER PAGE and MS ANTONELLA ZONA

Evidence heard in Public

Questions 1- 46

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WEDNESDAY 21 JANUARY 2009

Present

Arran, E
Brooke of Alverthorpe, L
Caithness, E
Cameron of Dillington, L
Dundee, E
Livsey of Talgarth, L
Palmer, L
Sewel, L (Chairman)
Sharp of Guildford, B
Ullswater, V

Witnesses: **Ms Josefine Loriz-Hoffman**, Head of Unit, **Mr Alexander Page**, Administrator and **Ms Antonella Zona**, Administrator, DG Agriculture and Rural Development, European Commission, examined.

Q1 Chairman: First of all can I thank you very much for coming over and seeing us. It is always a delight for us to go to Brussels to talk to people but it is a particular delight to welcome people from the other side here, so thank you very much for coming across and helping us with our inquiry into the review of the LFA scheme. There is a formal part I have to go through now telling you that this is a formal evidence collecting session so a note will be taken and a transcript produced. You will receive a copy of that as soon as possible and you will be able to go over it and correct any slips or mistakes that have crept in. The other thing is that this session is being web cast; there is a small theoretical possibility that somebody somewhere might be hearing what we are saying. We have never, ever had any evidence that that is the case but I have to tell you. Josefine, would you like to introduce your side and if you would like to make an introductory comment that would be very helpful to us, but if you would prefer to go straight to questions and answers that would be fine by us as well.

Ms Loriz-Hoffman: Thank you very much, Chairman. Thank you for having invited us and allowing us to elaborate on the subject and to answer your questions. I would say that from the questions which we have received we understand that you are very well aware of this subject so I will not have to do a long introduction. I will simply present where I am in the Commission and what I am doing. I am the Head of Unit of the Rural Development Unit dealing with the consistency of rural development. What we do is coordinate between the different units working with the Member States programmes and at the same time we develop the content and the legal framework of the rural development policy. On this specific subject I would like to say that the Less Favoured Areas scheme has for a long time been part of the Common Agriculture Policy and it is not a compulsory measure, so Member States can choose whether they want to take it up in their programmes but all Member States implement it at the moment. I would also like to underline that this current review is not a reform. The legal framework was redefined in 2005 when the ministers decided on the legal framework for the new programming period 2007-2013, so let us say that the framework is in place. The Commission's mandate is to clarify and set down the rules for delimiting the so-called intermediate less favoured areas and also the targeting of payments in line with the objectives of this measure. This also means that the mountain areas and the areas protected by specific handicaps are out of the mandate and these parts of the Less Favoured Areas scheme will not be looked at. Until we have new rules in place – to be decided by the Council – at the moment we are still with the old system.

Q2 Chairman: I am going to start off and ask you the nice general opening question. When you looked at this issue what did you think and what has emerged in terms of the strengths and weaknesses of the existing scheme as it has worked so far? Perhaps you could then give us an idea of the Commission's objectives in reviewing the scheme.

Ms Loriz-Hoffman: As I have said before, this scheme has been in place since 1975 and the LFA scheme provides a mechanism to support agricultural farming systems and with that the maintenance of landscapes in mountain areas first of all then in other less favoured areas which call the intermediate less favoured areas and then in areas under specific handicaps. The evaluation which was carried out in 2005-2006 states that the scheme has contributed in maintaining farming systems in fragile and marginal areas. It provides a contribution to this objective and we think in general this scheme supports the objectives as laid out under the Rural Development scheme and in particular under objective two which is protection of the environment and the maintenance of land management. It is an easy measure because once you have put the administrative arrangements in place then you can provide the support without any further specific rules which means that you have to delimit the zones, you have to determine the payments but then you have a scheme which is easily applicable. If we look at the weaknesses, I think the weaknesses concern in particular the system which is in place for the intermediate less favoured areas and you know that the Court of Auditors has criticised the system of delimitation of these areas which have been put in place by the Member States. Certainly for this part of the LFA scheme there is a lack of coherency, comparability and of transparency and this is due to the fact that in the Member States we have in place a diversity of criteria which they use to classify these areas which have been put in place by the Member States. This might lead to discrimination between beneficiaries and insufficient targeting of the aid. What we have also observed and what has also been said in the evaluation is that in some Member States, due to a low level of payment and sometimes strict rules of eligibility, these payments only contribute to a limited extent to maintaining agriculture. This means we have a problem, sometimes very low payments and then it is questionable whether these payments really are sufficient to maintain farming systems in place which we would like to have in a number of Member States. So these are the weaknesses we see and, following on

from that, the objectives of our exercise. First of all we think we have to adapt the intermediate FLA delimitation and payment system to the approach which has been decided by the ministers in 2005 and this concerns in particular the elements which are the objectives of the measure, which have been refined slightly, then the focus on the natural handicaps as being the reason for support and then the third element I think is the specific way to calculate the compensation based on the principle of costs foregone and income foregone. So these are the areas we have to adapt it to. Then of course we want to do something on the situation of the indicators. We would like to have these indicators more transparent and more based on scientific evidence. We also think that there is a need to have better coherence between the criteria used by Member States, although we are aware that we would like to give some weight to national and regional specificities. So Member States will also need a certain possibility to adapt to their specific circumstances. The objective is, after all, to minimise unequal treatment between beneficiaries. Then another point apart from the adaptation process to the legal framework and the improvement of the criteria I think is the targeting of the aid. There I think we have to ensure that the areas which are delimited are actually suffering from a disadvantage. We will come to that later on if we talk about these further steps in the delimitation process. Then also a target focussing more or going into the direction of supporting more extensive farming systems. This is also laid down in the regulation by saying that farming systems or extensive farming systems which are important for maintaining land management should be favoured. Then also to focus on the areas where there is the real risk of abandonment. Of course the systems we have in place at the moment do not all comply with our international commitments. We know that some of them are probably not WTO compatible. These are things we would like to improve within this process.

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Q3 Chairman: One is almost tempted to say the best of luck!

Ms Loriz-Hoffman: We know that the Member States are with us in this process.

Q4 Chairman: That was a brilliant and comprehensive review of where we are and where you want to go, so thank you very much. Do I get from you that you think the real benefit of LFAs looking back has been the delivery of environmental benefit?

Ms Loriz-Hoffman: Yes I think so. The real objective of the measure is to maintain farming because we think that farming is important in specific types of areas which are fragile and difficult and where, for example, the ending of an agricultural activity would be a threat for environmental objectives like biodiversity, water, water management and other things.

Q5 Chairman: So it is environmental maintenance or enhancement through agricultural activity. That does not necessarily mean the maintenance of the same number of farmers though, does it?

Ms Loriz-Hoffman: No.

Q6 Chairman: Let us go onto our next question from the Earl of Caithness.

Ms Loriz-Hoffman: May I add something about this? If you look into statistics you can see that the farms in less favoured areas, in the intermediate less favoured areas, as regards their size they are bigger than the average farms in non-LFA regions and the tendency we see is that they are gaining more surface in the development of time than the normal farms. So there is, let us say, a certain extensification going on by the merging of farms.

Q7 Earl of Caithness: Can I firstly follow up the Chairman's point on the purpose of your review. How much do you expect to reduce the LFA budget as a result of your work?

Ms Loriz-Hoffman: At the moment we spend about 12 per cent of the overall development budget on support for less favoured areas, the intermediate areas. There must not necessarily result a change in budget from the exercise we do which means that you have in principle two

components. You could have a change in the area under the scheme and then you could also have a change of the level of premium. So you have these two components in play and I think if there is a redefinition of areas we do not know what the result will really be although I should say that Member States, in the discussions we have had with them, have signalled – with some very few exceptions – that in principle there is no interest in extending less favoured areas, the intermediate less favoured areas. As regards the premium level we have certain upper and lower limits in the regulations and so far we have not had any specific critics or remarks from Member States on these levels which means that most of them can probably operate the schemes or the systems they have in place within these thresholds. At the moment I do not think it is possible for us to say what the result will be for the budget but anyhow the LFA measure is embedded in the overall rural development envelope and this envelope will not be changed by this revision exercise and by a different delimitation. Member States may take more or less of the envelope in order to care for the farmers in the future.

Q8 Chairman: So it is talking about the allocation within the rural development envelope rather than affecting the size of the envelope itself.

Ms Loriz-Hoffman: Yes.

Q9 Earl of Caithness: Coming onto the question I wanted to ask you, you propose EU-wide biophysical criteria and thresholds in order to classify less favoured areas; could you elaborate on how you arrived at those criteria and why it is deemed necessary to restrict the less favoured designation to areas facing natural handicaps only?

Ms Loriz-Hoffman: First of all let me say that for the moment we do not propose these criteria. We discussed them with Member States and we analysed them in the context of these options which we have also developed for the consultation and consultation process, but

what I should also say is that these criteria very much correspond to what the Council has set out in the general framework for this measure. First of all we tasked the joint research centre of the Commission to define a common framework for soil and climate criteria which would show and allow us to delimit every country's areas which are suffering from natural handicaps. The idea of the soil and climate criteria is directly spelled out in the regulations; the Council regulations define natural handicap as lower soil productivity and climate difficulties. A number of experts from different Member States have been called in and they have worked on these areas on the basis of an FAO approach on agricultural problem lands. The objective was to find a simple matter, something easy which is applicable to all Member States but also at the same time robust and transparent and which allows from a restricted number of criteria to judge whether areas are under handicaps or not. The outcome of this is that they have developed two climatic and four soil criteria and then there is another criterion which is a mixture, a so-called soil-water balance criterion when they have two components in one. Then they have also identified slope as a possible handicap. Each of these criteria has also been attributed a threshold value which indicates a severe limitation for agriculture in Europe, so independent from where this is exercised this is always considered to be a point where agriculture starts to have difficulties. We think that areas need a certain presentation in the overall utilised agricultural area; a certain percentage of the overall utilised area should suffer from this handicap. This is a condition that the whole area falls under consideration. The idea is also that as soon as one of these indicators – the threshold – is achieved in a region then from that moment on the handicap is present. Would you like me to give you the details of the indicators?

Q10 Chairman: No, I do not think we need to go into that.

Ms Loriz-Hoffman: We have two climate indicators: low temperature and heat stress (that is too much heat over a certain period). We have four soil criteria where one is, say, wet

conditions characterised under the criteria of rain. Then we have stoniness. All these criteria in principle fix the conditions under which the plants are suffering in a certain period from difficulties in following a normal growth regime. It can be because of the shortage of vegetation days or a shortage of water or, let us say, there is too much stony material which is an obstacle for optimum development. Any of these indicators and the thresholds with it describe a situation where the plants cannot develop as they should normally do and where agriculture is consequently having difficulties in following normal activities. On the question why we focus on natural handicaps, a number of studies indicate quite clearly that natural handicaps quite accurately describe those areas where agricultural production systems are handicapped and where there is risk of land abandonment. A clear direction which focuses on these natural handicap criteria is also set out in the Council regulations which make reference to that. The natural handicap criteria we are looking at also have a specific feature in that they are pertinent, they do not change over time (the circumstances may change and we will come to that later on); this condition in principle in a specific region does not change except if we have a further development of climate change which may change things like the water situation but in general these conditions do not change. We know that in the process before when we were discussing in 2005 the new legal framework we also discussed the so-called economic indicators or socio-economic indicators which were yield and other criteria but the difficulty is that these criteria deviate from the basis of the problem. The basis of the problem is that you have a natural condition for agriculture which makes production difficult and the more you try to measure this difficulty – not at the basis, at the handicap itself; let us say the result of the handicap which is the yield or which may be the income or whatever – the more you get in other factors because it makes a difference whether a good or a bad farmer is operating in a handicapped area. So if you look into the yield even in a less favoured area you can have a difference between a surface managed by a good or a bad farmer so all these

individual management and also input factors come into that and they no longer provide a clear picture. The other point is that if we operated with the socio-economic indicators we would have a difficulty in having the community reference. For these natural handicap indicators we have a threshold and scientists who say that under these circumstances it is difficult everywhere in the world. If you have, let us say, a certain yield which you think is a normal yield in Europe, nowadays with a Europe of 27 that can be quite a low yield. We think it would be difficult to have a common reference in such a system. Therefore we think that these biophysical indicators reflect a pertinent difficulty, a natural handicap situation; in principle they do not change over time and they allow us also to operate in a certain common way providing a general framework for a common new system.

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Q11 Earl of Caithness: That is very helpful. Your original criteria that you proposed seemed to many of us to be favoured to a central European climate rather than a maritime climate. Could you please confirm that when you are looking at this that you have accepted that field capacity days for rainfall and temperature can now be included and that soils that are already drained can be included? For many parts of northern Scotland and the whole of the UK it is a combination of these factors; it is not just one factor by itself that makes it a less favoured area, it is a complete combination. If you could confirm those two points that would be helpful and relieve many people's concerns.

Ms Loriz-Hoffman: You refer to a point which has been discussed with Member States. The northern Member States had difficulties with specific conditions of, let us say, a kind of maritime climate but under cold conditions. The experts have looked into this question of the field capacity days and it has been taken on board which means that we have refined the drainage criteria to take in this field capacity indicator so Member States will have the possibility to delimit according to this criteria. It has been taken on board, yes. As regards the other part of your question, the question whether already drained soil can be considered

also as being a natural handicap, in principle there are certain efforts that have been done for soils which are under drainage in order to bring them into a situation where they can be productive. That is my understanding. If the drainage is effective then there should not be a difficulty from my point of view. If the drainage is in, let us say, an imperfect situation or is damaged at all then that could be a difficulty. We have defined under drainage quite specific conditions, what we considered to be drainage which means this is referring to a specific drainage class according to a specific classification system. If this criterion is still met then it is a less favoured area but beyond that we think that the handicap is no longer present.

Q12 Chairman: There is a difficulty here because it is a penalty on investment, is it not? If there has been prudence and a willingness to invest to improve drainage the farmer is penalised, whereas he has been less entrepreneurial he gets a benefit. There is really a degree of perversity there.

Ms Loriz-Hoffman: Yes.

Q13 Earl of Arran: You have partly answered this question already, but still on this very tricky subject of biophysical criteria, in your opinion what degree of flexibility would Member States have to fine-tune the designations that flow from the biophysical criteria that you have in mind? Would you expect this to be done through eligibility conditions or might this be done through a second tier of country-specific biophysical indicators? Or is it a question of the best of luck? What is your view on this?

Ms Loriz-Hoffman: As I have said, we are starting from a set of biophysical indicators with a specific threshold. The experts say in their judgment that these criteria and the associated critical limits can be used anywhere to classify the land, but they have also recognised that certain natural handicaps can be overcome by technical progress and management intervention. A typical example of that is irrigation; I would say not typical irrigation but

artificial progressive irrigation. In these cases the original handicaps are still present; they are there but as a result there are no longer signs of a less favoured situation which means that the average outcome of the production is more or less comparable to what you have under normal conditions in a country. We think that under these circumstances these areas should not be classified. However, the specialists have looked into the types of criteria and they have identified that this is the case for only three of the criteria and these are the soil criteria which means that the length of the vegetation period or the temperature situation are things which will not change. Where you can do something is in the question of lack of water; irrigation can influence the soil/water balance and the other possibility is that you can do something about too wet conditions which means you can drain. The other criteria are, say, stable and always lead to a handicap except these three soil criteria: soil texture and stoniness, rooting depth and chemical properties. There Member States would have to look into whether the handicap is still visible in these areas in the production. To give you an example, in specific Member States there are difficulties or there is a less favoured situation for agriculture under one of these criteria (this is stoniness and rooting depth) but they are producing champagne quite successfully. So there is a question as to whether this is a less favoured area. There are specific conditions where the handicap does not really lead to a difficulty in production. We think Member States have to look into these regions and into the productivity situation. They should look to see whether the handicap is still manifest, whether it still shows out in production results or not and, if this is no longer the case, they should not consider these regions to be less favoured. I think that in order to ensure that this process is managed a little bit more or is executed by Member States we would probably have to set a framework on how to operate this verification process for three out of the eight indicators.

Q14 Earl of Arran: At the moment it does not look as though there is going to be a second tier of conditions?

Ms Loriz-Hoffman: I would say there is no systematic second delimitation step but there is a sort of fine-tuning exercise to be done by the Member States limited to certain of the criteria and I think it would probably be desirable to have a framework for this fine-tuning process put down in legislation. Member States would have or should have the possibility to use those indicators which, from their point of view, show what are best suited for this verification process. We are in discussion with Member States about this.

Q15 Lord Livsey of Talgarth: In your discussions with Member States and stakeholders, what additional or alternative criteria for classifying less favoured areas have been advocated most frequently? Clearly the status quo is something that may be jealously guarded and, as we understand it, some local authority areas have LFA type land and there is other land which perhaps could not be classified as such but nonetheless benefits. The whole question of the rejection of socio-economic factors which is apparent is probably something that may be on the agenda.

Ms Loriz-Hoffman: We have had a lot of bilateral meetings with Member States in order to allow them to explain their approach. You are right, the result of the consultation process is in favour of maintaining the existing system, but I think this is not really an option which we think we can seriously follow up. The point is that in all the discussions we have had we have not had any indication of other criteria we could use to describe these natural handicaps than what we have at the moment from the GSL, so let us say that we have had nothing new. A lot of Member States I should say are at the moment operating on the basis on index systems and they have, of course, suggested that these index systems are very valid systems as they are based on the same biophysical criteria which are under discussion now. This is partially true but the difficulty is that all these systems are different which means that these systems include a number of indicators, a lot of them stealing from the biophysical indicators we are looking at, but they give different weights to these indicators. To give you an example, you a scale of

points which describe the value of the soil and we have a Member State which pays below 28 points indicating a low quality of soil and we have another Member States which is paying below 53 points but we cannot say now whether the 53 points corresponds to the 28 or not. There is no comparability between these systems and also we cannot imagine that we would impose on 27 Member States a complicated index system only to allow maintenance of these existing systems. That seems to be difficult. Then on the socio-economic indicators I have already said that we consider them to be not sufficiently close to the handicap except for the difficulties. Then you have other indicators, the population density and things like that. This steals a little bit from the former philosophy of the method where we wanted to avoid people leaving the countryside but we think that LFA, apart from farmers, will not retain other people. Under the rural development policy we have better measures to address this migration and leaving the countryside problem and other indications we have had that we should take into account are remoteness, distance from markets or small structures of farms. This is something you can change; this can change over time and this has also been criticised by the Court of Auditors that some of the Member States had not looked for a long time into these kinds of indicators and whether it had changed over time. We think that these indicators do not correspond to the underlying idea of what a natural handicap would be.

Q16 Earl of Dundee: We know that the quality of biophysical data in some Member States is far better than it is in others. How do you think that data availability can improve?

Ms Loriz-Hoffman: You are right; at the moment Member States are not obliged to collect these indicators. Some do it for external reasons, for research or whatever; some have quite good databases on this so they can operate with this data. I think in any case during this process a lot of Member States became aware that it is useful to have this data for analytical reasons but also to look into the question of where there are difficulties and what is the specific qualification of different areas. However, if such a system should become a system

within a policy we would have to give Member States some time to build up the system and to get data so I could imagine that there would be a transitional period during which Member States which do not possess this information could get it.

Q17 Chairman: How long?

Ms Loriz-Hoffman: That depends also on what we see from Member States as an answer to the communication process which we will put in place in April. Maybe we can come back to you on that.

Q18 Earl of Dundee: If necessary data is not yet sufficiently available, how can we hope, with any accuracy, to assess the impact of those criteria?

Ms Loriz-Hoffman: First of all on a community level we have done impact assessments but that is on quite a rough level because we are operating with so-called pan-European data. That gives us pictures but they are unsatisfactory because we do not have sufficient detail of data. This detail of data is only available in Member States because it really concerns the situation in very small regional entities. We need the help of Member States to provide a more realistic picture because everything we do in terms of an impact assessment is incomplete at the moment and we are quite aware of that. This is one of the reasons why in the communication which we would like to put to the Council in April where we ask Member States there to use the data they have and to do a more detailed impact analysis of the options we have put forward in the consultation. We think an important number of Member States have much more detailed data than we have available and can provide us with quite a clear picture of what these biophysical criteria would give as a new LFA.

Q19 Earl of Dundee: So you are cautiously optimistic that there will not be an anomaly, that by the time an impact assessment is made there will be much more available data.

Ms Loriz-Hoffman: I would say not for all Member States - we should be clear on that – but for a big number of them.

Q20 Chairman: Do you think there is a danger that some Member States may find that the data they possess does not produce the outcome they wish and therefore may misplace the data?

Ms Loriz-Hoffman: When we were starting with the exercise in a lot of Member States we had the idea that data was not available but we have been working with Member States for more than a year and in this time we have got a lot of mapping and a lot of detailed analysis and then also Member States detecting that there were surveys underway. Meanwhile some of these surveys have been finalised so I think in a lot of cases the data is available but not at a central level in a consistent way or put into a framework. Bigger countries have regional collection systems but there was never a requirement to put all this data together in a consistent system. I think this is also part of the work that has to be done. There is data but sometimes it is dispersed over an area and I think it must be put together in a systematic way and then integrated into a coherent approach.

Chairman: I think we should move onto eligibility questions now.

Q21 Lord Cameron of Dillington: You have indicated that you would amend the rules for eligibility and I was wondering what is your preferred approach in this area is likely to be and what degree of harmonisation you would like to see across the EU.

Ms Loriz-Hoffman: I have already mentioned that a number of eligibility criteria which we have in place at the moment are not WTO compatible because they simply exclude certain production sectors or certain precisely defined agricultural activities from support. This is something which is not acceptable. The other point is that at the moment we have all over Europe about 150 different eligibility criteria in place. We also observe that some of these

criteria are in contradiction to the objectives of the measures. There are Member States who exclude part time farmers and we think that this is not quite understandable; as long as these people contribute to the objective of the measure we do not see a reason why they should not be compensated for the specific costs they have. There are a lot of criteria in place where we think they are simply not justified. On the other hand we think we need eligibility criteria which means ensuring we are targeting beyond the delimitation of areas. The delimitation of areas is the first step but then, let us say, within these areas Member States should have the possibility to better target the support and the aid and there we have to find objective criteria which do not discriminate between farmers and which are also in compliance with WTO and our obligations. What we have discussed with Member States so far is a specific point which comes out of the regulation directly. The regulation says that we should support extensive farming where it is necessary and where it contributes to maintaining the countryside. So there is the question as to whether we should support intensive farming systems. We have discussed that with Member States and I think the overall view is that there are specifically productive intensive farming systems which can be in place also in less favoured areas. Let us say, in a region that is suffering in principle from a lack of water, if you start concentrated systems of irrigation you can have important yields, very productive farming systems there but they do not contribute to what we consider to be the objectives of supported farming in less favoured areas. You have more extensive farming systems which contribute certainly but there are others where we think the question is whether they provide a contribution. We think that there would probably be a need to exclude such farming systems. This is something we have discussed with Member States and we are going to discuss further. This is an example of where eligibility criteria should be used and could be useful. We think that eligibility criteria first of all have to provide the possibility for Member States to better target the support but, on the other hand, I think we would also have to provide a framework for these

eligibility criteria so that we do not end up with the big number and diverse quality of eligibility criteria which we have today.

Q22 Lord Cameron of Dillington: There is a very varied take-up of the less favoured areas payments across Europe, surprisingly low in some places like Spain and Italy. What type of restrictions might Member States face on the eligibility conditions that they can impose in addition to EU-wide conditions?

Ms Loriz-Hoffman: We think that Member States themselves have an interest, given the limited financial framework they have, to bring the aid where it is really necessary in order to serve the objectives. As I said, I think we also have to provide for a certain frame on how they could do this targeting of support because we should not have systems in place which lead to inefficient spending of money and finally a lack of effectiveness. We have Member States where the level of the payment is very low and the evaluation analysis has told us that in some Member States levels are too low and a lot of farmers are excluded so that the aid does not have the effectiveness it should have. This is the situation which we have to avoid. I think we have to provide a framework for the eligibility criteria providing possibilities to target but also ensuring that we have objective criteria in place which do not hamper the effectiveness of the system.

Q23 Lord Cameron of Dillington: Is there not an option for saying that it is up to the Member States? If they do not wish to spend their money on less favoured areas, providing they use the 25 per cent of their rural development budget on Axis II they could spend it in completely different ways? That is the heart of the problem really.

Ms Loriz-Hoffman: They do not have to include less favoured areas. There are a lot of Member States who have designated less favoured areas and who do not pay at the moment. It is not something compulsory. I suppose that a lot of these areas where there is no payment,

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where Member States do not want to pay, at the end of the day they are under these regions where I have mentioned that they may have overcome the handicap. So this might be a situation, let us say you have a typical situation with wetland in coastal areas but where you have efficient drainage and other things in place and where you can have quite a productive milk production. This is not necessarily something a Member State should delimit as a less favoured area.

Q24 Baroness Sharp of Guildford: Could you tell us a little bit more about how you envisage the new payment system for LFA aid and work in practice? Will there be common rules for calculating additional costs and income foregone related to the handicap? Is the new payment formula likely to reduce the wide discrepancies in aid between different Member States? Are there plans to amend the floor and ceiling for the payment levels fixed by the Council?

Ms Loriz-Hoffman: First of all the principle which we have now fixed in the regulation - costs incurred, income foregone - is a recognised formula in the context of the WTO green box. It should avoid over-compensation which has also been a criticism raised by the court. They have said that they have the impression that in certain regions there is over-compensation so this should not happen with the application of this formula. It is a known principle which we apply at the moment also for the agri-environmental payments where Member States also have to calculate the premiums on the basis of this principle and are then looked at by independent experts and so on and forth. We think that the way to do it is known by Member States but we have also explained and set that out in a working document which we have discussed with Member States at the Rural Development Committee in 2007. We explained in principle what Member States should do agri-environmentally. The same principle applies here. We were looking to these explanations and guidelines to see whether for less favoured areas there would be adaptations necessary or something specific to be put

in but in principle we think that the rules should be the same. As I have said we think this is an effective possibility to avoid over-compensation and bring the correct payments in place.

Q25 Baroness Sharp of Guildford: To what extent is it envisaged that there will be a floor and a ceiling here?

Ms Loriz-Hoffman: Before I can answer your question I have to say this. This can however mean that we have difference in payments between Member States because the understanding is that the cost and the situation are different so you can have differences. We have a number of support schemes in rural development where we have upper limits and also for the agri-environmental scheme, but so far on LFA we have one Member State which has an interest in increasing the upper limit; all the others seem to be fine with this. Theoretically this is something which can be reviewed if Member States think that the calculation of costs shows or indicates costs which go much beyond the ceiling.

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Q26 Chairman: In what you have said you have made reference to the fact that you think in some areas the payments are too low, how would you tackle the too low payment problem? Would you do it through a floor or would you do it through eligibility or what?

Ms Loriz-Hoffman: The lower limits we have at the moment are simply limits for administrative reasons because we think that under 24 euros a hectare the administrative costs are higher than what the farmer finally receives. I think we will have to look into that. First of all we cannot fix in regulation minimum payments for Member States. This is not possible. This would also say that we have a certain assumption of what a minimal handicap would be in Europe and this is, from my point of view, quite complicated. I think we will have an upper limit but then we would have to look into the amounts which Member States define and they should have calculations behind that. Normally we discuss the element of these

calculations. We do not go into the details of the calculations but in principle we discuss with them the level and the amount and what the different components of these are.

Q27 Baroness Sharp of Guildford: Do you think at the end of the day this is going to lead to wider or fewer variations in the levels of payment between different Member States?

Ms Loriz-Hoffman: Fewer variations. I think we would have a tighter margin.

Chairman: Let us go on to one our favourite topics which is management and control. Lord Brooke?

Q28 Lord Brooke of Alverthorpe: I think to an extent you have touched on some of my question when you have been talking about data in the Member States. The Court of Auditors' report in 2003 was extensively critical of some of the Member States' management, control and reporting systems. Since then the EU itself has grown considerably with many new states now coming into play which may or may not have good systems of control. Could you say what you intend to do to try to meet the deficiencies highlighted by the Court of Auditors' report?

Ms Loriz-Hoffman: I do not think it is necessary for me to say that we have paid a lot of attention to what the Court has said about the scheme and its deficiencies. The first thing we have done is to ask for an evaluation to be carried out. This has been done by the Environment Agency in 2006 with a number of very valid results which we have taken into account now when looking into the scheme during the review process. We have also had a lot of exchange with the authors of this study of the evaluation and discussed the questions we had. Then when we put the new legal basis in place for the period 2007-2013 first of all one of the accusations in the report was that the system has possibilities of over-compensation. This is the reason why we have put in place the principle of calculation of the compensation according to the cost incurred income foregone principle. Over-compensation should not

happen in such a system. Then we have harmonised the concept of good agricultural practice; good farming practice was the principle up to 2007. Now LFA is put under the same basic scheme as the other area related support systems of the Common Agricultural Policy which is the cross-compliance, so there are the same basic rules now fixed in the regulation and same for all Member States which was not the case before (before, Member States had to define their good farming practice, they now all run under the same scheme). Then we put in place a new control and sanction system for this new period and on regulation where we clearly stipulate the control and sanction requirements Member States have to follow for this measure. Then another element which we have put in place for the new period is the common management and evaluation framework with indicators to monitor the progress and the results of the measures. Also for the LFA system there are specific indicators in place. Then we have started this review work by tasking the joint research centre to develop a system to delimit natural handicaps. We have put in place an impact assessment group in the Commission from different services - environmental colleagues, economic colleagues, regional policy - to go through this measure and to see where the difficulties are. Finally we are still in a quite extensive exchange process with Member States where we had a lot of bilateral meetings and discussions with them. This means that there are a number of elements which work for the same objectives so that we try to overcome these difficulties.

Q29 Lord Palmer: What measures, if any, might you consider introducing to improve your ability to monitor Member States' implementation of the scheme, thus enabling you to evaluate its effectiveness?

Ms Loriz-Hoffman: I have already mentioned this common evaluation and monitoring framework which we have put in place so you have a number of indicators which should measure the progress, efficiency and effectiveness of these measures. You have quite concrete input indicators. This is the amount of the expenditure you put in place for the

measure and then we control also the output, the number of supported holdings under the scheme. This builds up in a hierarchical process so finally, after all these indicators, we can better observe what kind of results you achieve in the framework of this measure. You come to an impact indicator on bio-diversity on maintenance of high nature value of farmland and forestry. We follow that up regularly in annual reports so Member States have to report regularly on an annual basis where they are with this measure, what they achieve with it and then also in the evaluation processes which are foreseen. This means that in the mid-term review and also at the end of the period Member States have to look into the impact the measure has had and they have to answer specific questions. One of these questions is as to whether and how far this measure has helped to ensure continued agricultural land use in areas with handicaps. They are specific questions addressing the difficulties which exist in less favoured areas and in the evaluation reports Member States will have to explain how the measure has contributed to these specific objectives.

Q30 Lord Palmer: Do you have any plans to change the annual basis of reporting back?

Ms Loriz-Hoffman: No. We have had the first annual report in 2008 and we are at the moment in discussion with Member States because there are sometimes difficulties with the indicators. Member States feel that it is not easy to report. However, we are in a permanent process and today we have a meeting in Brussels with the Rural Development Committee and there is another discussion on the indicators. We have also set up an evaluation network for rural development in order to discuss at length best practice on evaluation and how to best develop these systems of follow-up and of monitoring.

Q31 Lord Palmer: Is there any penalty if the Member States do not in fact complete the annual return?

Ms Loriz-Hoffman: If the report is admissible, so if the information is there we take it and nothing happens, but they have to deliver the results. I should say, if a certain indicator is missing we do not stop the payments but we work with them on a continuous basis on this and normally we also get that. This was the first report we have. For the coming years we will have a bit more rigid system in the sense that the report will not be admissible if a certain number of indicators are not provided. I think that through this Member States will themselves put it to a stronger discipline and we will get on board all the required information we need for the budget process. So it is not only a question of evaluation on the basis of these indicators but it is also to feed the budget process and to justify the attribution of the budgetary means for the next period.

Q32 Viscount Ullswater: When the LFA directive was first implemented in 1975 the system of payments to agriculture was completely different. It was very much subsidy payments, intervention payments and supporting for production. Now all of that has changed. How do you now feel the new revised LFA scheme fits in with things like the single farm payment, the agri-environment schemes and all the other things which have shifted away from production and much more to the environmental side of agriculture?

Ms Loriz-Hoffman: You are right, at a certain moment in time this was the only area linked payment but at the time it was also still linked to animals. I think in principle we have three main elements of area linked payments. First of all under the first pillar you have the direct payment schemes. This is clearly an income support instrument where you provide farmers with a certain minimum income which should provide a robust support of the incomes as a basic instrument. Then I think the LFA scheme is more specific. First of all, it is serving a specific objective as defined under rural development policy. Its objectives are at least partially environmental objectives. It is also on payment which adds to the income, that is the income these payments should serve in particular to allow farmers under difficult

circumstances to maintain farming and with that to contribute to maintaining land management and the countryside under difficult circumstances. In principle it is a compensation for these farmers operating under more difficult circumstances than a normal farmer in a region which is not handicapped. So far it is a specific regional instrument. Under the WTO we have also classified as a regional support scheme which makes reference to specific difficulties and which also has as an objective to serve environmental purposes, although it must not necessarily include any specific requirements to respect other environmental obligations than what is laid down in the direct payment scheme. Let us say it is simply compensation for the bigger difficulties these farmers incur. Then as a third layer I think we could identify the agri-environmental payment and the agri-environmental measures clearly should compensate farmers because they provide environmental services which go beyond what a farmer is normally expected to do. This is, let us say, the remuneration of an extra activity the farmer undertakes or the specific way to organise the management of agricultural land in order to produce a specific environmental benefit. This is then also specified so that the farmer has clear obligations which go beyond the baseline is, beyond what a normal farmer is expected to do and there is a specific payment linked to that which then reflects the specific costs and the income losses he suffers by following these specific activities. So I think you have the three layers: a general income support scheme, the direct payments and the specific support for farming in difficult regions in order to ensure that farming, biodiversity and landscape is maintained under these difficult circumstances, and then the agri-environmental schemes where you remunerate farmers for specific, well-defined environmental benefits they provide to society.

Q33 Viscount Ullswater: So this is really the LFA payment is really the only one which actually means that the people have got to farm. The single farm payment really does not include having to farm at all and some of the agri-environment ones can actually say, “No, we

do not want you to farm that area, we want you to leave it as natural as possible because it is the bird life we want to encourage". The LFA means that it has to be a farming system.

Ms Loriz-Hoffman: The actual legal basis we have in place defines farming also as maintaining the minimum requirement which means that if a farmer respects the minimum requirements under the first pillar he is also eligible under the Less Favoured Area scheme. Member States can, however, demand more specific conditions. They could, for example, say that farmers in LFAs would have to respect specific environmental aspects going beyond what they would have to do under the minimum requirements. Some Member States, for example, limit the livestock unit density in less favoured areas for those who want the payment. However, you have to see that you then switch a little bit into the direction of the agri-environmental schemes because there you can also support farmers for extensification. It is important to draw a clear line between what you think a farmer has to do under the Less Favoured Areas scheme and what you consider is a specific environmental benefit a farmer is paid for under the agri-environmental scheme. This is a demarcation line to be drawn if a Member State wants to charge or to have specific conditions for LFA payments which is possible in order to better target LFA to environmental purposes. This is possible but in any case should be considered as an area which has to be made consistent with what happens under the agri-environmental payments.

Q34 Viscount Ullswater: Do you see the schemes fitting neatly together or is there some overlap which we ought to be concerned about?

Ms Loriz-Hoffman: No, I do not think so. It depends on the Member States and how they design these systems. I think there is a certain openness and a certain possibility to design that, but I think it is important that there is sufficient awareness of where one scheme ends and the other starts. You cannot remunerate farmers for things twice and under the Less Favoured Areas scheme you should in principle compensate for natural handicaps where the

farmer has real difficulties. If you charge the LFA system with a lot of environmental requirements and specific conditions a farmer has to respect then you put him in a more difficult situation than a farmer in a normal region because they normally do not have to fulfil these requirements and you may also end up in a situation where you have a slight discrimination of farmers in LFAs because they would then have to respect higher requirements.

Q35 Earl of Caithness: One of the great advantages of the LFA scheme is that it is, compared to other schemes, remarkably non-bureaucratic and it is non-competitive. I think that is the point we were on a moment ago, just keeping the farmers in places where they would not be farming normally. I hope that does not change. However, given the alterations that you are proposing in your criteria, there is a danger that instead of the whole of the UK being one intermediate area the Commission will be faced with claims in the UK for intermediate areas, the islands and the mountains. Instead of having one holistic LFA for the UK you are going to be faced with three different categories within the UK as a result of your proposals.

Ms Loriz-Hoffman: Yes, but we have always had these three different parts. This is not new.

Q36 Earl of Caithness: It is new for the UK.

Ms Loriz-Hoffman: You do not have mountains.

Q37 Earl of Caithness: Yes, we do have mountains; it depends on how you classify a mountain.

Ms Loriz-Hoffman: You have islands I understand under article 20. These three elements, from my point of view, can play quite well together because the mountain areas are much easier to define because of altitude and you have slope and there are clear rules by Member

States to be respected and delimited. Under article 20, areas of specific handicap, the objective is not so much in maintaining against natural handicaps but it is more, let us say, for purely environmental reasons and landscape purposes. Islands are very much remote areas with specific circumstances. I think that all the three parts have specific purposes and objectives. In principle it does not seem to us to be a difficulty to have them in co-existence. I do not see that as a difficulty.

Q38 Chairman: Can I just say that the level of analytical clarity in what you have said to us today has been enormously helpful to us. It has really enabled us to understand the whole thing much better than we had before, so thank you very much indeed. I think the fact that you have such a high level of approaching it with a degree of analytical clarity actually produces a problem for you, does it not, because it is an area that has no analytical clarity whatsoever.

Ms Loriz-Hoffman: The difficulty is that first of all it is in principle a very technical matter with the pressures of the biophysical data and other measures. We did not enter too deeply into the discussion of the criteria until they are measured. I have people with me in case I needed help. At the same time, of course, this technical exercise of delimitation carries a lot of policy difficulties. If an area is in or out, that is an important question for an area and we are aware of that. In any case, I think that we tried to stick to the facts we have and to try to come with the work together with Member States to a situation where we bring a system into place which serves the objectives and is also applicable and feasible for Member States. I think this is very important.

Q39 Chairman: As I said, we have never had any evidence that anybody has ever listened to what we have said here so, just between you and me, do you think that Member States tended

to see LFA payments in the past as a bit of a slush fund that they can use to buy off nuisance farmers and keep them happy?

Ms Loriz-Hoffman: I think it is awareness raising about, let us say, the environment and the importance of farming for the environment because I grew up with the idea that forests are the best you can do for biodiversity which is not the case.

Q40 Chairman: Not our forests. There is no biodiversity in our forests.

Ms Loriz-Hoffman: I also had to learn that a lot of farming systems serve this objective much better. This was an awareness also that it is important to maintain these areas under specific conditions. I think you are right, what we have seen in the past and we have discussed this a lot with Member States and often refused, was that Member States wanted to change the LFA payment from one year to another quite drastically. We have already said that this cannot be a useful measure when it does not make a great difference whether it is paid or not; that is not logical in itself. I think today these things are taken much more seriously and that the Member States are aware that this is one of the three basic area-related schemes we have and that it should be used, from my point of view, in a good way to serve the whole exercise, in particular these regions.

Q41 Chairman: Can you give us some idea of the timetable for the review?

Ms Loriz-Hoffman: We are now in the impact assessment process and we intend to come to a decision by the Commission in a communication by the first of April. The communication will explain the exercise in which we are, it will set out these biophysical criteria as a possibility to delimit less favoured areas. We will in particular ask Member States to do concrete calculations and delimitation tests on the basis of these criteria and to come back to us with concrete mapping results.

Q42 Chairman: When?

Ms Loriz-Hoffman: I think Member States should have some months to do this exercise.

Q43 Chairman: Somewhere between what and what?

Ms Loriz-Hoffman: I think six months would be an appropriate time so that we would have a complete picture from the impact assessment. What we have now is an idea and we have a basis to compare with what we have got out of the European data set but we need more detailed information and this should come from Member States and complete the picture so that we can really say something about the impact of this system on delimitation. Then logically on that we should build proposals to be put forward to the Council and to be discussed subsequently in the order of time.

Q44 Lord Brooke of Alverthorpe: Chairman, I have a request rather than a question. I am wondering if we could have some up-to-date information from the Commission on the table of expenditure, what it is now.

Ms Loriz-Hoffman: What LFA is now?

Q45 Lord Brooke of Alverthorpe: Yes. For the whole of the EU, country by country.

Ms Loriz-Hoffman: For the whole of the EU we have an annual amount. Yes, we can get that for you. We have an idea about the total payment which is about 1.8 billion for the intermediate areas. This was in 2005, for one year. You have the data for the UK or should we also include that.

Q46 Chairman: Could you give us a table with the LFA expenditure for every Member State.

Ms Loriz-Hoffman: Yes.

Chairman: Thank you very much.