ENVIRONMENT AND RURAL DEVELOPMENT COMMITTEE

Wednesday 31 March 2004
(*Morning*)

Session 2

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ENVIRONMENT AND RURAL DEVELOPMENT COMMITTEE

10th Meeting 2004, Session 2

CONVENER

*Sarah Boyack (Edinburgh Central) (Lab)

DEPUTY CONVENER

*Eleanor Scott (Highlands and Islands) (Green)

COMMITTEE MEMBERS

Roseanna Cunningham (Perth) (SNP)
*Rob Gibson (Highlands and Islands) (SNP)
*Karen Gillon (Clydesdale) (Lab)
*Alex Johnstone (North East Scotland) (Con)
*Maureen Macmillan (Highlands and Islands) (Lab)
Mr Alasdair Morrison (Western Isles) (Lab)
*Nora Radcliffe (Gordon) (LD)

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Alex Fergusson (Galloway and Upper Nithsdale) (Con)
Janis Hughes (Glasgow Rutherglen) (Lab)
Jim Mather (Highlands and Islands) (SNP)
Jeremy Purvis (Tweeddale, Ettrick and Lauderdale) (LD)
Mr Mark Ruskell (Mid Scotland and Fife) (Green)

*attended

THE FOLLOWING GAVE EVIDENCE:

Joyce Carr (Scottish Executive Environment and Rural Affairs Department)
John McAllion (Oxfam in Scotland)
Fraser Scott (Farmcare Ltd)
Jim Walker (Quality Meat Scotland)
Allan Wilson (Deputy Minister for Environment and Rural Development)

CLERK TO THE COMMITTEE

Tracey Hawe

SENIOR ASSISTANT CLERK

Mark Brough

ASSISTANT CLERK

Catherine Johnstone
Roz Wheeler

LOCATION

The Hub

Scottish Parliament

Environment and Rural Development Committee

Wednesday 31 March 2004

(*Morning*)

[THE CONVENER *opened the meeting at 10:31*]

Common Agricultural Policy Reform Inquiry

The Convener (Sarah Boyack): This is the third evidence-taking session in our common agricultural policy reform inquiry. We hope that the panel that is before us this morning will enable us to explore food production and consumer interests as they relate to CAP reform.

I ask members to declare any relevant interests.

Alex Johnstone (North East Scotland) (Con): I declare my usual interests—I am a landowner and a member of the Scottish Landowners Federation.

Rob Gibson (Highlands and Islands) (SNP): I am a member of the Scottish Crofting Foundation.

The Convener: I welcome Ken Thomson, who is the adviser to the committee for this inquiry.

I thank the witnesses for submitting evidence in writing in advance of the meeting. It has been useful to be able to read it and to think of lines of questioning that we want to explore with you this morning. We will move straight to questions.

Maureen Macmillan (Highlands and Islands) (Lab): I welcome John McAllion—it is nice to see you again.

The Convener: Before Maureen Macmillan continues, I should indicate for the record which witnesses are in front of us.

I cannot read the signs at the opposite end of the table.

Jim Walker (Quality Meat Scotland): You have your specs on.

The Convener: Exactly. We have before us John McAllion, who is a trade campaigner with Oxfam in Scotland; Jim Walker, who is chair of Quality Meat Scotland; and Fraser Scott, who is operations manager for Farmcare Ltd. I apologise for interrupting Maureen Macmillan, but I wanted first to indicate who was who.

Maureen Macmillan: I want to ask John McAllion from Oxfam about some of the things that he has said in his submission.

At the bottom of the first page you say:

> "we are concerned that in practice 'decoupling' will be more apparent than real."

A couple of paragraphs later you say:

> "In other words, in practice subsidy payments will continue to influence production decisions, fuelling over-production, even though in theory the link between subsidy and production has been severed."

Can you explain why you think that? The other witnesses may also want to comment on the issue.

John McAllion (Oxfam in Scotland): There are a number of answers to the question. If we take 2002 as the point of reference, something like £746 million of CAP money is distributed in Scotland in any year. That figure is based on statistics that were provided by WWF Scotland and is derived from official Scottish Executive Environment and Rural Affairs Department statistics, answers to parliamentary questions and information that was made available to the CAP reform working group. The vast majority of that money is not included in the CAP reforms that are being discussed. In particular, the £290 million of export and production subsidies is not included. An element of subsidy will still be paid to producers in Scotland who produce a surplus and export that to the developing world at a price that is supported by export and other subsidies.

In a sense, decoupling is more apparent than real because it is based on historic payments. The pattern of distribution of support will be same as it always has been. That means that the bigger farmers—the agribusinesses—will continue to receive the vast majority of single farm payments. The smaller farmers will not receive them. The agribusinesses and the big farmers are the ones that tend to produce surpluses and export them. As a result of the payments, they will carry on doing that.

We believe that markets are not so much driven by consumers as by profit. If it is still profitable to dump surpluses generated within the European Union on the markets of developing countries—thereby making a profit that has been aided by subsidy—the big agribusinesses will continue to do precisely that. That is our main concern.

Maureen Macmillan: Is that happening? Are we dumping produce on third-world countries?

John McAllion: That is well documented. A major Oxfam report, "Rigged rules and double standards", exposes how, for a range of products, the developing world is subsidising agricultural produce in particular.

The European Union subsidises farm businesses to the tune of something like €115 million a day. If we consider the industrialised countries of the north—the EU, the United States of America and other countries—almost $1 billion a day is used to subsidise farm incomes. That is more than the income that 900 million people living in predominantly rural areas in the developing world have for themselves. We operate a very unbalanced and unfair trading system. The CAP is part of that. Our concern is that the CAP reforms do not address the international dimension.

Maureen Macmillan: Do you see a distinction between agribusinesses that produce a lot of surplus and producers in fragile rural communities in the Highlands and Islands? Producers in the Highlands and Islands are sometimes compared with third-world producers because they are simply primary producers: no value is added.

John McAllion: Oxfam argues that the CAP fails not only farmers in the developing world, but smaller farmers in the developed world. In Scotland, smaller farmers are being driven out of the industry. They are not being helped by the CAP; it is the bigger farm businesses that do well from the CAP. Our "Spotlight on subsidies" report drew attention to the fact that the vast majority of CAP payments go to the bigger farms and the agribusinesses. Smaller farms do not benefit. In a parliamentary answer, Ross Finnie pointed out that something like 8,200 small farms in Scotland do not even apply for CAP payments because they do not qualify. The distribution of CAP payments is very unfair. That hits small farmers in Scotland—as well as small farmers in the developing world.

Jim Walker: I would like to correct a few myths that floated about during that discussion. The red-meat sector is the particular interest of Quality Meat Scotland. The UK is only 60 per cent self-sufficient in beef production, only 85 per cent self-sufficient in sheepmeat production, and just over 70 per cent self-sufficient in pork production. The idea that somehow there is an oversupply of meat from the United Kingdom is a myth. Intervention stores in Europe are no longer full of unwanted beef. There is no beef currently in intervention stores anywhere across Europe and there is no sheepmeat in intervention stores anywhere across Europe. The EU exports only 8 per cent of the world's beef production. We are a tiny player compared with the United States, Brazil and Argentina. We export only 1 per cent of the world's sheepmeat production and 25 per cent of the world's pork production. We should put this discussion in that context.

EU figures for this year show that demand for beef in Europe will be about 7.6 million tonnes but that the EU will produce only 7.3 million tonnes—a 300,000 tonne shortfall. This is the first time in recent history that we have had a shortage of beef in the European Union. That shortage is manifesting itself in a big increase in the price of the beef used in products such as beefburgers and ready meals.

As I say, this is the first time that that has happened, so the committee should be aware that, as far as the EU and Britain are concerned, we are not talking about a world in which there is oversupply and dumping or storing of food, particularly in the red-meat sector, which does not have a market. We are talking about a market that is undersupplied, with a rising demand, particularly for beef. Consumption figures in Britain are at their highest for 15 years, so there is a demand for produce from Scottish farms. The idea of CAP reform and farmers being allowed to get nearer the marketplace has come about because there is a demand driven by consumers, not by profit. If consumers want to buy the product, they will pay the price that is required for them to get the products that they want. That will, in turn, at least give farmers and processors a sporting chance of getting a margin in the chain.

Fraser Scott (Farmcare Ltd): We are very much in a transitional period; CAP reform will take place over a number of years. In our business, we export cereal surpluses from the UK. It is not a very big tonnage and the majority of our exports—in barley, for example—are to markets within the EU. Many of our current exports are to specific markets, and we grow some of our barley specifically for export to other EU countries. It is not as if we are producing products that are going to third-world countries.

We are in a transitional period and we need the time to consider growing to specific markets in Scotland, the UK and Europe. It is not a case of just producing something for the sake of it. We are asking, "What can we grow? What contracts are available?" We have to say to ourselves, "We know what market we want to grow for. Here is the contract. Let's grow for it." We are not asking how much money we are going to get; we want to grow for a market, get the price right, make a profit and ensure that we are growing something that is specifically required, rather than growing X tonnes of a certain crop because we are going to get a payment. That is the important thing. We no longer believe that we should get payments just for growing 15 million acres—or whatever the figure is—of wheat. We are looking at the market and growing for it.

The Convener: John McAllion and Jim Walker talked about products going to developing countries. If those products are not from Scottish farming, do they come from other European countries, or is it from the US that subsidised food is still going to developing countries?

John McAllion: It is difficult to know exactly who is in receipt of export subsidies. In 2002, £215 million was paid through the CAP to producers in Scotland, partly in the form of export subsidies, so there are exports going from Scotland into the developing world. We cannot trace them directly, of course, because the Scottish Executive, the UK Government and the European Union refuse to reveal who is in receipt of those payments. We have been pressing the Scottish Executive to publish a list of all those farm businesses receiving in excess of £20,000 per annum in subsidy. That information should be published so that the Scottish taxpayer knows who is getting the money and to what use they are putting it. We cannot get that information because the Scottish Executive claims that that would be an invasion of the privacy of those businesses, although if they are legitimate grants—which they are—I do not see in what sense that could possibly be an invasion of privacy.

Dairy produce, cereals and sugar are all being exported from the UK into the developing world. There is absolutely no doubt about that. Many people in the European Union have argued at the highest level that the European Union has a trade deficit with the rest of the world. What they do not explain is that, over the past decade, that trade deficit with the rest of the world has come down from some €7 billion to just €200 million. In fact, British farm businesses are exporting in big numbers into the developing world.

An example of that is exports to Jamaica, where European Union exports of milk powder have more than doubled during the 1990s, with the result that the Jamaican market has been flooded with cheap milk powder products that have been bought up by the big processor, Nestlé, which operates in Jamaica to the detriment of Jamaican farmers who produce fresh milk and have seen the demand and the market for their milk collapse. Their share of the market has collapsed, their income has collapsed and their families have been put at risk because of the policies that are pursued by the European Union, including Scotland, which is part of the same set-up.

10:45

Jim Walker: Just to clarify, no beef would be exported to any country outside Britain because beef exports are currently banned. The only way to export is through the date-based export scheme, which I hope we will be able to remove over the next three months. The help of this committee and others would be extremely welcome on that.

Approximately £25 million-worth of sheepmeat is exported from Britain, but all to the near continent: France, the Benelux countries and Italy. None is exported to third-world countries. We do not grow sugar in Scotland. Fraser Scott might be able to add to this, but I am well aware that any cereal exports from the Scottish market are specific products for specific markets, almost exclusively on the near continent.

The majority of the milk that is produced—mainly in the south-west and north of Scotland—goes to liquid consumption because there is so little milk production. That milk is supplied through dairies such as Graham's Dairies Ltd and Wisemans. More than 50 per cent of the rest goes into cheese. There are no powder processing facilities in Scotland. We are talking about something that might be an issue in other European countries, but it is not an issue in Scotland.

The £200 million that John McAllion mentioned is not paid directly to any Scottish farmer. Scottish farmers receive direct subsidies of £450 million per year—they have exactly the same subsidy levels and historic levels as other European farmers. Part of the confusion that we have seen this morning is because we are talking about CAP reform, not about changing World Trade Organisation agreements; that is a completely different issue for another day. The European Union is taking the first step in trying to set itself up so that WTO negotiations take place in an atmosphere that allows the EU to do better than it is currently doing. CAP reform and the WTO are not the same thing, and export tariffs and trade barriers and the other concerns that John McAllion has should be taken up during WTO negotiations and not during a committee meeting about CAP reform and its effect on Scottish farmers and consumers.

The Convener: Do you want to come back on that, John? I do not want the discussion to become a dialogue between the two of you.

John McAllion: Exactly, but it is important to draw the distinction. The issue is not just about farming. The direct farming sector in the UK is worth less than 1 per cent of the gross domestic product, but the agri-food sector is worth approximately 8 per cent of GDP. Processors qualify for payments under the CAP. Export subsidies would go to processors and exporters and not directly to farmers. There are people operating within that sector in Scotland and the UK who get subsidies to export produce into developing country markets with terrible consequences for the farmers in those areas. It is time that that issue was addressed.

Alex Johnstone: I am in danger of straying into WTO issues. John McAllion uses the word "surpluses". How do you define a surplus? For the purposes of simplicity, let us consider something simple such as the international wheat trade. How do you define a surplus within that?

John McAllion: A surplus is produce that cannot be sold into local markets and has to find a market elsewhere.

Alex Johnstone: So are you opposed in principle to the idea of the international trade in wheat?

John McAllion: No, we are in favour of international trade in wheat, but we want that trade to be fair to both the developed and the developing world. The current situation is very unfair to the developing world and rigged in favour of the developed world.

Jim Walker referred to the fact that we no longer have warehouses stuffed full of milk powder and cereals waiting to be destroyed or disposed of in some other way. That is true, because it is now exported with the assistance of export subsidies. It is not always exported elsewhere in the EU, but outwith the EU. A special payment is made for trade outwith the EU that goes to part of the agri-food sector in this country to enable it to export the surpluses that it cannot sell in the EU at a price that will bring a return. It is a profitable business; it makes money for agribusinesses in the UK, but it destroys the livelihoods of farmers in the developing world. That is Oxfam's main concern.

Alex Johnstone: It becomes clear to anyone who has studied the international grain trade that grain production is not consistent from year to year. It follows a three-year, five-year or eight-year cycle. As a consequence, the storage of surpluses over that three-year to eight-year cycle is essential for stability in world trade. At present, we are in a position in that cycle in which the stores in Europe and North America are almost empty. Consequently, the demand for grain is higher than it has been for a number of years. Would you define the stores being full as a surplus? How do you interpret the fact that the stores are almost empty?

John McAllion: As I said, I define a surplus as produce that cannot find a market locally, either in Scotland, the UK or the European Union, which means that the producer must search for buyers elsewhere.

Alex Johnstone: Therefore, I suggest that, over the five to eight-year cycle, which is accepted as the normal cycle in the international grain trade, there is not, and never has been, a surplus.

John McAllion: The idea behind the common agricultural policy is to ensure that farms in the European Union secure the food supply for the nation states of the European Union. Given that, why does the European Union export subsidised agricultural produce to the developing world? Why are European Union taxpayers expected to support that export? That export is unfair because farmers in the developing world were told that they should have a comparative advantage under market conditions. Now they need comparative access to subsidies. European Union and US agribusinesses receive subsidies, but farmers in the developing world do not. The situation is unfair and rigged and it is time that it was addressed. However, that will not happen unless the matter begins to be addressed through the common agricultural policy.

Alex Johnstone: Are you aware that, in the past 12 months, grain exporters from Europe have been subjected to levies because of shortages in Europe? Rather than an export subsidy, an export levy has been in place.

John McAllion: The situation varies from year to year. There was a time when export subsidies were meant to be phased out or reduced dramatically, but in years in which there were shortages, producers could carry over export subsidies and save them up to use to their advantage in other years. It is possible to turn off the public because of the complexities and technicalities of the common agricultural policy and how subsidy is paid. Oxfam does not speak from Oxfam's perspective; it speaks from the perspective of countries in the developing world. At the WTO meeting in Cancún, those countries demanded that the CAP be reformed in an international context and in a way that is fair to them, as well as being fair to farmers in the European Union and the United States.

Alex Johnstone: Do you see the European Union's farmers having a role in international markets in the future?

John McAllion: Yes, as long as the trade rules are fair to both the developed and the developing worlds. Oxfam's point is that the trade rules are not fair; they are rigged and use double standards. It is time that that issue was addressed and one way of doing so is through reform of the common agricultural policy.

Fraser Scott: Scotland currently has a deficit in wheat. World stocks are about 120 million tonnes, which might sound a lot, but is actually only eight days' supply. We have great opportunities in the EU and further afield. We have to get our markets and growing costs in order, but there is a great opportunity in other countries, such as China. China is a big agricultural producer, but what we can do in Scotland, for example with malting barley, gives us great opportunities for developing markets.

Alex Johnstone is correct that production is cyclic. Given the rise in the population, there will be more people to feed in the next 50 years. The environment and the weather cause many problems in production here, in the US and in Europe. We must be careful about saying, "We want to produce X tonnes." We must have some contingency measures in place.

Jim Walker: I find the definition of a surplus that has been given extraordinary, if it means that producers should produce only for the local market. That would make New Zealand's agriculture interesting, given that it exports more than 90 per cent of its dairy, sheepmeat and beef products to markets throughout the world. I reiterate that Great Britain is only 60 per cent self-sufficient in beef and 85 per cent self-sufficient in lamb. We cannot fulfil the consumer demand for the product, which means that we suck in imports from developed and developing countries from throughout the world. We are a ready market for beef from Argentina and other South American countries and from African countries. We want to address that situation in this country, because we want to be allowed to produce for a market requirement and consumer needs. As a result, we hope that the proposed changes to the CAP will allow us, as Fraser Scott said, to focus on the marketplace and on real demand. If the demand exists, the margin and the profit should follow later.

Rob Gibson: I am an old-fashioned internationalist, and my party believes that people in the third world ought to be able to have a development box in which a prime part of their agriculture could produce for the local market.

The mid-term review appears to see Scotland in a similar way. Less favoured area payments, the national envelope and modulation are means whereby we can take account of the difficult conditions in which highland farming produces for the market—conditions that put such farming at a disadvantage compared to many of the lowland areas. Since the bulk of Scotland has less favoured area status, I would like the panel's views about how to better target less favoured area payments; about the length of time the national envelope for beef should be maintained, especially in the interests of places like Orkney, which produces very high quality beef; and about how modulation might be used to help support the non-agricultural element of keeping people in the countryside so that they can produce specific product for the market.

Jim Walker: We know that about 83 per cent of Scotland has LFA status. We are concerned that changes to the CAP will mean that we might not have the raw material that lowland finishers, processors and others need to supply market demand for quality beef and sheepmeat. Primary producers in the hills and uplands of Scotland might decide, for example, to farm sheep and reduce cow numbers because doing so would make it easier to keep a farm in good agricultural condition. It would also reduce a farm's cost base, because there would be no need for the machinery and so on that suckler cows require. If that happens, it is possible that what we describe as the engine room of the industry in Scotland—the raw material source—might dry up. That would be a disaster for the Scottish farming and processing industries, and for Scottish consumers, who would lose the ability to buy quality Scottish beef from shelves around the country.

Recently, we commissioned surveys that, every month, track consumer attitudes and demand for Scottish products. The surveys show that we have hit the highest levels of awareness of Scottish beef and the highest numbers of those who are prepared to buy the product in the history of its production. When the Scottish public were questioned on the subject, more than 70 per cent knew what the beef looked like; were aware that it is produced to a high standard; and said that they would like to have the chance to buy it.

You quite rightly pointed out that instruments such as the national envelope, the targeting of LFA support and modulation can be used to allow the continued production of raw material. The timing of the national envelope is interesting, because two things need to happen over the next 12 months to assist the Scottish beef industry. First, at some point, beef from over-30-months cattle born after 1 August 1996 will be reintroduced into the food chain, which will increase the supply of beef in the UK market by about 175,000 tonnes in 2005. Despite the undersupply of manufactured beef across Europe, people are nervous that, unless the markets that are currently closed to that beef are opened up, there could be a market dislocation in the early stages of its reintroduction. We simply do not know what will happen.

At the same time, primary producers in the hills and uplands are making decisions about whether to keep cows in future. As 75 per cent of the quality beef that is produced in Scotland comes from the suckler herd and is not a by-product of the dairy herd, the price of those store cattle and calves will certainly drop. At the moment, when the animals are sold at an auction mart, they carry a subsidy entitlement. The buyer of the cattle—the man who finishes them—is able to claim beef special premium payments and slaughter premium payments and can then give some of that money to the primary producer, which adds to an animal's value.

A male animal, for example, that is 10 months to a year old, leaving an upland farm in Scotland, would be worth about £500, give or take. Of that £500, about £200 is the subsidy that the next person who buys that animal would get if he took it to finishing. The way in which historic payments are calculated means that the primary producer—

the man who sells that calf for £500—will not get any part of that £200 subsidy.

11:00

It is likely that next year, when the single farm payment is introduced, those animals will reduce in value to the primary producer from £500 to £350 or £400 or whatever the price might be, potentially at the same time as beef is reintroduced from over-30-month cattle. If the price of cattle drops, a fairly marginal existence at the moment will become an existence that does not yield a profit. The simple answer to that is to get rid of the cows, keep the single farm payment, to which the farmer is entitled, because the historic basis is there for doing that, and continue to farm sheep or something else. That is why we are so interested in a national envelope payment for areas such as Orkney—and others across Scotland—where primary production takes place. Rob Gibson is correct that the remotest areas will be under the greatest threat.

A national envelope needs to last until the transition period is over, because beef production is a two or three-year cycle. You put a bull out to a cow now, she produces a calf in nine month's time, and you kill the animal 18 months to two years later, so you are talking about a three-year cycle. The national envelope would have to last for at least one beef production cycle, until the market settles down. Hopefully, the demand for beef will continue to rise, and we will get access to export markets, which will allow the finish price of animals to rise, then the returns to primary producers from the marketplace will increase, which will make their decision to keep cattle on much easier.

The final method that Rob Gibson talked about is modulation. Most of the talk about modulation funding has been about environmental benefits around the country and other diversification programmes. I have no problem with that, but it is also possible to pay for quality production through modulated funds. Articles 21, 23 and 24 of the rural development regulation, as amended last year, allow for assistance for people who produce quality. With regard to quality, Scotland is second to none, in terms of its standards and the number of animals that meet the spec and find consumer markets readily, because the beef essentially is reared on grass on the hills and slaughtered for a quality market.

I ask the committee to examine those issues in its final report. The issue is not only the environment or diversification, but quality food production. In our view, all three can co-exist. It is possible to keep cows on the hills of Scotland in an environmentally friendly way, and encourage quality production from the engine room of the hills and uplands in Scotland, to allow the meat from finished cattle to reach the shelves of retailers in this country or other places that want to buy quality products. That is what the CAP is about—producing for a marketplace, not producing for a surplus, as John McAllion explained earlier.

Rob Gibson: Thanks for a detailed explanation. Some of the other witnesses may have something to say, but I have a couple of follow-up questions.

John McAllion: May I come in? With reference to Jim Walker's remarks about surplus, of course nobody objects to any country exporting produce as part of international trade. New Zealand does that without the massive subsidies that the European Union farms receive. Nobody would have any objection to EU farmers exporting a competitive product, but what we object to is the massive subsidies that allow them to compete unfairly in global markets.

CAP payments are targeted entirely at the people who least need them. An analysis of the 2002 payments shows that 47 per cent of farmers in Scotland received just 4.2 per cent of the cash that was available, which amounted to an average payment of about £1,500 each, while fewer than 2 per cent of the farms in Scotland received a massive 17.3 per cent of the cash. In fact, 27 farm businesses in Scotland are receiving around £250,000 or more every year from the common agricultural policy. Those farms are not in the marginal areas of Scotland.

If you are asking me whether modulation at 10 per cent addresses that problem, the answer is that that does not go far enough. To start to tackle the unfair distribution of subsidy payments throughout the country, modulation would have to be nearer the limit of 20 per cent. Does it help the situation to base the single farm payment on historical payments? Of course not, because that freezes the unfair distribution of payments—something must be done about that. I hope that the committee will address those two areas in its final report; if they are not addressed, the payments will not make a substantial difference to marginal farming areas in Scotland.

Fraser Scott: I agree with Jim Walker, in that we need the market. Beef is important in Scotland, as are sheep, and cereal producers in Scotland need internal markets as well as external markets. Producers need to be able to grow cereals at the right cost of production to supply the fattening areas of Scotland. We do not seek to inflate the market; it is more important to get the cost of production and the market right so that businesses can get contracts and move forward. I return to the fact that we must be focused; if there is a good market for Scottish beef, we must be able to produce cereals at the right cost.

I agree that modulating payments to feed into environmental issues is what the public want and require, but it is important to ensure that we do not confuse the matter and make modulation too complicated. We need to look after our environment, and farmers want to do that, but it is important for the process and the payment system to be simple. How will the payments be issued? If we make the system too complicated and there is a lot of work involved in getting money to do something, people will not do it, so it is important to keep the system simple.

On the historical basis of payments, we will have time on our hands in the next few years to change our businesses and to focus on the market. Historical payments will certainly help Scotland's farmers today but, as I mention in my submission, farming policy in 10 or 20 years' time should not be based on payments that farmers were given between 2000 and 2002. We must be given time to change our businesses in relation to the market. We will see what changes come about, but we need a policy from the Executive on how to move forward. It is important that things do not change too quickly, because we have to structure our businesses for the next 10 to 15 years.

Rob Gibson: I want to follow up a couple of points. First, the obvious point about data protection is rather interesting. If someone is in receipt of a payment from an enterprise company, that information will be published in the local papers. It is an anomaly that that is not the case with agricultural payments. You might want to comment on that. The Executive seems to hide behind the fact that the European Union will not shift on that point, and the committee ought to take the matter seriously.

Secondly, I want to refer specifically to supermarkets. Labelling on the quality of our beef is a good idea. Our beef ought to be available to our population at reasonable prices—we form a market that could do with high-quality food, given the state of our health. Do you think that pressure should be put on supermarkets to label food to show not only where it comes from but the processes that are involved in its production? Should that information be made available to consumers, and does the mid-term review have any leverage on that?

Jim Walker: I do not think that there is any scope for that in the mid-term review of CAP reform, but there have been beef-labelling initiatives from Europe and labelling is compulsory for fresh produce on the retail shelves around Europe. The country of origin has to be stated, along with the kill code of the abattoir.

Quality Meat Scotland has run campaigns during the past few months, and more than a million leaflets have been delivered to households all over Scotland in the past week to explain the system so that people understand it when they go shopping. For the committee's benefit, I point out that if the kill code on the pack begins with 1, the meat comes from a Scottish abattoir or processing facility. If the code begins with a number between 2 and 8, the meat comes from England. Codes that begin with 9 indicate that the meat comes from Northern Ireland. If the code begins with anything else, the pack is not from the UK and it is up to people whether or not to purchase it.

Rob Gibson: You are advertisers with a gigot problem.

Jim Walker: Exactly.

The problem comes with processed food. Once something is done to such products—if salt or pepper sauce is added, or whatever happens to them—all that they need to carry is a label or ticket that says "Processed in the UK" or "Processed in the EU". Thereby hangs the problem, as a big percentage of food—33 per cent according to our most recent survey—is processed before consumers see it. There is no necessity or requirement to carry labelling other than in respect of where the processing took place and it would be extremely useful if the committee and the Parliament did all that they could to lobby in Europe and Westminster to get that changed as quickly as possible. Scottish farmers and the Scottish food industry would take their chance with the best or the cheapest in the world as long as there is clear labelling to allow consumers to have a choice.

Rob Gibson is right to say that every consumer should have the choice to buy high-quality food. If they can pay for it, they should be able to decide whether to do so. We already know that supermarkets and others are importing vast quantities of protein from other countries. Steaks from Argentina, Namibia, Australia and other parts of the world are freely available on shelves throughout Scotland—I could take members to any number of outlets today and find those. However, there is a problem when one sees ready meals and other processed products. A person will have no idea about what they are buying or the production standards that have been used.

It is interesting to make international comparisons, which John McAllion has majored on this morning, and compare the sizes of farms. In Scotland, LFA farms average 112 hectares. In general, farms throughout Scotland average 173 hectares. The average size of a beef farm in Australia—which is one of the biggest exporters of beef in the world—is 13,500 hectares. Last week, I met a farmer from Brazil who farms 144,000 hectares, which I think is bigger than Denmark. He thinks that he has 150,000 beef cows on his ranch, but he can never get them all in at once. He gathers them twice a year to vaccinate them for foot-and-mouth disease. He does not have

Scottish Environment Protection Agency or Health and Safety Executive inspections or many of the other inspections that our producers and processors are used to having in order to produce to quality standards that allow consumers to know what they are buying.

Rob Gibson is quite right. If we are able to label meat and then sell the positive message of standards of production and quality, not only can we be internationally competitive, as there can be differentiation, but the size of farms will not matter. The big farms will employ numbers of people—the big farms and big processors employ the 30,000 people who are currently involved in the Scottish red-meat sector. Small-scale farmers can be either part time, or full time if they want to be, which would be fine. Nobody is squeezing anybody out. However, a small farmer in a remote area will find it extremely difficult to compete in an international marketplace against competitors with 150,000 cattle and 144,000 hectares, no matter how much support CAP or the Scottish Parliament throws at them through social or productive subsidies.

The Convener: Nearly every member wants to come back in. Members who have already said something want to come back in, but preference should be given to members who have not yet said anything. Are you finished, Rob?

Rob Gibson: I think that John McAllion wants to say something.

The Convener: I ask John McAllion to keep what he says relatively brief so that others can contribute.

John McAllion: Oxfam is very much in favour of CAP reform. It favours a green, fair, sustainable, and, above all, transparent common agricultural policy. It very much supports transparency in all CAP payments. Some £750 million of payments are paid in Scotland every year, which dwarfs the amount that is being spent on the new Scottish Parliament building. Unlike what is being spent on the new Scottish Parliament, such payments are not one-off payments; they recur year after year, but taxpayers and citizens do not have the right to know who is getting how much of them and to what use they are putting them. That is a national disgrace.

On the scale of farm businesses, in a global context, there are currently two farming models. One model is large-scale, cattle-intensive farming—which is hugely supported by measures such as the common agricultural policy—and the other is small-scale, smallholder, labour-intensive farming. Oxfam passionately believes in labour-intensive smallholding farms because we believe that such a model will allow the developing world to produce its way out of poverty. However, the model is under threat as a result of global trade rules and subsidy systems such as the CAP.

The Convener: Perhaps the transparency issue is something that we should take up with the minister. He will be our next witness in three weeks' time, so perhaps we can follow up those issues then.

Karen Gillon (Clydesdale) (Lab): I am interested in some of the comments that Jim Walker and Fraser Scott made on the national envelope and historical payments.

I am glad to hear Jim Walker argue his case, because he is the only witness who has argued in favour of the national envelope, and I would be interested to know why he believes that the national envelope is a much better option than modulation. He talked about how modulation can be used to support quality beef production and about Orkney being a quality beef producer. Why could modulation not be used instead of the national envelope? A number of other witnesses have said that the national envelope is not the right way forward and are concerned about its possible implications.

Fraser Scott made a comment about the historical payment and about farmers needing time to change—he mentioned 10 to 15 years. Should the historical payment stay for at least 10 years? If not, after what length of time should there be a review? That is an issue.

11:15

Fraser Scott: It is, but I did not say that; I said that our investment decisions are made over 10 to 15 years. The historical payment will give us some time in the short term, but I am sure that there will be a review in about five years' time, and we need to look at it, because we have a registered period in which we know the basis of the payment, however much it gets modulated or changed, which I am sure that it will. That takes us back to my point that we are growing for the markets going forward, not looking back. I am trying to get over the fact that we can grow only the products for which we have contracts out of which we are able to make money. The baseline for the historical payment is from two or three years ago, but things change and businesses change. However, in the short term, the historical payment will give us some time to review our businesses.

Karen Gillon: Has there been any analysis of what the market is and of what Scottish people buy?

Fraser Scott: In what way?

Karen Gillon: If the idea of decoupling is to allow farmers to relate their farming to their local markets, has there been any analysis of what the local market is and what the purchasing trends are among Scottish people?

Fraser Scott: In Scotland, Farmcare Ltd has local businesses and has export contracts for malting barley, milling wheats and other high-quality wheats, for example. We are being offered contracts for two or three-year terms; millers and maltsters are asking us what we think our costs of production will be in future and whether, if they offer us contracts at £X, we will be able to make money. It is important to know what policy will be—what we might or might not get and how policy will change—because we will be able to decide, if we know our cost of production, which is the most important thing, whether to take a contract at £80 per tonne. When we plan our budgets, we must ask ourselves what it costs us to produce a tonne of wheat or barley. If we manage our fixed costs, inputs and rents properly, if we are able to negotiate properly and we know what we have coming in, and if we know that we produce our wheat at £70 per tonne, we are able to take on a contract at £80 per tonne or to fix a price on the futures market, develop our risk management and say, "Yes, we can develop our business over the next few years."

We will start to plant the crops for 2005 in July and August this year. We have to ask ourselves what we should grow, what market we are going for, and what it costs us to produce the crops. If, in August, wheat is only £60 per tonne and it costs us £70 per tonne to produce, are we going to put wheat in the ground? On the cereals side, we must find mechanisms—whether contracts, futures trading or something else—to ensure that we put something in the ground that we are growing for a market or that we are able to hedge forward and out of which we will make some money. We are in the risk game, and some will be happy to put wheat in the ground if the market is £50 per tonne, but we have to consider what we are going to grow for specific markets, whether wheat, milling wheat or barley.

Karen Gillon: Perhaps I am being naughty, but if the market is prepared to pay you only £50 for a product, why should I pay you to sell it for £60? If I want to buy something from a shop for £1, but it costs the person in the shop £1.20 to have it, why should someone else pay for them to get £1.20?

Fraser Scott: In future, we will grow for the market, so the price will be £1. I hope that we can grow the product for 80p and make a profit.

Karen Gillon: So you would need a subsidy.

Fraser Scott: At the end of the day, there will be decoupled payments and we will examine our markets. When we do our budgets, we will examine all that comes in and goes out. Historical payments are important—not just for the growing of the crop, but for what you want us to do with the money. That is why modulation has been introduced and payments have been directed into other areas.

Karen Gillon: If the market can sustain a price and you can produce for less than that, without payment, why should you get payment? If the market price rises and you can make a profit without receiving a subsidy or a decoupled payment, why should you still get the payment?

Fraser Scott: It depends on how we want to move forward with the policy of farming Scotland and whether we want farmers not to have set-aside or environmental initiatives. If payments are truly decoupled and a farmer is making a profit from his farm, his business will be well run and environmentally the farm will be the same. We must ask ourselves what we want to do with environmental and decoupled payments. We must take time to allow that to emerge. Ultimately, payments will be decoupled and the true market will be revealed, if we allow that to happen.

Jim Walker: Karen Gillon asked what consumers want to buy. A big part of the work that QMS does is to track consumer trends, demands and needs. For example, we know that on average Scottish consumers eat 22g of lamb a week, compared with 54g in England and 58g in Wales, where people are big lamb eaters. We know that on average people eat 16kg or 17kg of beef a year, whereas in Argentina they eat a whopping 60kg a year—down from the maximum of 100kg, which I am not sure would be great for anyone.

We track markets both at home and abroad. Last year, in conjunction with an organisation called Food from Britain, we carried out a big study of all European markets where Scottish red meat—beef, in particular, and lamb—may be sold again, such as Italy and the Benelux countries. In those countries, the product still has a fantastic reputation. There are high levels of recognition of the brand and of the name Scotch: 57 per cent of people in Scotland and 31 per cent of people in England, which has 50 million consumers, say that they would pay more for Scotch beef.

Our problem is that we do not have enough supply. I have seen probably 17 models that try to illustrate the reaction in Scotland to CAP reform and decoupling. The EU, the Scottish Agricultural College and QMS have a view on what will happen, but the truth is that no one knows. I do not think that the vast majority of people—including those in this room, but especially those on farms across the country—understand the huge change in attitudes to farming that decoupling will bring. This will be a fundamental change. It has the potential to be the biggest change that has taken place in my lifetime and in the past 40-odd years. It is a huge change when a farmer does not have to keep something physically in order to get support payments.

Let us say that the figure for beef supply drops by 10 per cent in Scotland. That is 50,000 animals out of 500,000. Right now, we cannot meet the demand for the product that exists. If we continue to grow demand, we will have a serious problem. Abattoir costs will rise, because when throughputs drop the unit cost per head increases.

The reason why we are suggesting a national envelope is simple. We are examining the whole industry and what will happen to Scotland if abattoirs have increased costs and overcapacity. We want to be able to meet consumer demand for the product. At the moment, a national envelope is the only tool that is available to act as a backstop in case, as I explained earlier, farmers take the decision to put off animals.

I have no problem with the rural development regulation being a tool to use in the future, but there is no delivery mechanism right now and right now is when the decisions for 2005 will be taken. It will be possible to amend the rural development regulation beyond 2006 for 2007 and potentially take the money from the national envelope, transfer it to the second pillar and pay it through the rural development regulation, but that ability does not currently exist. My concern and that of the meat industry—Scotland red meat plc—is that by the time the decision could be taken to move that money and deliver the funds back into the industry through the rural development regulation it would all be done and dusted. Once cattle start being removed from upland farms or hill farms around Scotland, they will never return. Suckler cow production in Scotland is currently a very marginal enterprise.

Remember that we are taking the decision against the backdrop of there being no export markets. The market for beef from Scotland would currently be worth £150 million, which is what it was worth in 1995 before the ban on beef. Prices are artificially constrained because we have no competition in our marketplace from exports. We need a mechanism to act as a backstop until that market reopens and works normally and we are in a normal market situation.

If there were free markets, no over-30-months scheme, none of the fallout from BSE and none of the problems with exporting, the decision to allow market forces to prevail and not have a mechanism such as the national envelope would be simple. However, we are not in that position. The market reality is that cattle are now worth £1.90 a dead-weight kilo in Scotland compared with £2.50 in 1995. They are worth 60p less per dead-weight kilo, which equates to about £200 an animal, because we do not have access to the markets that want to buy our beef. That is why we need to have a mechanism in place until the market settles down; it needs to be in place for two or three years.

Karen Gillon: Why are the beef farmers in Clydesdale telling me that they do not want a national beef envelope?

Jim Walker: The reason for that is simple. It is because individual farmers are looking at their own individual take from subsidy. They will get more money, if they are finishers of cattle, by having the money to themselves. They will get the money as a single farm payment.

We are looking at the whole of the Scottish beef industry and the supply of cattle in the future. If an individual in Clydesdale or anywhere else in Scotland decides to put off 50 cows, it is a marginal decision for his business, but if 5,000 producers decide to put off 50 cows, it has a massive effect on the overall balance of the meat industry in Scotland. Our job is to put forward arguments and the case for the Scottish red-meat industry. Farmers, as individuals, can argue for what they want on their own farm; like anybody, they will try to maximise the return to their own business. However, that will not necessarily be in the best interests of the Scottish industry as a whole—now or in the future.

Nora Radcliffe (Gordon) (LD): I will start with a couple of questions for Fraser Scott.

First, it is generally seen that the historical farm payment is an interim measure to give stability. I would like some technical advice about what practical constraints there might be on farmers adjusting their arable cropping business. Jim Walker said that we have to keep the envelope for three years because there is a three-year beef cycle. Is there a similar cycle of production that we need to be aware of when we try to decide on a sensible way to move from an historical farm payment to a different way of distributing the money?

Fraser Scott: The important point is the time factor and the recognition that many farmers are not thinking about what effect the payment mechanism will have on their business. It is important that budgets are produced, as they are in any professional business, and that we examine our fixed costs. All those things need time so that we can get to a situation where people realise that the payment might change.

The important aspect is farmers realising, as Jim Walker said, that the way in which we will go forward in the next 10 years requires a fundamental change in mindset: it is certainly the biggest change since the mid-1970s. It is about farmers concentrating on how they can manage the risk over the next few years, how they can trade and how they can reduce the risk in trading their cereals, beef and so on. Farmers should ask, "What does it really cost me to produce at this level?" Perhaps they should take out the historical payment and rental payment and have a look at the fixed and variable costs that they are putting into their business. People really have to focus on their business during the interim period because there is going to be fundamental change during the next few years.

11:30

Jim Walker: This is 2004. The mid-term review took place in 2003. I spent a year running backwards and forwards to Brussels to agree the agenda 2000 and to lobby in the agenda 2000 negotiations. At that time, with agreement from the Commission and the Council of Ministers, we were promised that there would be a review of cereal prices in 2003 and a look at how the reforms of 2000 were operating in other sectors. We then got a fundamental reform of the CAP package.

Do not believe for a second that now that we have had a reform, that is the end of the reforms. What is happening now will be happening in 10 years. As long as it is not on the record, I will bet the price of my house that in 2008, three years after the start of this reform, we will have another fundamental reform. I would not get hung up on the fact that payments will be based on the period 2000 to 2002, because it will change again.

We should not rush in with decoupling and the attitude that we should allow farmers to get used to that first, then change again in 2008. There has been a move to area-based payments south of the border, and you have all read the reports of what is happening down there and the disastrous consequences for small, extensive, family-run beef and sheep farms, which are getting wiped out.

I have a friend in Devon who won the lottery. He currently gets a subsidy of £30 per ewe equivalent. He is 57 years old and he is about to get £384 per ewe equivalent in an area-based payment because he happens to fall on the right side of a line. However, there are family-run, livestock farms—not big farms or agri-businesses—that are losing hundreds of thousands of pounds and that is the alternative to historical payments as things stand. We should let historical payments bed down, and use the tools that are available to protect the bits of the industry that the forward strategy and other initiatives in the Parliament have agreed are important for the Scottish economy. Let us then work on the changes, which might be a move from the national envelope to rural development in 2007, 2008, or whenever. The change must be gradual or the fallout will be colossal.

Rob Gibson knows that better than anyone. We just have to look at the redistributive effect of the change from hill livestock compensatory allowances to LFA support, which changed the production-based headage subsidy to an area-based subsidy. That is evidence of what a screw-up such changes can be and the pain that massive redistribution can cause.

The pain is not always caused to the small farmer; it can also affect the guy who happens to be in the wrong place, farming the wrong thing on a particular day of the year. We should not fall into the trap and that is why we welcome what the Executive announced today.

Nora Radcliffe: I take all that on board, but I am trying to get a feel for where we are going to be in 10 or 15 years. We know that we are not going to stick with historic payments and that there will be change. We are trying to establish a degree of certainty about what that change will be and the speed with which it will come about, and we are trying to get a feel for the constraints on making those changes. You said that we have to take into account the three-year cycle of beef production. I am asking whether we have to take something similar into account for arable farming. Are there constraints on the crops that can be grown or how they are grown that we should know about to inform our conclusions about how the changes should happen?

Fraser Scott: The farmer will have to decide whether he farms the land or not. He will have to ask whether he should farm a percentage of the land and what is the best crop to grow. If we have good wheat, barley or rape markets, perhaps rotating those crops is the correct thing to do. The focus should be on working with retailers and merchants and growing the crops that they need.

At the end of the day, we are supplying the food chain through retailers who sell a product to the public, and it is important that we get that line correct. Some fairly important decisions will have to be made, even in our businesses in Scotland. We will have to sit down and say, "We shouldn't be growing this crop. What else are we going to do?" We need to focus again on the costs and the budget and say, "No, we shouldn't be growing that crop. Let's grow this crop on contract." It will be much more down to the market than to people saying, "We'll do this for you and you'll be all right." We will have to get farmers to ask what the right crop is to grow on their land and what they grow really well. Whether their crop is potatoes or a cereal, farmers must ask what their farms can produce and whether they can get their costs thoroughly focused. That will allow the market to come in, but we need that period of time. We cannot just stop and start such things.

Jim Walker: The other thing that we should take into account is something that has not been mentioned this morning but which is absolutely vital. We work not in a British market or a Scottish market, but in a European and—for red meat, I hope—a world market. We must look at what our competitors in the European Union are doing with their farming businesses as a result of CAP reform. As you know, the French are not even going to start the reform until 2006, when we will be a year into it. They are going to retain 100 per cent of the suckler cow premium, which will retain the same number of suckler cows as they currently have. The Irish have plans to retain all their suckler cows as well. The Spanish and the Portuguese will retain their sheep annual premium to protect their sheep flocks.

Those are just small examples of European Union countries that are focused on an area of production that is important to them doing something specific to protect that interest in the period of transition from production-based subsidies to the decoupled, or greener, world that we are moving into. It is important that the decisions that are taken in Scotland are not taken in a blinkered way, without taking into account what farmers in other countries are doing. We have to compete with those people, both in our own market and in other European markets. If we are at a competitive disadvantage, it does not matter how green or socially acceptable the policy and the payments are, we will go out of business. Without businesses being run in the countryside, environmental management becomes more difficult.

Nora Radcliffe: Jim Walker has already answered some of the questions that I was going to ask. However, I would like the panel's opinion on a question that has not been raised so far. Is there sufficient professional advice and data available to farmers to make sensible and informed decisions about their businesses? As Jim Walker has said, there will be a huge and fundamental change and they will have to look at things in a completely different way. Is there a support mechanism to help them to do that?

Jim Walker: There is a huge amount of information out there. One of our main remits at QMS is to provide information, but the difficulty is in providing it in a format that is both understandable and usable by individual businesses. In the main, we are talking about 15,000 to 17,000 small businesses and individuals who work mostly on their own—there are big agribusinesses in Scotland, but they are not in the majority. They need time to understand what the changes mean and to focus on what the marketplace wants from them. If someone is a primary producer of sheepmeat, lambs or store cattle in the north-west Highlands of Scotland, they can feel pretty remote from the marketplace that sells those products for them and from the consumers that buy them.

A priority for us is to ensure that those people at least have access to information that lets them know that what they are doing on their farms will allow them to have a margin in the marketplace that they are selling into. It is a question not just of selling cattle to a finisher in Aberdeenshire, but of whether the guy who is selling the finished animals in Aberdeenshire is working with a processor who has a marketplace that will give him a margin. Unlike the pig industry, which is pretty tight, the red-meat industry has a long supply chain, and there has to be a margin for each person in that chain.

Anything that can be done to facilitate providing such information is helpful. We are setting up three monitor farms, as we call them—one in the north-west, one in the north-east and one in the south—to allow farmers to talk to one another and to help themselves, as happens in New Zealand. It is about farmers talking to farmers. If you lecture them, they will not do it. If you get other farmers to say that something is a good idea, they might do it. Nora Radcliffe is right to say that farmers are confused and nervous about the changes and are not quite sure what to do. That is why we are nervous about any decisions that they might make in isolation, without knowing the big picture.

Fraser Scott: A significant amount of information is out there, which professional advisers can provide. It is important to note that much information has still to be released, such as definitions of good agricultural practice under set-aside regulations and about how we farm our land. A pretty fundamental change will be made to the way in which farmers farm, so it is almost up to farmers to go out there and find the information. In the areas where I work, much advice is available.

John McAllion: I take my two fellow witnesses' word for it that all the advice is out there about how to run a farm business profitably, especially when it is in competition with others in the rest of the United Kingdom and the European Union. I hope that the committee does not fail to take a global perspective and to remember that we are not just talking about successful businesses competing against other successful businesses in France, Germany or elsewhere; there are implications for the developing world.

People here may regard decoupling as a radical step in agricultural reform, but in the developing world, it is seen as a device to allow EU and US representatives to argue in WTO negotiations that they have decoupled subsidy from production while they continue to pay exactly the same subsidies through single farm payments to farm businesses, which allow them to continue to produce for export, to continue export dumping in the developed world at uncompetitive market prices and to undermine farmers elsewhere in the world.

I have one plea to the committee: do not lose that perspective. It is important that Scotland remembers that it is part of one global society. We have responsibilities to the developing world, not just to people who live and work on this island.

Eleanor Scott (Highlands and Islands) (Green): What does the panel understand farmers will receive the single farm payments for?

Jim Walker: The definition that has been used is that the payments are for good agricultural practice, whatever that might mean. I would like such payments to be used by Scottish farms to produce quality food—not just beef, lamb and pork—for a market that exists. We have ample evidence in every sector in Scotland that the quality production in which we are involved is exactly what consumers want, whether from the dairy industry or from the beef, sheep and pig meat industries.

The other aspect is responsible management of the environment. Quality Meat Scotland has undertaken research by asking consumers whether they are comfortable with subsidy payments to farmers. It is surprising that more than 50 per cent of consumers support the payment of EU subsidies to farmers, provided that those farms offer quality food and—interestingly—that families are looked after. Looking after the landscape and the environment is further down the list—that is a given; as farmers, we are expected to do that. We look to the payments not only to allow good agricultural practice to continue and the environment to be managed, but primarily to allow quality food to be produced for a ready market.

In the transition period, as the EU enlarges and budget constraints kick in, there is no question but that support payments—single farm payments or otherwise—will reduce over time and that farmers will have to earn their profit, their margin and their livelihood from a real marketplace. The more the committee, we and anybody else can do to help farmers out there to focus on a real marketplace, the more chance they will have of long-term survival. That is the key for us beyond 1 January 2005. People must ask: what is our market? They should know their market. If they want to sell on the bottom shelf, they will never compete with Brazil. They want to be on the top shelf so that people are prepared to pay more for their goods.

Fraser Scott: I agree with Jim Walker. We must ensure that we do not put in place measures for the responsible management of the environment just because they sound good. If we say that bird scrapes in fields are the thing to do, we must have proof that they work. We do not want ideas to come out from wherever that do not have proof, backing or a definition of what they are trying to do. We need to prove that the initiatives benefit the environment. At the end of the day, farmers will receive payments for their environmental initiatives. We must ensure that what the public want is good for the environment and is not pie in the sky.

11:45

John McAllion: Jim Walker summed up the issue when he talked about the payments being for good farming practice, "whatever that might mean." The problem is that nobody is sure exactly what it means and which cross-compliance standards will be applied. Pillar 2 payments under the CAP amount to only 5 per cent of the total payments under the CAP; 10 per cent national modulation will not change that situation much. The single farm payments, which will make up a large part of payments, will free up farmers to make decisions that are based on market analysis, but they will also be able to carry on as before—farmers will not be required to stop practices that were supported through the previous CAP subsidy systems. We are concerned that nothing much will change and that farmers will carry on exporting to markets in which they can make a profit, which might be damaging to farmers in the developing world.

Fraser Scott: The proof of the pudding will be in the next few years, when farming will change fairly radically and grow to suit the market. I do not believe that farmers will decide to grow an acre of wheat simply because they will receive a payment for doing so. Farmers will grow to suit the market.

John McAllion: For profit.

Fraser Scott: We are all in business to make a profit.

Jim Walker: Support payments are paid to the primary producers who produce raw material, but there is also a huge food industry in Scotland to process the food. Without that raw material, the food processing industry cannot exist. The processing sector supports the Scottish economy to the tune of more than £1.5 billion a year. John McAllion quoted agriculture's contribution to GDP as being 1 per cent. That is correct for the UK, but the figure is more than 3 per cent in Scotland, and in many areas it could be nearer to double figures. I know from the foot-and-mouth outbreak in Dumfries and Galloway that more than 20 per cent of the GDP of the area comes from either food production or food processing. We give that quality food production away at our peril, because the Scottish economy will be the worse if it disappears.

Eleanor Scott: I have a quick follow-up question about the environmental goods that farmers are being asked to deliver. The panel will agree that those are also extremely important to Scotland's economy. We have heard a lot from other panels about land management contracts, and much is expected of them. Do the witnesses have any comments on them? Given that recent farming practices have had a serious effect on the environment in Scotland, according to some environmental groups, will the cross-compliance rules be burdensome on farmers or so loose as to be meaningless?

Fraser Scott: I return to the point that we must prove that environmental practices are beneficial to the environment. I do not understand the land management contracts—perhaps another witness can comment on them—but we must ensure that environmental measures are good for the environment. Many measures that farmers take today are good for the environment. If certain actions are to be specified for payments to be received, we must ensure that those actions are good for the environment and for Scottish agriculture.

John McAllion: In principle, we support land management contracts and cross-compliance standards. In principle, it is a good idea to involve farmers in how the land is preserved and looked after. The problem is that we are not convinced that that is likely to happen. The decision to base the single farm payments on historical production will reward large-scale, capital-intensive farming, which damages the environment. The Executive seems to be doing two contradictory things: it speaks about land management contracts that will encourage farmers to look after and preserve the environment, but at the same time it rewards them for farming practice that damages the environment. The two approaches are contradictory, so we are not entirely convinced that what is promised in the fine words about land management contracts will be delivered in reality.

Jim Walker: I was part of the group that was involved in the forward strategy and I was one of the authors of the report, "Custodians of Change: Report of Agriculture and Environment Working Group", which sets out the environmental policy for Scottish farming. I was also there—believe it or not—at the conception of land management contracts. The contracts are a good idea, because they will pull together a plan for the whole farm that encompasses food production, environmental management and diversification, bringing those matters under one umbrella. Such an approach makes things much easier to manage; it enables us to take an holistic view of a farm and to decide what is best for that particular unit, rather than require a farm to comply with various aspects of an individual scheme that might not be suitable for it. The plan could be tailor-made: we would want to produce the biggest volume of crop from the best arable land in Scotland, whereas poorer land or land that lends itself to increased environmental management could be managed appropriately.

I gave this example when the idea of land management contracts was being considered. Although we spend a huge amount of money in Scotland on environmental improvement—currently, £130 million is spent in pillar 2 payments on LFA support, forestry and environmental management—much of that improvement is never seen by the general public, because it does not happen near Edinburgh, Glasgow, Aberdeen or wherever; it happens on the tops of mountains and hills around Scotland and only the enthusiasts ever see it. It would be much better if we could use some of that money, through land management contracts, to develop walks between Edinburgh and Haddington, for example, or around farmland that is not as productive as other land, or on other little ideas that would give access to the general public, so that they could see the benefits that they get from their contribution to agriculture.

The idea of land management contracts is that there should be a base payment—a tier 1 payment—an additional payment for people who are prepared to do things a bit differently and a bit better, and a tier 3 payment for very special sites, such as sites of special scientific interest or sites of niche production in Scotland. There would be ways of tailoring a land management contract to the individual needs of a farm.

The current regulations contain no delivery mechanism for land management contracts. The committee and the minister—whoever he or she might be in 2006—will have to argue with the European Commission about that. Land management contracts are a good idea. Farmers want to be involved in them and I am sure that the committee does too, but a hell of a lot of work remains to be done to ensure that the EU allows flexibility and subsidiarity for Scotland—as it has done to a limited extent in the context of the CAP reform package—and to ensure that the rural development regulations are tailor-made for Scotland's needs. I suspect that that will have to be a priority for the committee during the next couple of years.

The Convener: I will wind up now. Nearly all committee members demanded an extra go at the end, so I will be brutally fair to all of you and let no one back in.

I thank the three panellists. We have had stimulating conversations and what we have discussed certainly builds on what we have done in the past. Given that we considered the consumer angle this morning, I was fascinated that our largest-growing market, organics, and what we might want as consumers was not picked up by anyone, but I will leave that sticking to the wall.

Jim Walker mentioned access issues. Colleagues might want to have a look at the submissions on access that we received in the most recent round of submissions to the committee, before we hear from the Deputy Minister for Environment and Rural Development, who will be the next witness in our CAP reform inquiry.

Before I suspend the meeting for a couple of minutes to allow the witnesses to move, I ask the committee's permission to change the running order of the meeting. We are supposed to be considering the renewable energy inquiry next, followed by subordinate legislation and then item 4, on the Water Environment and Water Services (Scotland) Act 2003. I want to move item 4 up the agenda and consider it next, because we are running about half an hour later than we anticipated. We will restructure the agenda thereafter. Is that acceptable to members?

Members *indicated agreement*.

11:54

Meeting suspended.

11:59

On resuming—

Water Environment and Water Services (Scotland) Act 2003: Annual Report to Parliament 2003

The Deputy Convener (Eleanor Scott): Sarah Boyack has had to rush off, which is why I am in the chair. I do not know whether she will manage to get back, but we will carry on anyway.

We move to consideration of the Water Environment and Water Services (Scotland) Act 2003 and the annual report to Parliament. I welcome to the committee Allan Wilson MSP, the Deputy Minister for Environment and Rural Development, and his officials.

Members may recall that during consideration of the Water Environment and Water Services (Scotland) Bill, the Parliament agreed to an amendment requiring Scottish ministers to prepare an annual report. The report summarises action taken during the year to comply with the requirements of the European water framework directive. Today we have the 2003 annual report before us—the first such report to be produced under the new requirement. I thank the minister for providing the committee with advance copies.

Minister, would you like to make any opening remarks?

12:00

The Deputy Minister for Environment and Rural Development (Allan Wilson): I am pleased to be here to present the committee with the first annual report on the implementation of the water framework directive in Scotland. As at least some committee members will know, the submission of an annual report to Parliament was a provision that was agreed to during the process that led to the passing of the Water Environment and Water Services (Scotland) Act 2003. The report highlights the considerable progress that has been made since the passing of that act a year ago. It focuses on achievements during 2003 and touches on key issues for 2004.

The Deputy Convener: I invite questions from members.

Maureen Macmillan: What progress has been made on flood management? Do current schemes take the Water Environment and Water Services (Scotland) Act 2003 into account? In Moray, significant schemes are being prepared and concerns have been raised that they are not being prepared in the spirit of the act. Will you comment on that—without focusing on particular schemes unless you feel that that is appropriate?

Allan Wilson: I understand the point that Maureen Macmillan makes and obviously I do not want to comment on the flood alleviation proposals in Moray. We have set up a national advisory committee to consider various issues pertaining to sustainable flood management. I have met members of that committee, and their priorities are to produce a definition of sustainable flood management—surprisingly enough—that is appropriate for Scotland, and to produce guidance for local authorities, which will be responsible for implementing sustainable flood management. The committee will report to ministers in December and a consultation paper will be issued subsequently.

Maureen Macmillan: I just wanted some reassurance that, where flood management proposals are being worked up, cognisance is being taken of what might be announced in December. I would not like flood management proposals to be tabled if there had been no consideration of sustainability—not that I am saying that that is going to happen.

Allan Wilson: I would be very surprised if that were to happen; I have no knowledge of it happening anywhere. Obviously, the process of designating responsible bodies for flood management is under way. It is no secret that local authorities will be so designated and I do not imagine that any local authorities are not aware of the duties that will be imposed on them as responsible bodies for the furtherance of sustainable flood management.

Maureen Macmillan: Some environmental non-governmental organisations have criticised the proposals for flood prevention.

Allan Wilson: We would have to consider the individual plans to see whether the proposals satisfied the approved definition of sustainable flood management, when we have that definition. Different people may have different views on what constitutes sustainable flood management. We have yet to agree a definition.

Maureen Macmillan: I can see that we are going to go round in a circle, so I will desist.

Nora Radcliffe: What a pleasure it is to be dealing with European legislation on the front foot and not on the back foot. I appreciate having an annual report so that we can check on progress and see where we are going.

I have a series of questions, which I will ask individually, rather than in a block.

Characterisation is one of the fundamental ways to benchmark. Could you comment on characterisation, particularly that of wetlands, coastal waters up to 3 nautical miles and private water supplies? Those all extend the scope of the water framework directive and are important.

Allan Wilson: I will deal with wetlands first. We have been making considerable progress on the inclusion of wetlands in the provisions of the 2003 act. SEPA has been working in conjunction with Scottish Natural Heritage and environmental NGOs on a strategy to ensure that all such provisions are fulfilled. The Executive proposes to provide SEPA with extra funding for further research on the protection of wetlands. Further, in the Executive's consultation paper on the regulation of controlled activities, we propose to extend the protection of wetlands to include abstraction and building and engineering works.

As I said, considerable progress has been made and we are ahead of the game. It is a pleasure to be in that situation in respect of the implementation of the water framework directive and its subsequent processes. As Nora Radcliffe pointed out, that is not always the situation.

On characterisation more generally, significant progress has been made on identifying water bodies and producing a draft risk analysis. SEPA aims to issue a consultation paper on the results of the risk analysis in July, and so is on target to meet the 2004 EU deadline. As far as I am aware, there are no problems in prospect on that front.

Nora Radcliffe: On private water supplies, we are talking about abstraction licensing for small private abstractions. Will that go right down to very small, private water supplies that serve a handful of houses, or will such licensing come later?

Allan Wilson: I do not know.

Joyce Carr (Scottish Executive Environment and Rural Affairs Department): That issue will be raised in the consultation paper that we are about to issue. There are different tiers of authorisation, depending on the perceived risk to the water environment. At very low levels of risk, registration might be required merely to inform SEPA where the various private water supplies are located, principally with a view to enabling them to be better protected.

Nora Radcliffe: There is a huge issue in the north-east in particular, where we have a vast number of private water supplies, not all of which are known about.

We come now to Eurospeak and typology. Can we see an example of a typological report, so that we can understand what it is about? I understand what it is for, but I would like to see a real one, to see whether it would inform my understanding.

Joyce Carr: SEPA will have such reports. I am sure that I can get examples sent to the committee.

Nora Radcliffe: That would be helpful. We know what such reports are for, but seeing a real one would be helpful.

You have answered my question on resources by saying that SEPA is getting more resources.

Allan Wilson: I do not want you to run away with the impression that there is an unlimited supply of Executive cash out there simply waiting to be expended, because that is not the situation. As you probably know, we are reviewing expenditure on all our services as part of the budgetary review. We are not able to splash resources about willy-nilly. I hope that the committee will appreciate the fact that we have been able to secure extra resources for additional wetlands protection, given the discussions that we had this time last year.

Nora Radcliffe: That point is well made.

Will we get more information about developing pressure-specific biological classification tools, so that we can understand that area better?

Allan Wilson: I will request more information.

Joyce Carr: SEPA will be working on that during coming years. Work is in hand, but we are at only the early stages.

Nora Radcliffe: Thank you again. It is a pleasure to be ahead of the game.

Allan Wilson: It is indeed.

Rob Gibson: I am keen to discuss planning permission for fish farming. Are you content with the progress that is being made towards democratisation? After this first year of the implementation of the directive, given concerns about fish farming, are we moving rapidly enough towards having more democratic control?

Allan Wilson: We are certainly moving much more rapidly than we were this time last year. I appreciate that you were not a member of the Parliament then, but—

Rob Gibson: I was a member of the public and was listening to the producers.

Allan Wilson: I was not trying to be disparaging in any way. Your seat was obviously occupied by someone else.

As a consequence of pressure from Maureen Macmillan, the good lady sitting next to you, and from the previous Rural Development Committee, we were able to push forward the issue of incorporating aquacultural planning in land planning arrangements, which I supported as the deputy minister responsible for the aquaculture industry. That was quite difficult, as we did that against the advice of planning officials in the Development Department at the time, but we can take joint credit for it. That is important because there was consensus in the aquaculture industry —and among those representing wild-fish interests and, crucially, local authorities—that we were taking the right and logical step. Obviously, what we propose cannot happen overnight and there is a requirement to ensure that everyone with an interest has their say in the process.

I believe firmly that improving the ecological and chemical status of our raw water resource—increasing the purity of the supply and generally having a better water environment—is good for the aquaculture industry, as it is for other industries such as the whisky industry, as it adds value to their products. I understand that there are concerns about the costs of the proposals to businesses, which must have their eye on the bottom line; however, in general, improving our water environment and, more specifically, water quality is good for those businesses.

Rob Gibson: We all wish that to be the case and we underline your faith that the process will improve our aquaculture industry.

Alex Johnstone: The minister might be surprised to hear that I was going to ask about planning permission for fish farms as well, and that I planned to commend him for demonstrating considerable caution. I notice that the report says that a consultation exercise will take place in advance of the publication of legislation in 2005. That concerns me, because when there is consultation on such issues the Executive usually keeps a comfortable distance from influencing how it runs. Would not it have been more advantageous in this case if the Executive had put itself in a position in which it could send out clear signals to ensure that the industry could, in the interim, develop in a way that would be conducive to the eventual legislation that will be introduced?

12:15

Allan Wilson: We have issued revised locational guidelines, which I think perform such a function in the interim. As you know, the Crown Estates commission effectively devolved its rights of planning de facto to planning authorities—at least, it did that so that planning can be done in consultation with terrestrial planning authorities. Processes were and are under way that address some of those concerns. Obviously, it will be better once everything has been properly consulted on, approved and implemented. We are working as quickly as Government processes allow.

Alex Johnstone: You have said that a consultation will take place, but are you confident that the Executive has given an adequate steer that will protect the industry from any radical decisions that might emerge from an open-ended consultation?

Allan Wilson: I am not sure what you have in mind, but obviously we do not want to prejudice the outcome of the consultation by trying to predict its ultimate shape. I am talking about what we do in the interim to ensure that the industry and local interests can co-exist; I am sure that they can co-exist.

Karen Gillon: I am interested in the progress that has been made in relation to regulations on diffuse pollution and the likely timescales for those.

Allan Wilson: We have, of course, made considerable progress more generally in the area of the regulation of controlled activities since 2003. A consultation paper is scheduled to be issued in April 2004, which is next month. The regulations will cover point-source pollution, abstraction and impoundment and building and engineering works in or in the vicinity of a water body.

Diffuse pollution is not included in the proposed set of regulations. There will be three tiers of control—registration, registration under general binding rule and, of course, licensing—but diffuse pollution has not been included because we wanted to wait for the outcome of the CAP reform process. A working group will then be set up to discuss the appropriate way forward over the coming months. As I said, there will be a consultation paper in April on other forms of pollution, such as point-source pollution, but not on diffuse pollution. However, we intend to add it to the list. We have also been carrying out a scoping study to identify the activities that need to be controlled and which can be controlled proportionately. The working group will want to progress such discussions.

Karen Gillon: Therefore, can I assume that there is a medium-term timescale rather than a short-term timescale, given the potential work that is involved?

Allan Wilson: We are talking about a period of months. As I said, the consultation paper is scheduled to be issued next month and a working group will be established over the next few months that will specifically consider diffuse pollution. Such pollution is not included only because of the CAP reform discussions.

Nora Radcliffe: I forgot about another issue that I wanted to raise. The report is the first such annual report. We are still at the high-level stage on all the preliminary work that must be done on characterisation, typology and so on. Are you thinking about the stage at which we will involve people in sub-river basin management and planning? How soon will we come down to levels in which there is local involvement, which we thought would be a strength of our approach to the water framework directive?

Allan Wilson: To a certain extent, that is already under way. Last year, SEPA carried out a roadshow to discuss river basin management with interested stakeholders. As you know, the stakeholder forum, which encompasses everybody who has an interest and a few more besides, is having meetings and there are bilaterals between SEPA and individual stakeholders across the board. There is no doubt that that work includes the Convention of Scottish Local Authorities, the Scottish Landowners Federation, Scottish Water, the clean coast Scotland campaign and other bodies that are involved with SEPA in taking forward river basin management planning and—as I said earlier to Maureen Macmillan—defining the responsible bodies, not that there is a statutory link between the two issues.

Nora Radcliffe: I presume that when risk assessments have been done, the particular water catchment areas that are most at risk and on which the most work needs to be done will be defined as sub-river basins for management purposes.

Allan Wilson: I understand that SEPA plans to issue a consultation paper in the spring—that will be fairly soon, given that I see the crocuses sprouting—on that specific issue.

Karen Gillon: I am interested in how you see the matter integrating with other Government priorities, particularly the biodiversity strategy. How will they work together, pull together and have a sustainable future together?

Allan Wilson: There are clear and obvious links between them. I mentioned wetlands, which have important implications for the preservation and conservation of species. A lot of that work is done interdepartmentally as well as between the relevant agencies. As I said, the national stakeholder forum comprises everybody that you might expect to be involved in the development and implementation of the biodiversity strategy. I would expect officials to be speaking to one another about those matters. Perhaps Joyce Carr will confirm that.

Joyce Carr: Scottish Natural Heritage is involved in a lot of our working groups and it will be designated as a responsible authority, so it will be required to have those links.

The Deputy Convener: I have a question on the no deterioration in status obligation—I have trouble saying that—in the water framework directive. What progress has been made to implement that obligation? Will its implementation be tied up with the publication of the final characterisation report in December?

Allan Wilson: Neither the water framework directive nor the 2003 act defines when that policy will come into force, but we believe that it is appropriate to take the characterisation report that is due in December as a baseline for it. Therefore, it is proposed that SEPA will regulate on that basis from the introduction of the controlled activities regime in October 2005. However, that policy will apply only to new activities and it is also proposed that existing activities will be regulated on the basis of the status quo until 2012. Those proposals and others like them will be set out in the consultation paper on characterisation that we will issue in April.

The Deputy Convener: As there are no further questions, I thank the minister and his officials.

Renewable Energy Inquiry

12:23

The Deputy Convener: The next agenda item is on renewable energy in Scotland. I hand over to Tracey Hawe, who will give the convener's feedback.

Tracey Hawe (Clerk): Members will probably be aware that the convener attended the Enterprise and Culture Committee's meeting on renewable energy yesterday. She told me that she intends to redraft the paper that the Environment and Rural Development Committee considered previously and to pass the paper back to members for their comments before it is submitted to the Enterprise and Culture Committee as part of that committee's inquiry.

Are members content with that approach?

Members *indicated agreement*.

Subordinate Legislation

Rural Stewardship Scheme (Scotland) Amendment Regulations 2004 (SSI 2004/109)

Tribunals and Inquiries (Dairy Produce Quota Tribunal) (Scotland) Order 2004 (SSI 2004/119)

Less Favoured Area Support Scheme (Scotland) Amendment Regulations 2004 (SSI 2004/128)

12:24

The Deputy Convener: Under the next agenda item, we have three statutory instruments to consider under the negative procedure. The Subordinate Legislation Committee has considered all three instruments but has commented only on the Rural Stewardship Scheme (Scotland) Amendment Regulations 2004 (SSI 2004/109). An extract of the committee's report has been circulated. Do members have any comments on the instruments?

Members: No.

The Deputy Convener: Excellent. Are members therefore content with them and happy to make no recommendations to the Parliament?

Members *indicated agreement*.

The Deputy Convener: Thank goodness for that.

Annual Report

12:25

The Deputy Convener: The last item on today's agenda is consideration of the committee's annual report for 2003-04. A copy of the draft report has been circulated, but members are asked to note that as our reporting year runs from 7 May 2003 to 6 May 2004, the report may require to be updated to reflect any additional work in progress up to and including our meeting on 5 May 2004.

Rob Gibson: I thought that the report's predictive content was very interesting. It is clear that you know what we are doing, so at least that is useful.

The Deputy Convener: I should remind members that the format of the annual report has already been approved by the Conveners Group and that there are limits on its length and content. I invite comments from members.

Alex Johnstone: I am just glad that there are limits on the length and content.

Nora Radcliffe: I will be more positive and say that the draft report was highly succinct.

The Deputy Convener: Is everyone happy with the draft annual report?

Karen Gillon: It is an accurate reflection of the work that we have undertaken.

The Deputy Convener: The next meeting will be on the morning of Wednesday 21 April. It will include an evidence session with the deputy minister that will cover both the budget process and CAP reform. We will also deal with petitions and have an update on European issues.

Meeting closed at 12:27.

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