



National Audit Office

**REPORT BY THE
COMPTROLLER AND
AUDITOR GENERAL**

**HC 513
SESSION 2009–2010**

31 MARCH 2010

Defra's organic agri-environment scheme

Summary

Agri-environment schemes

1 Farmers who join agri-environment schemes receive annual payments in return for managing their land in ways that will protect or enhance the natural environment or historic landscape. The Government has set aside £1.7 billion of EU funding and an estimated £1.2 billion of UK matched funding for agri-environment schemes in England. The schemes are due to finish in 2013 and EU funds, including those voluntarily reallocated from money that would otherwise have been paid to farmers through the single payment scheme, need to be used by the end of 2015 or the money cannot be claimed from the European Commission.

2 Agri-environment schemes are the main part of the Rural Development Programme for England. The schemes are overseen by the Department for Environment, Food and Rural Affairs (the Department) and administered by Natural England, a Non-Departmental Public Body. The Rural Payments Agency makes payments and carries out compliance inspections.

3 There are three agri-environment schemes open to new applicants, with a combined budget of £2.1 billion over seven years up to 2013-14. The Organic Entry Level Stewardship scheme (the Scheme) is typical of English agri-environment schemes in that it pays farmers to implement and maintain environmental land management measures over a five-year agreement. It is also intended to secure further environmental benefits by supporting organic farming. We focus in this report on the Organic Entry Level Stewardship scheme, but many of the lessons learned are likely to be applicable to the Entry Level Stewardship scheme for conventional farmers. Principles of sound financial management have wider application.

4 Natural England forecast as at March 2010 that the Organic Entry Level Stewardship scheme would make £197.7 million total payments to farmers over the period 2007-08 to 2013-14, made up of the following elements:

- £30 per hectare per year to reflect the cost of maintaining organic certification.
- £30 per hectare per year to compensate for the cost of implementing environmental management measures. Some examples include hedgerow management, putting in place measures to preserve biodiversity or conserve species, and protecting archaeological features or historic buildings.
- Farmers converting their land to organic farming methods are entitled to claim a further £175 per hectare per year 'conversion aid' for the first two years (or £600 per hectare per year for three years for farmers growing top fruit such as apples, plums or pears). Conversion aid is intended to help offset the transitional costs of changing from conventional to organic farming.

5 The policy justification for spending UK taxpayers' money on top of EU funding is to achieve environmental benefits over and above the requirements of the single payment scheme to maintain land in good agricultural and environmental condition. We considered three key risks to value for money:

- **The utilisation of EU funds.** The European Commission will retain any funds not used by the 2015 deadline.
- **Achievement of environmental benefits.** We examined what benefits the Scheme is achieving by encouraging farmers to adopt organic farming methods, and how far it has led to improvements in land management.
- **The quality and efficiency of Scheme administration.** We considered the accuracy and timeliness of payments to farmers, and the reasonableness of Scheme administration costs.

Our findings

On utilising available EU funds

6 The Department's forecast for expenditure of EU funds on the Scheme assumes constant take-up each year, but our analysis is that this may prove over-optimistic. Natural England and the Department monitor ongoing expenditure, especially of UK Exchequer funds, very closely. Monitoring of EU funds has, up until December 2009, not been undertaken in such detail. Natural England estimated in July 2009 that expenditure would total £176.3 million over the life of the Scheme. Natural England has subsequently revised its estimate and in March 2010 forecast that total spend would be £197.7 million. This change results from an upward revision in forecast take-up, from 20,000 hectares each year to 22,600 hectares each year up to December 2013. We found that there has been a tailing off in applications for the Scheme. Taking account of this information in our analysis of Natural England's data for spend to date available at the time of our audit, our statistical projection of trends indicated that take-up would total between £159.2 million and £160.4 million, assuming that 90 per cent of farmers would renew agreements due to end during that period. This would mean that all the EU funds made available for the scheme may not be claimed.

7 The Scheme best supports farming sectors that already have a strong organic contingent, and the pattern of Scheme take-up reflects adoption of organic farming methods in the industry as a whole. Market prices can be expected to be a greater influence on the viability of farming businesses than support payments. The Scheme nonetheless benefits larger farms, especially in the beef and dairy sectors, more than smaller farms. Farming experts regard conversion aid as the most important component of the Scheme, as it supports farmers through the costly process of converting to organic farming. This support has had a marked positive impact in the beef, sheep, dairy and arable sectors, but is less helpful in more land intensive sectors, such as pigs and poultry. The higher rate of conversion aid for top

fruit, such as apples and pears, does not cover typical additional net costs experienced during the conversion period but is more than needed to compensate for the costs of converting to organic farming taking the five-year agreement as a whole. In the long term, the additional payments for organic certification are sufficient to tip the balance for dairy farmers between losing and gaining money per hectare as a result of converting to organic farming. Payments typically have least financial benefit for soft fruit and poultry farmers, and those with smaller farms, among whom take-up has been low.

8 The Department and Natural England did not build contingencies into original planning but in response to year on year monitoring have started to take steps to address the potential under-utilisation of EU funds. The Department can divert under-used funds from one agri-environment scheme in the Programme to another. In June 2009 the Department had reported an underspend to date of over £420 million in the Programme which means, however, that there is limited capacity to rely solely on this option to absorb unused funds. This was in part due to exchange rate movements which made available additional funds. In addition, however, exchange rate movements mean that the UK contribution needed to utilise all the EU funding for the Scheme may be some £20 million higher than the Department originally anticipated. In 2009 the Department started informal discussion with the European Commission with a view to changing the co-financing rate, so as to increase the proportion of payments to farmers reimbursed from European funds. The Department has not yet submitted a formal proposal and the outcome of this approach has yet to be determined. Starting in 2010 Natural England plans to administer a £14 million programme using funds drawn from the Rural Development Programme for England between 2010 and 2013 to provide training and information for farmers. The initiative has broad aims and extends beyond Organic Entry Level Stewardship, but will seek to encourage farmers to renew their agreements and to take up the most suitable environmental options. It will also promote the Scheme to likely new entrants. Natural England has not yet developed a method for evaluating the success of the new training and information programme.

On environmental impact

9 To the extent that it has encouraged adoption of organic farming the Scheme has contributed to achievement of environmental benefits, but the Department cannot quantify the impact of the Scheme in securing these environmental benefits. Research indicates that organic farming delivers environmental benefits, and in particular has been shown to have benefits for biodiversity. The nature and quality of environmental benefits can nevertheless vary by farming sector, and will differ according to the farming practices used. The Department has insufficient research evidence to quantify the extent to which the Scheme has contributed to achieving benefits of this kind, or how the impact may vary between farming sectors.

10 The money paid to farmers for adopting management measures should have had more demonstrable environmental impact over and above the benefits secured from organic farming. Some 72 per cent of farmers in the Scheme believe the Scheme has had a positive environmental impact, but do not distinguish between benefits from organic farming or from additional management measures. Many of the Scheme's management options are designed to be easy to implement, with minimal impact on farmers' businesses, so as to encourage farmers to join. We found that 57 per cent of farmers chose some measures that involve managing features already in place on their farm. Many of the more challenging options are rarely implemented. In 2006 the Department had recognised from piloting the Scheme that there was likely to be an element of deadweight in this way, and that 90 per cent of options chosen under the Scheme would continue under Environmental Stewardship guidelines if farmers left the Scheme. The Department made subsequent changes to the environmental management options available under the Scheme, but the majority of agreements nonetheless still focus on a very narrow range of measures. Part of the training and information programme which Natural England will introduce in 2010 will be aimed at encouraging farmers to adopt a wider range of management options most appropriate to the local environment.

11 Securing environmental benefits depends on Natural England ensuring that farmers maintain Scheme obligations throughout a five-year agreement. Inspection cases are selected by the Rural Payments Agency based partly on risk criteria, with the remainder chosen at random. Our review confirmed that the proportion of Scheme beneficiaries failing inspections and triggering payment recoveries was higher in the risk-based sample than in the random sample, suggesting that the risk criteria used had been successful in identifying cases most likely to be in breach of Scheme requirements. However, the risk factors applied should continue to be kept under review.

12 Inspections could be tightened up to give Natural England stronger evidence that all the land entered into the Scheme continues to be registered as organic for the duration of the agreement. Because of changes to field boundaries, it is common for there to be discrepancies between the land registered as organic at the start of the agreement and amounts subsequently claimed. We found that Rural Payments Agency Inspectors had not always documented evidence that they had examined a farmer's certificate of organic registration, or that they had reconciled the land parcels listed on the certificate to those claimed for under the Scheme.

On scheme administration

13 Estimated administration costs per claim have reduced over the past four years and are lower than those for the single payment scheme, but IT costs remain high. Natural England does not separately account for the costs of administering Organic Entry Level Stewardship, distinct from the rest of the Environmental Stewardship scheme, and did not have a robust estimate at the outset of the likely administrative costs of the organic Scheme. We estimate, however, that processing the Scheme cost an average of £637 per claim in 2008-09, of which 84 per cent relates to IT costs recharged to Natural England by the Department. As a comparator, we estimated the cost of administering the single payment scheme in 2008-09 to be £1,743 per claim.

14 Farmers are satisfied with the quality of service Natural England provides.

Natural England has considerably reduced the time taken to process Scheme applications and make payments. It has centralised processing in one regional office and has an ongoing programme of efficiency measures. Farmers we surveyed do not see administrative burdens as a barrier to take-up, and although some applicants thought the process could be simplified, only 6 per cent of farmers were dissatisfied with the service they received from Natural England.

Value for money conclusion

15 The Department and Natural England have not optimised the value for money achieved from the EU funding available for the Scheme. Over-optimistic and simplistic straight-line forecasts of take-up, and an inability to make up the shortfall quickly present a risk that EU funds will not all be utilised. The Department is spending more to engage with farmers, but in view of probable high renewal rates we are not convinced that this will necessarily have much impact on Scheme take-up. The Scheme may have delivered some environmental benefits, particularly from organic farming practices, but the Department is unable to quantify these and many farmers appear to have been paid for activities they were previously undertaking. On a more positive note, farmers are satisfied with the quality of service provided by Natural England. The processing cost per claim has been substantially reduced, but IT costs do still remain high.

Recommendations

16 The issues raised in this report centre around the importance of more sophisticated financial management and a stronger evidence base against which to assess performance. We have raised these issues previously on other areas of the Department, such as its management of the Rural Payments Agency and the Business Waste Programme. The Department will need to strengthen staff skills in these areas if it is to learn lessons from these reports and avoid the need for us to raise these points again in future.

17 On the Organic Entry Level Stewardship scheme, we recommend:

a To improve the take-up and the effective use of funds:

- This report highlights concerns about the Department's forecasting, planning and monitoring of substantial projects similar to issues we have raised in previous reports on the Department. The Department should apply a robust framework for methodical scrutiny and challenge of plans and budgets to all its projects; consider the impact of a range of potential outcomes in terms of cost and impact on scheme objectives; put in place from the outset arrangements for monitoring and evaluation; establish contingency plans up front; and set trigger points for implementing them in the event performance falls short of forecast (see paragraph 6).
- The Department should review conversion aid rates, based on a robust analysis of current market conditions in each agricultural sector (see paragraph 7).

- Natural England should specify what impact it expects the training and information initiative to have on Scheme take-up, and on the range of management options adopted. It should consider how it might be used in conjunction with promotional interventions to encourage take-up of a wider range of management prescriptions in a variety of farming sectors, and should put in place measures to evaluate the impact of the initiative in an objective way (see paragraph 8).
- b To improve the environmental impact of the Scheme:**
- The Department should explore whether, for future schemes, the onus could be put on farmers to demonstrate the environmental benefits delivered by their agreements (see paragraphs 9-10).
 - The Rural Payments Agency should remind Inspectors of the need to reconcile land parcels listed on farmers' certificates of organic registration to land parcels on their Scheme agreement. Natural England should robustly challenge inspection documentation received from the Rural Payments Agency in which inadequate evidence of organic certification is provided (see paragraph 12).
- c To improve the cost-efficiency and effectiveness of Scheme administration:**
- To be able to test the value for money of the Scheme, benchmark the efficiency of Scheme administration against other initiatives, and look for further efficiencies, Natural England should measure the cost of administering Organic Entry Level Stewardship distinct from Entry Level Stewardship and the rest of the Rural Development Programme for England (see paragraph 13).