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**Environmental Conditionality on
Direct Payments to Land Managers**

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Preface

- Andrew Moxey (Pareto Consulting), Davy McCracken (SRUC) and Steven Thomson (SRUC) were commissioned (see Appendix 1 for outline remit) by the Scottish Government to draft a conceptual paper on the potential use of direct payments with enhanced conditionality in order to achieve environmental policy objectives, as part of post-2024 rural support.
- This version of that paper has been edited to reflect feedback received from a group of Scottish Government and Agency Officials. Whilst there was broad agreement amongst feedback that enhanced environmental conditionality merits further consideration, views differed on both the relative reliance that should be placed on conditionality within a mix of policy instruments and the specifics of how conditionality could be framed and implemented. As such, the paper identifies points for further discussion, which would need to be addressed as a next step in taking forward this work.

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Purpose

1. The purpose of this document is to scope out whether it may be feasible to improve delivery of environmental outcomes - in line with Scotland's strategic goals for the environment and climate change - through increasing the environmental conditions associated with any future direct payments made to farmers and other land managers.
2. As enhanced environmental conditionality of direct payments is only one potential aspect of future agricultural and environmental support, it is important that this 'conditionality' concept is not considered in isolation. Rather, it must be seen as **part of a wider package** of support that delivers social, economic and environmental outcomes from the land-based sector (including 'rural development' measures such as agri-environment and forestry schemes).
3. The global climate and nature crises **require a radical change in approach** to the way we manage and use our land. The design of future rural support will have an important influence on the delivery of Scotland's climate change and environment targets, including the vision and outcomes of Scotland's Environment Strategy¹. It is widely acknowledged that the current support system under the CAP has not been effective in delivering the intended improvements in environmental performance. There is a **significant opportunity** to design a future payment system that supports farmers and other land managers to transition to ways of working that make their business more environmentally sustainable while also helping to drive innovation, efficiency, productivity and competitiveness. Additionally, the design of future rural support presents important opportunities to promote **a more integrated approach** towards achieving policy goals across different land use sectors, beyond agriculture – including forestry, deer management and sporting estates.
4. To achieve the transformative changes required, a key challenge will be to simultaneously deliver against multiple economic, social and environmental outcomes (relating to, for example, rural livelihoods, food security, reducing negative environmental externalities and increasing positive externalities) **whilst minimising necessary transitional disruption** within budget, administrative capacity and trade (i.e. WTO) constraints. Including **tighter environmental conditionality** on the existing system of area payments as part of the policy mix may offer a more effective approach for delivering these multiple outcomes than an abrupt switch to alternatives would² – provided that the conditions adopted are:
 - **sufficiently ambitious** to support the scale of transformative change required;
 - accompanied by other more **targeted measures**, including a well-funded and designed agri-environment scheme; and
 - supported, where appropriate, by **planning and advice** to help ensure effective delivery of intended outcomes³.

¹ <https://www.gov.scot/publications/environment-strategy-scotland-vision-outcomes/>

² Any economic analysis of alternative policy options would need to account for the balance between multiple policy outcomes, for uncertainties in the likelihood of achieving any or all desired policy outcomes, and for different levels of disruption along different transitional pathways.

³ The evidence from greening and other approaches shows that having a well-informed and planned approach to implementing environmental management on land is essential if it is to produce the desired results, i.e. the right management in the right place is required in order to achieve the desired environmental outcome. In order for that to happen effectively, a plan or audit coupled with appropriate advice is an essential building block.

5. The brief was to provide **some initial considerations** as to whether - or not - such an approach could be feasible in practice, and if so, what broad range of factors would need to be considered further when investigating the practicalities involved. Hence, it is recognised that additional more detailed discussions would need to take place if the pros and cons of taking such an approach were to be considered in more detail. For example, further analysis would be required to assess the **scale** of contribution required from environmental conditionality to meeting climate, biodiversity and other environmental targets – and to test whether proposals are sufficient to achieve this.
6. The brief provided by Scottish Government for this scoping exercise (see Appendix 1) highlighted that the primary focus of any enhanced environmental conditions on direct payments should be to help promote the land uses changes needed to achieve the outcomes of Scotland’s Environment Strategy, including meeting our statutory climate change goals:
 - Scotland's **nature** is protected and restored with flourishing biodiversity and clean and healthy air, water, seas and soils;
 - We play our full role in tackling the global **climate** emergency and limiting temperature rise to 1.5°C;
 - We use and re-use **resources** wisely and have ended the throw-away culture;
 - Our thriving, sustainable **economy** conserves and grows our natural assets;
 - Our healthy environment supports a fairer, healthier, more inclusive **society**;
 - We are **responsible global citizens** with a sustainable international footprint.
7. This scoping exercise also recognised that any enhanced environmental conditionality could not be the only means by which those environmental outcomes are achieved. A **wider package of targeted measures**, including well-funded agri-environment support and encouragement for nascent private markets in environmental services, would be required to fully deliver the Scottish Government’s environmental ambitions and the scale of the environmental outcomes required.
8. However, consideration of that wider package of measures falls outwith the remit provided for this particular document. Nevertheless, it will be essential to know the wider context within which environmental conditionality on direct payment sits if that approach is to be investigated any further after this initial scoping exercise.

Background Context

9. Traditionally, provisioning ecosystem services (e.g. food and timber production) have been prioritised over other services associated with rural land, including carbon sequestration, flood regulation, regulation of air and water quality, and cultural services relating to people’s enjoyment of the landscape and wildlife. However, there is increasing recognition that **a more balanced mix is required for sustainable development and wellbeing**, and that this may require trade-offs between different services, or at least changes to how traditional provisioning services are managed⁴. This is not, and should not be interpreted as, abandoning food production, but is about being open to changes in the mix, location and management of food production necessary to achieve a better balance across a wider range of ecosystem services. Within bounds, many ecosystem services can be generated jointly,

⁴ The 2019 global assessment by the Intergovernmental Science-Policy Platform on Biodiversity and Ecosystem Services (IPBES) concluded that ‘The great expansion in the production of food, feed, fibre and bioenergy has occurred at the cost of many other contributions of nature to quality of life, including regulation of air and water quality, climate regulation and habitat provision.’ https://ipbes.net/sites/default/files/2020-02/ipbes_global_assessment_report_summary_for_policymakers_en.pdf

but **beyond certain thresholds increasing one service leads to reductions in others**. There is also significant potential for **synergies** through careful stewardship. For example, food production depends on the continued flow of a wide range of ecosystem services, and many measures to protect and restore ecosystem health will also improve the long-term resilience and productivity of farming systems.

10. The range of ecosystem services that can potentially be derived from land is wide and varied, with the level and mix generated by a given parcel of land dependent jointly on its **biophysical characteristics** (e.g. soil, topography, climate) and **on how it is used** (e.g. land cover plus types and intensity of activities).
11. For example, a parcel of land in East Lothian has different inherent **agricultural and ecological potential** to a parcel on Skye but, within the given potential of each, the actual level and mix of delivered ecosystem services will also be influenced by **what covers the land** (e.g. crops, grass, trees) and **how that land cover is managed** (e.g. frequency of field operations, unit volumes of chemical applications, stocking densities).
12. In addition, year-on-year variation in, for example, weather conditions and the incidence of pests and diseases can cause **fluctuations over time** in the level and mix of services from a given parcel of land, even if other factors are held constant.
13. This highlights that delivery of ecosystem services is highly **context specific**, varying spatially (e.g. even from one side of a glen to the other) and temporally. As such, policy efforts to alter the delivery of ecosystem services need to exhibit a degree of **flexibility** in terms of which outcomes are sought at particular locations and how they are sought⁵.
14. Moreover, **network and scale effects** mean that ecosystem service delivery at a given location can be influenced by what is happening at neighbouring or even more distant locations. For example, hydrological linkages across a catchment, or mosaic habitats and wildlife corridors across a landscape. Importantly, ecosystem services are themselves inter-connected, sometimes delivered as complements, sometimes as substitutes (hence the possibility of trade-offs).
15. All of which means that policy efforts also need to account for variable interactions and linkages between parcels of land, both in biophysical terms and in management coordination terms, and between ecosystem services. This applies both to single management units (e.g. a farm) but also to collections of management units (e.g. across a catchment), and implies **a need for some form of spatial planning** to identify how patterns of land use can be configured to deliver desired ecosystem services.
16. These considerations are relevant regardless of whether land is managed by the state (e.g. as with some forestry), by NGOs (e.g. as with some conservation reserves) or by private individuals and businesses. Moreover, these considerations are also relevant regardless of whether policy measures seek to influence land management through advice and training, regulatory obligations and/or financial incentives. That is, it is necessary to first identify and prioritise **desired outcomes** and acceptable trade-offs and **how they can be achieved** by actions on-the-ground, before choosing which specific policy mechanisms and measures can best secure delivery. Consideration could potentially

⁵ It is perhaps worth noting that prior to the rise of standardised agri-environment schemes, individually-negotiated management agreements tailored to specific sites were commonly used across the UK in relation to land subject to environmental designations. Management actions would be suggested on the basis of local experience and scientific knowledge (including modelling) to reflect what a site could deliver and how.

be given to whether it would be feasible and desirable for the Regional Land Use Partnerships (RLUPs)⁶ to play a role in informing regional decisions over environmental conditionality, in light of the above.

17. Current discussions around post-Brexit land use policy outcomes have included consideration of how to achieve “**public money for public goods**”, which mostly map neatly on to ecosystem services⁷⁸. Public goods are goods that are both non-excludable and non-rivalrous (i.e. individuals cannot be effectively excluded from their use, and use by one individual does not reduce their availability to others). As well as supporting delivery of public goods, government typically promotes a broader range of positive outcomes (including market goods) that are in the “public interest” or “for the good of the public” but which do not fall under the strict economic definition of “public good”, such as healthcare, education and social housing. Some commonly presented public good outcome categories relevant to agriculture and land use are listed below, noting that some (e.g. (f) to (k) below) are perhaps closer to “public interest”.

Examples of ‘public good’ outcome categories	Relevant Environment Strategy outcomes
a) biodiversity	Scotland's nature is protected and restored with flourishing biodiversity and clean and healthy air, water, seas and soils
b) air quality	
c) water quality	
d) soil health	
e) climate regulation (including hazards such as droughts and flooding)	We play our full role in tackling the global climate emergency and limiting temperature rise to 1.5°C
f) sustainable resource use	We use and re-use resources wisely and have ended the throw-away culture
g) national food security and sustainable timber production	Our thriving, sustainable economy conserves and grows our natural assets
h) animal/plant health and animal welfare	
i) landscape, heritage and public access	Our healthy environment supports a fairer, healthier, more inclusive society
j) rural cohesion	
k) sustainable global footprint	We are responsible global citizens with a sustainable international footprint.

18. Land management activities can also be categorised in a number of ways. The following is offered as an initial classification (with some overlap between some categories) to distinguish between different types of effort that could be expended in pursuit of delivering public goods:

(a) audits and plans – baselining of the current situation of a management unit (e.g. farm) in terms of site conditions, to help identify what needs to change and how this could be tackled. For

⁶ That the SG is committed to introducing in 2021, and to that end has asked the Scottish Land Commission for advice on.

⁷ However, the degree to which effective delivery of any public good can be achieved through increased regulation, improved environmental conditionality or incentives to land managers, will depend not only on the public good under consideration and the scale of delivery desired but also on a political decision on the balance to be struck between the use of “carrot and stick”.

⁸ Noting that one member of the group proposed that “public goods for public money” is a more appropriate phrase since it avoids implying that actions taken to achieve favourable outcomes for the public require to be funded accordingly.

example, a requirement to map soil condition across a farm and to produce a soil management plan with specific actions;

(b) advice and training – to improve awareness/understanding of opportunities for change, and skills to realise them. For example, attending group demonstrations of best management practices or formal CPD requirements;

(c) edge and/or spot management changes – adjustment to the management of field margins or discrete in-field features, to mitigate negative effects of other within-field activities and/or enhance positive effects. For example, a requirement to maintain wider buffer strips along watercourses to combat pollution runoff, maintain specific discrete habitats, such as ponds, or combat invasive non-native species;

(d) areal management changes – adjustment to within-field practices to mitigate negative effects. For example, a requirement to avoid arable soil compaction, reduce chemical usage or reduce stocking densities;

(e) areal land cover changes – switching between different cover types. For example, converting arable to grassland or grassland to forestry;

(f) restoration activities – to repair degradation. For example, peatland restoration or renovation of disused buildings;

(g) community engagement – to enhance local social capital, increase health and wellbeing benefits from the local environment (e.g. by improving public access) and/or raise mutual understanding of land management issues.

19. The majority of rural land in Scotland is managed by private individuals and businesses, who often possess valuable site-specific knowledge about their land and also represent important contributors both to rural communities and to rural economies. Although consideration may be given to changes to the regulatory baseline over the longer term, it is assumed that the policy emphasis will largely remain on seeking public good ecosystem service delivery **through supporting private land management** rather than through, for example, encouraging wholesale changes in ownership or management responsibilities (e.g. via NGOs or public bodies)⁹.
20. This implies that the current reliance on **uptake of desired management practices linked to support payments** will continue. This could (as in England) be interpreted as necessarily requiring an almost complete switch to using only (yet undefined) agri-environment type policy measures. However, this is not the only option¹⁰ since some provision of public goods is already sought (albeit weakly) through current cross-compliance and greening conditionality attached to decoupled area payments under Pillar I of the Common Agricultural Policy (CAP), and this conditionality could be extended¹¹.

⁹ Such policy options are available, but do not appear to have widespread political or community support and hence seem unlikely to be introduced to any great extent in the near future.

¹⁰ It is important to recognise that all payment mechanisms deploy variants of conditionality. The question therefore becomes how is that conditionality best delivered, e.g. whether it is applied to (more-or-less) all eligible land using an existing administrative system for direct payments or selectively via specific targeting and competition using an as-yet-undefined administrative system and set of payment rates. In other words, there is a practical judgement to be made about what can be delivered in the near future, and more philosophical judgements to be made about broad & shallow vs. narrow & deep and efficiency vs. equity.

¹¹ Indeed, the introduction of 'eco-schemes' under the CAP essentially follows this model.

21. In either case, the same processes of prioritisation and identifying required changes on-the-ground would be required, as would a degree of flexibility to suit site-specific circumstances. Similarly, both approaches would require some form of monitoring and inspections. As such, the choice between the two approaches depends more on other considerations, including likely uptake rates, relative administrative ease and breadth of contribution to the range of policy objectives. Tighter conditionality on area payments offers some attractive advantages for each of these:

(a) Voluntary uptake of agri-environment schemes can be patchy, reflecting a combination of factors including inertia, perceived bureaucratic complexity and inadequate incentives. By contrast, **uptake of decoupled payments is higher**. This may reflect higher payment rates but is likely to also reflect the non-competitive nature of such support and the stronger motivation of aversion to losing an 'entitlement'.¹² This implies that tightening conditionality on area payments is likely to improve environmental management of more land than expanding agri-environment schemes will, at least in the short-term;¹³

(b) Administratively, creating new systems for different and greatly expanded agri-environmental schemes is likely to be challenging. By contrast, systems are already in place for administering decoupled area payments and should be capable of accommodating adjustments to conditionality requirements relatively easily. This would preserve a degree of **familiarity** for administrators and applicants alike;

(c) In addition, under WTO rules, whilst calculation of payment rates under agri-environment schemes has to be justified in terms of income forgone and costs incurred,¹⁴ decoupled area payments are classified as decoupled income support and therefore require no equivalent explicit justification within the **WTO's Agreement on Agriculture**¹⁵. As such, area payments are easier to set administratively (although it is possible that other WTO members will seek to challenge payments under either approach) and to implement in practice;

(d) Retaining at least some level of decoupled area payments will provide a degree of **stability**,¹⁶ helping incumbent land managers to remain in place and thereby contribute to social and economic outcome across rural Scotland. This continuity matters in terms of site-specific (often tacit) knowledge about land capabilities and past management that can guide changes, but also

¹² Parallels can be drawn with Land Manager Options under Land Management Contracts or, further back, the original entry-level Tier of Environmentally Sensitive Areas.

¹³ Concerns have been expressed in England about the loss of behavioral leverage that immediate abandonment of cross-compliance risks given that new agri-environment support (through ELMs) is still under development and will be phased in.

¹⁴ Payment by Results can potentially avoid this, but many existing schemes actually base payment calculations on management actions due to farmers' risk preferences and difficulties in monitoring outcomes – thereby reverting back to the WTO criteria. The use of auctions to set payment rates, whether for Results or Actions, is another possible approach.

¹⁵ 'Green-box' support is permissible to any extent and is considered not trade distorting – and therefore has no inherent link to agricultural production. Examples include the current BPS and Greening schemes as income support tools and also agri-environmental payments which must be linked to an Environmental Strategy and based on income foregone and additional costs incurred by farmers. Any environmental payments made to farmers are considered to be under the auspices of the Agreement on Agriculture whether they are available to non-farming enterprises, or not. See: https://www.wto.org/english/tratop_e/agric_e/agboxes_e.htm

¹⁶ The level of area payments is expected to fall and may continue to do so over time. Moreover, tighter conditionality may imply higher compliance costs and therefore a lower level of net support even if the gross level remained constant – although allowing greater local flexibility in management prescriptions may mitigate this.

in terms of resident land managers' contributions to community cohesion and social capital and the need to minimise disruption under the Just Transition principles.¹⁷

(e) Similarly, a degree of support stability will help to maintain capacity for **food production** and multiplier linkages to the wider **rural economy**.

22. Not all public good ecosystem services nor all management actions listed in paragraphs 17 and 18 above will necessarily fit easily into conditionality requirements. For example, restoration activities typically require upfront capital expenditure that is unlikely to be covered by standard area payments, highlighting the importance of a **complementary, well-funded agri-environment scheme**. Similarly, collaboration (or at least coordination) across different management units to adjust catchment or landscape-scale land use patterns may require separate measures.
23. However, at least some services and actions will be suitable for inclusion in conditionality requirements. For example, drafting of and adherence to meaningful management plans and modifying some in-field management practices. Hence there is a need to progress discussions around policy priorities, on-the-ground changes needed to achieve them, and which changes can be sought through tighter conditionality on area payments rather than separate agri-environment schemes.
24. These discussions should include consideration of:
 - the contribution that agriculture and land use can make to achieving the outcomes of the **Environment Strategy**, and how this links to wider goals for Scotland's **economy and wellbeing**;
 - how to deliver policy outcomes in a more **integrated** way across different types of land use - including agriculture, forestry, deer management and sporting estate management; and
 - whether there is scope to promote **targeting** and delivery of policy outcomes at **appropriate spatial scales**, including any interaction with the role of RLUPs.

Suggested Approach

25. Whilst the *Farming and Food Production Future Policy Group* have not yet reported, there has been considerable discourse around the required direction of travel for future rural support policy as outlined above. The Scottish Government's consultation on the "Future of Scottish Agriculture"¹⁸ and the "*Future Strategy for Scottish Agriculture*" by the Agricultural Champions¹⁹ both stress the need to derive **greater public good / public value for money** from rural support payments. As noted above, this will be core to achieving Scotland's climate change and environment targets.
26. The options/mechanisms to deliver such 'public good' ambitions have yet to be fully explored within the UK and the discussions in other administrative regions are more focused on revolution of agricultural policy, rather than a stepwise evolution. The UK and Welsh Governments have set out ambitious agendas to transform support away from direct agricultural support (albeit with relatively

¹⁷ Although there is a risk of over-claiming the uniqueness/effectiveness of agriculture in delivering public good outcomes. There are, in theory, other possible mechanisms and approaches that could also be used to achieve these outcomes e.g. a universal rural income support scheme.

¹⁸ See

<https://www.webarchive.org.uk/wayback/archive/20170701124644/http://www.gov.scot/Topics/farmingrural/Agriculture/The-Future-of-Scottish-Agriculture>

¹⁹ See <https://www.gov.scot/binaries/content/documents/govscot/publications/progress-report/2018/05/future-strategy-scottish-agriculture-final-report-scottish-governments-agriculture-champions/documents/00536005-pdf/00536005-pdf/govscot%3Adocument/00536005.pdf?f>

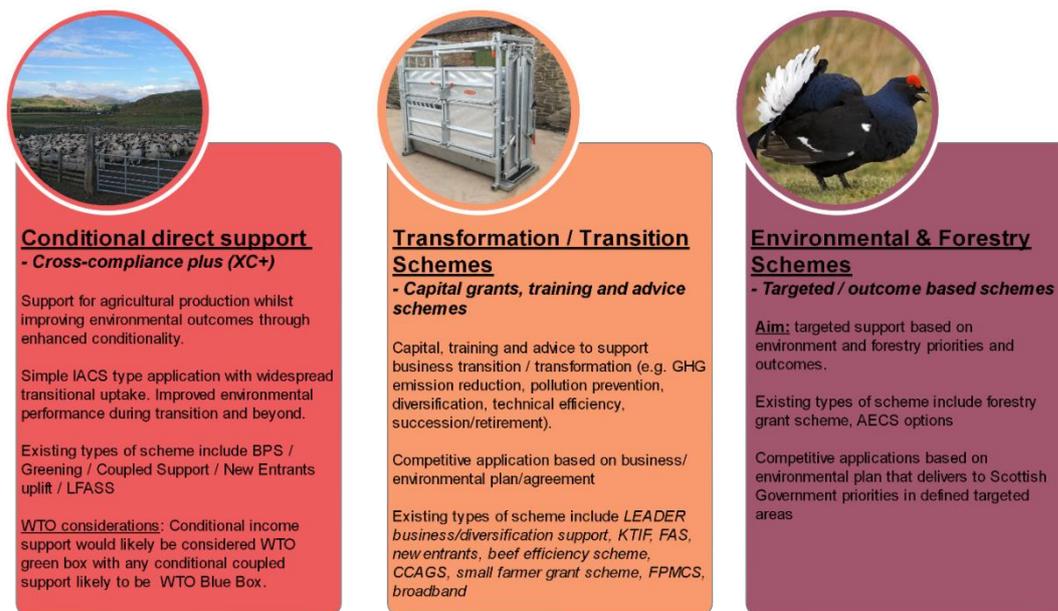
weak conditionality), towards a system of environmental payments based on outcomes/results. These approaches require development of an **entirely new rationale and suite of delivery mechanisms** for agricultural land management support. As such, retention of a modified form of **direct payments with strengthened conditionality** offers **many advantages** over a shift to (as-yet-undefined) alternative delivery arrangements where uptake by land managers would also be uncertain.

27. Leaving the constraints of the current CAP regime gives significant scope to improve the existing delivery model and to address specific weaknesses, without a wholesale change to a completely new and perhaps complex delivery system. This approach appears to have similarities to the next, ongoing, evolution of the CAP where increased conditionality and eco-schemes²⁰ are being considered as options for more devolved, and environmentally responsible CAP schemes within the EU's regions.
28. It is important to recognise that effective future agricultural support in Scotland will require a number of different approaches to deliver the desired outcomes to help the Scottish Government achieve its ambitious targets regarding the food and drink sector, climate change, biodiversity and wider environmental health. Therefore, understanding the overarching policy framework in which any future direct support with enhanced conditionality sits is vital as many priorities will still **require dedicated, targeted approaches** to deliver the desired outputs (e.g. for forestry, priority habitats and species and climate change mitigation).
29. The Scottish Government has not yet made long-term commitments with regards to future agricultural policy (post 2024) in Scotland. However, it is essential that effective and meaningful **transition pathways** to any future support schemes are identified early to ensure there is a 'just transition' approach where nobody is left behind without having been given an opportunity to change management practices (i.e. avoidance of unintended consequences). An evolution of direct support payments to have greater environmental conditionality would be a rational transition framework that causes minimum socio-economic disruption whilst embedding the principles of enhanced environmental stewardship across most Scottish agricultural businesses.
30. Without suggesting what any future Scottish rural support policy framework may look like, it is worth recognising that a number of existing policy schemes or delivery mechanisms may be maintained or evolved in the short to medium term. Figure 1 provides an illustration of a support hierarchy in which environmental conditionality might sit. Within this illustrative framework, **Conditional Direct Support** is complemented by schemes designed to support **Transition/Transformation** (to aid land-based industries to restructure, become more efficient, improve environmental performance or add value); and schemes targeted at **Environmental and Forestry** priorities (to deliver priority measures which are not appropriate for direct payment conditionality; and which may be supported on the basis of payment by outcomes or results).
31. The types of support illustrated in Figure 1 purely act as a reminder that future direct support with enhanced conditionality will sit within a broader suite of policy measures. No indication of how the available budget should be distributed across different policy themes is provided - as that will be determined by political direction and policy decisions (and may well change over time). That said, in order to remain attractive, any future direct support would need to be at a level that encouraged **widespread uptake** to deliver environmental outcomes as proposed here. It would also be **vital for sufficient funding to be allocated to Environmental and Forestry schemes** in order to achieve priority outcomes that cannot be delivered through conditionality.

²⁰ See <https://ec.europa.eu/eip/agriculture/en/news/new-guide-%E2%80%9CUsing-eco-schemes-new-cap%E2%80%9D>

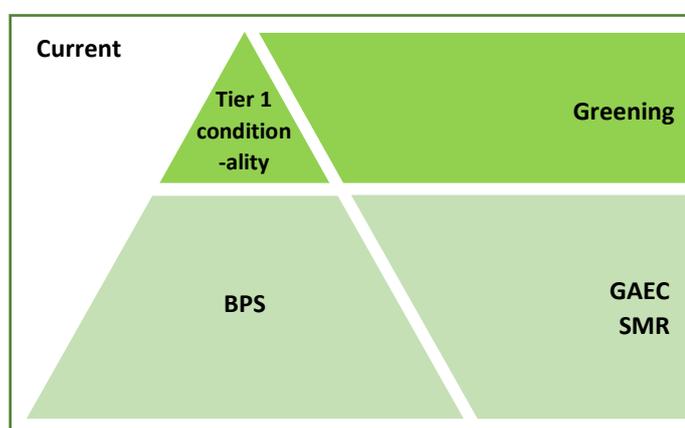
32. The approaches described here are evolutions of existing mechanisms, meaning change will be more easily managed from both administrative and land managers' perspectives. This framework provides a **relatively stable policy platform** for future financial support that will help to drive the transformative changes needed to achieve Scotland's climate and environment targets within the WTO green box criteria (with some blue-box support required if coupled support remains a priority). Within the framework's wider suite of delivery schemes, allocations of future support budgets could be easily changed over time as political and Scottish Government priorities evolve.

Figure 1 Illustration of the types of schemes that could sit alongside conditional direct support.



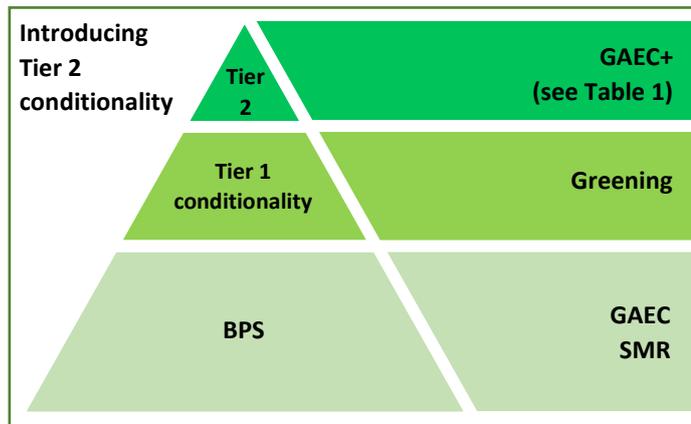
33. One of the founding principles of this scoping paper is the evolution of the Basic Payment Scheme and Greening Payments into a single income support scheme with different **payment tiers** based not only on land-use but also on the **extent of conditionality** achieved by land managers. The number of tiers is not particularly relevant at this stage, rather what this demonstrates is how WTO green box support can be relatively simply evolved where the payment rate becomes increasingly determined by mandatory and voluntary conditionality measures. For illustrative purposes only, we sketch out the addition of two further tiers whilst keeping greening, though after transition the final state could evolve most simply to two tiers: a core payment dependent on a mandatory set of conditions with a higher tier of payment for additional options from a menu.

a. **Currently**, the Basic Payment Scheme (BPS) is conditional on farmers complying with Good Agricultural and Environmental Condition (GAEC) and Statutory Management Requirement (SMR) cross compliance measures. In addition, the Greening Payment, that currently attracts 30% of the direct support budget, acts as a “Tier 1 conditionality” payment. Since evidence suggests that the EU greening requirements are not well



designed for achieving environmental priorities in Scotland, these could potentially be amended during the Stability and Simplicity period up to 2024²¹.

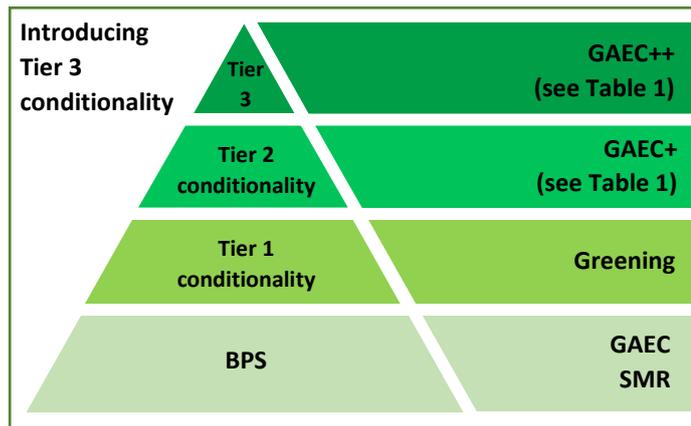
- b. It would be relatively straightforward to introduce a second, higher tier of conditionality if wished – described here as “**Tier 2 conditionality**”. This would be pre-announced and would allow land managers the opportunity to plan and/or invest (perhaps with support through small environmental capital grants for hedgerow planting, fencing, etc.) to enable them to meet Tier 2 conditions. The budget for direct payments could be distributed



between the tiers (ratio to be determined). For example, land managers could receive a proportion of their direct payment on the basis of meeting GAEC, SMR and greening requirements; and the remainder if they meet Tier 2 conditions. This effectively would **incentivise land managers to deliver greater ‘public goods’ if they want to maintain their existing levels of support**. The conditions in Tier 2 would include both mandatory and voluntary measures (examples are set out in Table 1 p18) described as **GAEC+**. In return for the Tier 2 payment, land managers would be required to comply with a set of mandatory measures; and to choose a minimum number of voluntary measures from a menu. This would allow land managers the flexibility to select the conditions most relevant to their holding, while still meeting a minimum standard of environmental gain in return for payment. Given the variation in land cover and habitats across Scotland, it would be essential to ensure that mandatory measures are suitable for all farming systems and locations, and that there is a sufficiently wide range of voluntary options available for land managers to choose from. In order to build on the existing model for direct payments, it is assumed that land managers would sign up to conditions on an annual basis. Further consideration could be given to the feasibility of requiring land managers to commit to undertaking some or all conditions on a multi-annual basis, to support longer-term management where this will enhance the outcomes achieved. However, this would require careful assessment of delivery implications. Further consideration could also be given to whether greening requirements in Tier 1 should be replaced altogether, given evidence of their limited effectiveness, or whether some elements of greening (e.g. the Ecological Focus Areas requirement) should be retained.

²¹ For example, by replacing the crop diversification and permanent grassland greening requirements with conditions that are better-tailored to Scottish priorities, while retaining/strengthening the EFA requirement.

c. Following a period where land managers get familiar with Tier 2 conditionality, a third tier of conditionality could be introduced, including more ambitious measures. Examples of mandatory and voluntary measures that could be included in “**Tier 3 conditionality**” are set out in **Table 1**, described as **GAEC++**. As before, the direct payments budget would be distributed between tiers, in order to incentivise uptake of Tier 2 and 3 payments and conditions.



34. Using this approach, providing the conditionality measures are well designed, much greater public value could be derived from support payments, whilst maintaining food production across Scotland. Further, opportunity may exist within this approach to **minimise on-the-ground compliance inspection** need by putting the onus of compliance proof onto the land manager and using increased (but proportionate) non-compliance penalties to deter falsified claims.

Specific environmental outcomes potentially achievable from enhanced conditionality

35. Paragraphs 6 to 8 above highlight that the primary focus of any enhanced environmental conditions on direct payment should be on helping promote the land uses changes needed to achieve the outcomes highlighted in Scotland’s Environment Strategy. It is also recognised that any environmental conditionality on direct payments would need to sit within a **wider package of targeted measures**, including something akin to a well-funded agri-environment scheme, in order to achieve the scale of the environmental outcomes required.
36. That context needs to be kept in mind together with the fact that what follows should be regarded as **illustrative** not definitive with regard to any environmental conditionality on direct payments. Much more **detailed discussion and analyses** would be required before any specific list of environmental measures to include within such conditionality could be decided upon. Moreover, since the need to consider and agree relevant measures applies regardless of whether they are to be implemented via tighter conditionality or some other mechanism (e.g. regulation or agri-environment schemes), there is a generic need to define measures. Overall, a combination of regulation, conditionality and agri-environment support is likely to be required: regulation to prevent negative externalities (such as direct pollution); tight conditionality on direct payments to reward delivery of public goods; and agri-environment schemes to support more ambitious environmental management and restoration²². The aim here is therefore merely to categorise **types of measures** likely to be more or less compatible with conditionality requirements rather than specify measures in detail.
37. Paragraph 17 above provided a range of ‘public good’ outcome categories, not all of which are being considered in this scoping exercise:

²² Agri-environment schemes could also provide capital payments to enable land managers to comply with management conditions for accessing higher level ‘tiers’ of direct payments.

- Agricultural emissions related to **air quality (b)** are dominated by ammonia. An independent report published in autumn 2019²³ recommended that the Scottish Government should work with SEPA and the agricultural industry to develop a voluntary code of practice. The report also highlighted that in some instances changing farm management to reduce emissions (e.g. through covering slurry tanks and lagoons) will require significant up-front investment, which may be difficult for many farmers in the short term, and hence a more detailed analysis of the costs and benefits of possible mitigations set within the Scottish context is required. Consideration of potential air quality measures to include within environmental conditionality is therefore more appropriate to consider in the future, in order to take into account any developments on the code of practice and/or findings from the cost and benefit analyses.
- **Rural cohesion (j)** could potentially be considered as a desired outcome from enhanced conditionality on direct payments. For example, this might include **LFASS-type support**, on the basis that maintaining **high nature value farming systems** in an area under natural constraints could help to ensure positive environmental management continues to be applied, while also supporting rural communities. However, the delivery of such environmental outcomes is not currently a condition associated with LFASS support and careful consideration would need to be given to what such conditions could be. Further consideration would also be required over how any future LFASS-type support could be more closely targeted towards supporting and rewarding high nature value farming systems, since the current scheme is not optimally designed for achieving this. Hence we consider that the question as to whether such LFASS-type support sits best within direct payments or elsewhere in the wider support framework requires further consideration.
- Enhanced conditions could also be considered to achieve additional outcomes – such as **national food security (g)** and/or **animal/plant health and animal welfare (h)** – which are more directly related to agricultural productivity outcomes (though also having wider indirect benefits if they improve the cost-effectiveness of the farming enterprise). Again, we consider this question - as to how broad the outcomes expected from enhanced conditionality should be – will require further consideration.
- Some aspects of **landscape, heritage and public access (i)** could similarly be achieved via an enhanced environmental conditionality approach. But as landscape outcomes are in practice likely to require well-funded, targeted agri-environment type approaches, we have limited consideration in this scoping phase to where measures focussed on preservation or maintenance of natural heritage features on farms could potentially help underpin any more targeted landscape scale delivery. Further analysis is required to explore the extent to which conditionality could help to support improvements to public access to the environment.
- Further consideration could be given to whether there are opportunities within environmental conditionality to promote **sustainable resource use (f)** (for example, by adopting circular economy practices and reducing waste) and to improve the sustainability of Scotland’s **global footprint (k)**.

38. The focus of this scoping phase of the work has therefore been put on those outcome categories from paragraph 17 - **biodiversity (a)**, **water quality (c)**, **soil health (d)** and **climate regulation (e)** – where **direct environmental benefits** would be expected (even if achieving a larger scale of impact would

²³ <https://www.gov.scot/publications/cleaner-air-scotland-strategy-independent-review/pages/3/>

also require such environmental conditions on direct payments to be complemented by additional agri-environment type approaches).

39. As is highlighted in paragraphs 13 and 21 above, **ensuring flexibility to address site-specific circumstances** will be essential, regardless of whether the environmental outcomes are being sought via conditionality on direct payments (which provides more ‘universal’ coverage) or via an agri-environment approach (where uptake is likely to vary around the country).
40. This document is focussed on setting out why Scottish Government might want to use the former approach rather than only the latter, and hence is not focussed on the detailed conditions per se. But that lack of focus on the specific details also reflects the fact that those detailed conditions – and whether they vary from geographical region or farming system – will need careful consideration and discussion as to the level of outcomes achievable and the practicalities of implementation.
41. It will also be important to recognise that site-specific circumstances will not only vary between geographical regions or farming systems but also within any specific geographic region or farming system. Nevertheless, it is still feasible to make some general comments about how some of the desired environmental outcomes highlighted in paragraph 38 are likely to be similar or vary between different regions or farming systems:
- Improving **soil health** and **climate regulation** is likely to be a **common desired outcome** irrespective of farming system or geographical location. Although some of the specific opportunities - and hence conditions - may differ (e.g. a greater scope for peatland restoration/management in uplands areas and a greater scope for agroforestry creation/management in lowland areas), **the vast majority of farms/crofts across Scotland** will need to do more to address these two environmental outcomes in the future in order for Scotland to achieve Net Zero by 2045²⁴.
 - Addressing **water quality** issues (such as diffuse pollution, nitrate leaching, pesticide contamination and soil erosion) is not confined to the more intensive farming systems (such as dairy, arable, horticulture pigs and poultry) but nevertheless will be a much more consistently occurring environmental issue within **lowland Scotland**²⁵. Some of these water quality issues (such as pollution from sheep dip or from forestry harvesting operations) will be an issue in some **upland areas of Scotland**, but here there will be a more consistent need to address **water quantity issues** and hence help alleviate flooding further downstream.
 - There are a wide variety of pressures on **biodiversity** in Scotland²⁶, but in **upland farming systems** there is likely to be a need **to retain some form of agricultural/grazing management** in order to maintain appropriate management of high nature conservation habitats and species, while in **lowland farming systems** the biodiversity imperative is likely to revolve around **redressing the habitat simplification** that has occurred through loss of habitats and inappropriate management (including lack of management) of those fragments that remain^{27 28}.

²⁴ <https://www.gov.scot/publications/protecting-scotlands-future-governments-programme-scotland-2019-20/pages/5/>

²⁵ <https://www.sepa.org.uk/regulations/land/agriculture/sector-specific-issues/>

²⁶ <https://www.nature.scot/scotlands-biodiversity/key-pressures-biodiversity>

²⁷ http://minisites.ieep.eu/assets/223/WP5ND1_agbiodiversity.pdf

²⁸ <https://www2.gov.scot/Resource/Doc/197434/0122614.pdf>

42. Payments to farmers to deliver public goods can be broken down into three main groups – with the examples provided within each simply intended to be **illustrative** not definitive:

Group 1: Measures which **do not require any significant degree of tailoring to local conditions**. The management required - and hence costs for land managers - will vary but often will not be very large. These sorts of measures include:

- Maintaining and preventing loss and damage to existing habitats considered to be of biodiversity or wider environmental value, such as hedgerows, field margins, areas of species rich grassland;
- Improving soil health through understanding its current condition and developing – and implementing – appropriate soil and nutrient management plans;
- Understanding the risks to animal (and potentially plant) health on farms and implementing appropriate health and biosecurity plans;
- Practicing systems such as organic farming, which have a range of environmental benefits and can be applied nearly everywhere.

Group 2: Measures which **require some reflection of local conditions** (e.g. farm type, geographical area) and where the **management required and costs for land managers are likely to be higher** than those within Group 1. These sorts of measure include:

- The establishment and management buffer strips, beetle banks, skylark plots, grass margins, field corners etc.;
- Requiring the establishment of soil cover at particular times of the year, particularly during the winter;
- Managing semi-natural habitats, for example grassland, heathland, moorland, etc;
- Undertaking and implementing farm level plans to minimise GHG emissions and to maximise carbon sequestration and storage.

Group 3: Measures which are **much more targeted in nature**, including **more demanding location specific environmental land management**. These measures are akin to many of the current suite of measures available under Scotland's current agri-environment scheme²⁹. However, the introduction of enhanced conditionality on direct payments may mean that the anticipated outcomes from some of these existing measures may be more relevant to seek to achieve through conditionality (incorporating GAEC+ or GAEC++ in the above framework).

43. The relative easier implementation of **Group 1** type measures may make them more relevant to consider under **GAEC+** in the framework outlined in the previous section, while the additional management requirements associated with **Group 2** type measures would potentially make them more relevant to consider under **GAEC++**.

44. Some of the existing Scottish **agri-environment measures** also have the potential to sit within one or other of these two Groups and be more appropriately – and more widely – delivered via the environmental conditionality route. In addition, some measure within Groups 1 and 2 may have clear environmental benefits irrespective of the scale at which they implemented, hence their implementation could be set as **either mandatory or voluntary** depending on local priorities.

²⁹ <https://www.ruralpayments.org/topics/all-schemes/agri-environment-climate-scheme/management-options-and-capital-items/>

45. However, the environmental impact of some of the other measures in these two Groups (but especially Group 2) may be **dependent on a high uptake** at the farm and landscape level at which they are implemented. Hence their uptake could be set as **mandatory** within the suite of measures which land managers have the opportunity to choose from.
46. The background section above has highlighted that any selection of measures to include under enhanced conditionality will need to take into account the **wide variation** in farm types and biophysical characteristics that occur across Scotland. Hence we suggest that there will be a need to include **a suite of measures** - some of which may be set as mandatory while others are regarded as voluntary. Land managers would be required to comply with all mandatory conditions (as well as existing greening and cross compliance requirements). Land managers would then have the **flexibility** to select a minimum number (to be decided) of voluntary conditions, allowing them to choose the conditions that are most relevant to their situation and hence increase the likelihood of achieving the desired environmental impact.
47. Table 1 provides an initial illustration of where examples of existing measures could potentially sit within the GAEC+ or GAEC++ and Mandatory or Voluntary matrix (columns 2 to 5). It also provides examples of measures which are not suited to an environmental conditionality approach and hence likely to still require implementation and delivery of environmental outcomes through a well-funded, more targeted agri-environment approach (column 6).
48. These examples are **illustrative** only. Further analysis and reflection will be needed to agree the key policy objectives to be delivered; and to identify the measures that should be included within environmental conditionality in order to achieve them. Further detailed consideration will also need to be given to the following issues:
- a. As indicated in paragraph 43 above, **GAEC+** measures primarily relate to more easily implemented **Group 1** measures while **GAEC++** measures relate to **Group 2** measures which require more effort to undertake. It is suggested that both categories should include a suite consisting of Mandatory and Voluntary measures, but the **required uptake** of these will need to be considered further. Criteria for differentiating GAEC+ from GAEC++ measures, and the **level of ambition** they should each be required to achieve, will also need to be explored further. For example, it may be desirable to further increase the level of ambition of GAEC++ measures (beyond the illustrative examples given in Table 1) to justify the extra payment rate and achieve agreed outcomes.
 - b. The composition of the final suite of environmental conditions made available within this matrix will need to take into account whether or not the suite made available might also need to **vary geographically**. Any potential role for Regional Land Use Partnerships in informing the targeting and coordination of measures (e.g. in order to promote uptake at an appropriate spatial scale) will also need to be considered further.
 - c. The focus in these examples is also on measures that can be delivered by farmers and crofters. Once the framework within which the enhanced conditionality sits is clearer, a key priority will be to explore the feasibility of **broadening eligibility** for direct payments to **other land managers**. Consideration should also be given to opportunities for achieving wider land use objectives (e.g. in relation to forestry, deer management and sporting estate management) through environmental conditionality, and for promoting a more **integrated approach** to land management, helping to create multifunctional landscapes.

- d. Further detailed consideration would also be needed to determine whether measures could be selected which deliver on **multiple environmental outcomes**³⁰. The original intent of Table 1 was to highlight examples of existing measures where such multiple outcomes were likely. However, it proved extremely difficult to group measures in this way, since the vast majority of existing measures are primarily focussed on delivering one environmental outcome or another. Obtaining multiple outcomes from any one measure associated with environmental conditionality (or indeed any delivery mechanism) therefore requires careful deliberation and designing.
- e. Careful consideration would also need to be given to whether or not obtaining multiple outcomes from single measures is feasible from a practical perspective. Attempting to obtain multiple outcomes is likely to **add to the complexity of the conditions** associated with any one measure – in practice, this might not only serve to dilute the level of each environmental outcome delivered by that measure but the complexity might also reduce land managers’ willingness to implement that measure. Any opportunities to avoid or manage these risks should be explored further.
- f. The primary focus of this scoping document was to consider whether strengthening environmental conditionality of direct payments was feasible or not and could deliver increased benefits. **The conclusion is that it is**. But the design of any such measures will need to be carefully thought through, not only involving the choice of the measures to deliver the environmental outcomes desired but also – as the next section highlights – the practicalities around delivery and implementation.

Delivery Implications

- 49. Regardless of the policy option(s) adopted in the future, challenges will inevitably be faced in **designing, implementing and monitoring** specific schemes. For example, if on-the-ground measures relevant to achieving desired environmental outcomes can be identified and agreed, the details of prescribed management actions (or outcomes if payment-by-result mechanisms are used) have to be codified and communicated to scheme applicants (comprising a broader range of land managers than previously) and systems for monitoring compliance and outcomes have to be instigated. Similarly, processes for **applications and appeals** need to be designed and resourced.
- 50. Given that environmental management and/or outcomes are generally harder to monitor than, for example agricultural commodity production, **implementation costs** are likely to be unavoidably higher for schemes with this kind of environmental conditionality. This will be amplified if greater flexibility is allowed to accommodate variation in regional priorities and measures, and if higher tier measures require greater monitoring/inspection³¹.

³⁰ Note however that assessing - and just as importantly quantifying - the co-benefits delivered from any one measure will be a complex and potentially impossible task. At best, a qualitative listing of the main benefits expected might be feasible.

³¹ When assessing delivery implications, it will be necessary to clarify detailed requirements under each tier e.g. whether the conditions under Tiers 2 and 3 relate to the entire area of the holding or a proportion of it.

Table 1 Examples of measures where enhanced conditionality could potentially be achieved under GAEC+ or GAEC++ approaches, together with examples of measures not suited to such an approach and hence more suited to delivery of environmental outcomes under an agri-environment approach

Environmental outcome likely to be achieved*	Environmental measures potentially suited to delivery under enhanced conditionality				Environmental measures <u>not suited</u> to delivery under enhanced conditionality
	GAEC+		GAEC++		
	Mandatory	Voluntary	Mandatory	Voluntary	
Primarily Climate Change Benefits	<ul style="list-style-type: none"> • Soil Testing • Nutrient Management Plan • Carbon Audit 	<ul style="list-style-type: none"> • Implement an Animal Health Plan • Provide constant soil cover • Minimise soil disturbance 	<ul style="list-style-type: none"> • Soil Testing • Nutrient Management Plan • Carbon Audit 	<ul style="list-style-type: none"> • Cover and aerate slurry and manure while stored • Establish and maintain grass clover swards • Select more drought resistant crop varieties 	<ul style="list-style-type: none"> • Peatland restoration • Agroforestry creation and management
Primarily Biodiversity Benefits	<ul style="list-style-type: none"> • Management or restoration of existing hedgerows^{AECS} • Management of existing species rich grassland^{AECS} • Habitat mosaic management^{AECS} 	<ul style="list-style-type: none"> • Unharvested Conservation Headlands for Wildlife^{AECS} • Creation of beetlebanks in arable fields^{AECS} • Management of wader grazed grassland^{AECS} 	<ul style="list-style-type: none"> • Management or restoration of existing hedgerows^{AECS} • Management of existing species rich grassland^{AECS} • Habitat mosaic management^{AECS} 	<ul style="list-style-type: none"> • Wild Bird Seed for Farmland Birds^{AECS} • Creation of hedgerows^{AECS} • Moorland Management Plan^{AECS} 	<ul style="list-style-type: none"> • Outcome based results schemes targeting particular habitats or species at landscape scale
Primarily Water Quality or Flood Management Benefits	<ul style="list-style-type: none"> • Management of water margins in arable fields^{AECS} • Stubbles followed by green manure in an arable rotation^{AECS} 	<ul style="list-style-type: none"> • Management of water margins in grassland fields^{AECS} • Follow best practice with metaldehyde slug pellets 	<ul style="list-style-type: none"> • Management of water margins in arable fields^{AECS} • Stubbles followed by green manure in an arable rotation^{AECS} 	<ul style="list-style-type: none"> • Establish biobeds in sprayer handling areas • Develop and implement a Farm Waste Management Plan^{AECS} • Converting arable at risk of erosion or flooding to low-input grasslands^{AECS} 	<ul style="list-style-type: none"> • Capital works • Sustainable drainage systems or large-scale flood mitigation measures^{AECS}

*At this stage, the separation of environmental outcomes into where the primary benefit would lie reflects the fact that the vast majority of existing measures primarily focus on delivering one environmental outcome or another. Careful consideration and design will be required if multiple outcomes are desired from any one measure; ^{AECS} Indicates where a measure is currently part of Scotland’s existing Agri-Environment & Climate Scheme (AECS)^[1] (though detailed requirements would need to be reviewed/adapted for environmental conditionality purposes) The relevance of existing measures under the Forestry Grant Scheme for inclusion under enhanced conditionality would also need consideration^[2]

^[1] <https://www.ruralpayments.org/topics/all-schemes/agri-environment-climate-scheme/management-options-and-capital-items/>

^[2] <https://www.ruralpayments.org/publicsite/futures/topics/all-schemes/forestry-grant-scheme/>

51. Consequently, whilst efforts should be made to deploy **digital technologies** for applications (e.g. on-line forms) and monitoring³² (e.g. remote sensing, drones, digital farm records, geo-tagged digital photos), it is likely that additional **administrative resources** will be required, including for staff training. The latter may also be required to establish the necessary complement of farm advisers capable of providing integrated environmental and business advice to all land managers.
52. All of the above considerations apply to tighter environmental conditionality, but some cost elements may be lower than for alternative mechanisms for delivering improved environmental outcomes since systems are already in place for existing area payments.

Outstanding issues that remain to be considered

53. The initial draft of this document highlighted a number of questions that would need to be considered to (a) **guide any further refinement** of this scoping document or (b) **inform the more detailed analyses and discussions**.
54. The comments received from across a range of Scottish Government departments and agencies meant that some of those initial questions (such as **the importance of developing an approach that complies with WTO green box regulations**, and a number of questions around **the practicalities of implementation and delivery in practice**) could be incorporated and further expanded within the main body of this revision.
55. It was, however, clear from the combined responses that for the majority of those initial questions there was **either a divergence of opinion** in how the question was answered or those commenting felt that **further more detailed analyses would be required** to inform any answers.
56. Addressing such outstanding issues **will be essential after this scoping) phase**, if a decision is taken to **continue to investigate in detail** the potential for increased environmental conditions being attached to any future direct payments. Importantly, Scottish Government **agricultural policy and inspection staff need to be proactively involved** in any further discussions since tighter environmental conditionality builds upon the current support system.

³² Requirements for monitoring to ensure public accountability could be relaxed to tolerate (for example) a lower rate of inspections and/or less precision in meeting eligibility and performance criteria, perhaps through a different risk-based approach.

Appendix 1: Draft Scottish Government Working Assumptions

- As reiterated in the **Environment Strategy vision and outcomes document**³³ published in February, the Scottish Government ‘will seek to maintain or exceed EU environmental standards’. We also wish to remain broadly aligned with the spirit of EU rules to facilitate Scotland’s future re-entry to the EU. At the same time, we wish to use the opportunity of EU exit to establish a domestic rural support regime targeted on Scottish needs.
- The environmental conditions attached to direct payments should therefore be at least equivalent in their level of ambition to the new CAP rules; but we should take the opportunity to design rules that are best suited to Scotland’s circumstances.
- In your considerations, it would be helpful to **highlight where they diverge from the new CAP proposals**, so we’re aware of where the differences lie.
- The key assumption is that we are **aiming to develop measures that are best tailored to Scotland’s needs**, and recognise that this may diverge from policy approaches in other parts of the UK.
- As above, it will be helpful to **highlight the areas where there is policy divergence**, particularly with rules in England.
- In broad terms, Environmental Direct Payments should be designed to promote the changes in land management needed to deliver **agriculture/land-use’s contribution to achieving the Environment Strategy outcomes on nature, climate change and resources** and other relevant output targets e.g. on tree planting and peatland restoration.
- In some scenarios, e.g. for high nature value farming systems, there may be scope for Environmental Direct Payments to promote **continuation** of existing practices, rather than changes in land management.
- It will also be important to take into account the following factors, which will influence the level of ambition achieved through Environmental Direct Payments:
 - What it is reasonable to expect farmers and other land managers to do in return for the **level of payment** received.
 - What types of measures **lend themselves to generic conditions**, bearing in mind that some more ambitious and bespoke measures may be better suited to a voluntary, multi-annual, agri-environment approach.

³³ <https://www.gov.scot/publications/environment-strategy-scotland-vision-outcomes/>



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