



House of Commons
Environment, Food and Rural
Affairs Committee

Reform of the EU Sugar Regime

Second Report of Session 2005–06

Volume I



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Sugar Regime**

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*Report, together with formal minutes and lists
of oral and written evidence*

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Environment, Food and Rural Affairs Committee

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Summary

We welcome the Commission's approach to reform of the EU sugar regime, which centres on price reductions, as this is an essential element in bringing the European sugar market into balance. Setting the price low enough to drive out the inefficient producers, but high enough for the most efficient to prosper, is the critical balance that will define the success of the reforms.

It seems certain that pressure will be applied in the negotiations, from other Member States, to dilute the price cuts significantly. The UK Government's negotiating position must be to support the Commission in minimising any such dilution.

Given the highly competitive climate in which manufacturing operates, and the pressure which the large retailers can bring to bear on their suppliers, it is likely that consumers will benefit from some degree of sugar price reduction in the medium to longer term.

Direct payments to sugar beet growers must be fully decoupled from production, in order to minimise market distortion. The UK Government should strongly oppose any attempt to introduce the option of partial decoupling into a compromise package.

We are concerned about the unfair impact on the UK of applying the proposed price cut to the new unified quota. The UK Government should negotiate for a change in the proposals, so that the UK's industry is adequately recognised in the compensation package.

The UK Government should ensure that the final reform package allows the UK's sugar beet industry to exploit its position of relatively high efficiency. No distortions should be allowed into a compromise deal that could discriminate against the UK beet sector.

We recognise the benefits in terms of biodiversity provided by beet growing in the UK. But these benefits should be secured, and funded, through targeted agri-environmental programmes under the CAP.

The Government must negotiate to ensure equitable terms of competition between the cane and beet sectors in the UK. The cane sector is unduly disadvantaged by the proposals as they currently stand and we are sympathetic to the suggestion of retaining some form of refining aid.

The UK Government should support the maximum possible increase in the level of assistance for the ACP countries, both in 2006 and in the subsequent years covered by the Commission's Action Plan.

In its role as President, the UK Government should use all its efforts to achieve agreement on a sugar reform package. The EU should not miss this opportunity for reform.

1 Introduction

1. The European Union's Common Market Organisation for Sugar, generally known as the sugar regime, has remained virtually unchanged since its establishment in 1968. It has survived various reforms of the Common Agricultural Policy (CAP), including the recent radical changes agreed in 2003, and several enlargements of the EU. It is one of the few remaining examples of a "classical" CAP support system, including minimum prices, import tariffs, export refunds and production quotas. The regime was last reviewed in 2001, when it was "rolled over" for another five years. The current sugar regime is due to expire on 30 June 2006. The background to the current regime is summarised in Annex 1 to our report.¹

2. The regime has attracted criticism, especially since the reforms of other aspects of the CAP in 2003, which meant that sugar regime is anomalous in its structure of high support prices, quotas and export refunds. Other drivers for reform include World Trade Organisation (WTO) negotiations, which aim to eliminate export subsidies and to significantly reduce import tariffs, thus diminishing the protection afforded to the EU's internal sugar market. Even while these negotiations are going on, however, elements of the existing regime have been declared illegal by the Appellate Body of the WTO, adding to the pressure for change.

3. In September 2003, the European Commission issued proposals for reforming the regime. Negotiations have continued ever since, and the Commission's latest legislative proposals were published on 22 June 2005. The Commission hopes that an agreement on these proposals will enhance the EU's negotiating position at the WTO Ministerial meeting in Hong Kong in December 2005 and increase the chances of an overall trade agreement.

Background to our inquiry

4. Our predecessor Committee reported on the Commission's 2003 proposals for reform in July 2004.² In that report, the Committee stated that reform was "inevitable and long overdue", and broadly supported the reform proposals. The report recommended a lower import tariff rate, significant reductions to the internal market price and the elimination of production quotas. The Committee also stressed that reform of the regime would help in bringing the Doha Round of the WTO negotiations to a successful conclusion.³

5. The UK, which currently holds the Presidency of the EU, has declared its ambition of reaching agreement on the Commission's proposals at the Agriculture Council on 22-24 November. The UK has stated:

1 See page 48

2 Environment, Food and Rural Affairs Committee, Twelfth Report of Session 2003-04, Reform of the Sugar Regime, HC 550-I, 10 July 2004 (<http://www.publications.parliament.uk/pa/cm200304/cmselect/cmenvfru/550/55002.htm>)

3 HC 550-I, paras 27, 33-35, 55

The EU's sugar regime is an important element of reform of the Common Agricultural Policy. We will want to achieve a consensus amongst partners on a market-based, liberalising reform. Reforms on these lines will strengthen our wider trade and development objectives, putting the EU in a better position to contribute to an ambitious outcome in the world trade talks.⁴

6. In turn, the Commission has stated that it hopes an agreed package will be ready to take with it to the WTO Ministerial meeting which starts in Hong Kong on 13 December 2005. The package forms part of a wider deal on agricultural support, which is a key element of the Doha round of the trade negotiations, which it is hoped will be completed in Hong Kong. For this reason, successful reform of the sugar regime is especially important.

Scope of our inquiry

7. We decided to undertake a brief inquiry into the Commission's new proposals as a follow-up to our predecessor Committee's report. It was not our intention to rehearse all the arguments from that earlier inquiry, but to examine the likely impact of the reformed regime on sugar producers and processors in the UK and the wider EU. Our aim was to see how, a year on, matters had progressed and how the Government's position had developed. For ease of comparison, we have summarised the Government's response to our predecessor Committee's report of 2004, and noted any change in the Government position since then, in the appropriate sections of this report.⁵

8. The very short timetable imposed on us by the need to report before the potentially crucial Council meeting on 22-24 November has meant that we have not been able to devote as much time as ideally we would have liked to the important issue of how the reforms will affect the African, Caribbean and Pacific (ACP) countries. However, we did receive written evidence from the ACP London Sugar Group, and raised the concerns of ACP countries with the responsible Defra Minister. We comment on this aspect of the reforms in part 8 of our report. We also intend to keep this aspect of the reforms under review and will return to the subject in the New Year, following the WTO meeting, when the final details of the development elements of the reform package are likely to be finalised. We also look forward to the report of the inquiry into the sugar regime of the Sub-Committee D of the House of Lords European Union Committee, due to be published in December 2005, which has focused to a much greater extent on the implications of the reforms for ACP countries.

9. We took oral evidence from representatives of Tate & Lyle Sugars Europe (hereinafter referred to simply as Tate & Lyle), the UK Industrial Sugar Users Group (UKISUG), the Dutch Beet Growers' Federation, the National Farmers' Union (NFU), British Sugar plc and Defra. We also benefited from informal meetings with Ms Joan Noble, an independent consultant on sugar issues⁶ and Mr Lars Hoelgaard, Deputy Director-General of the

4 UK Presidency Priorities, presented to the European Parliament 23 June 2005

5 Environment, Food and Rural Affairs Committee, Sixteenth Special Report of Session 2003-04, *Reform of the Sugar Regime: Government Reply to the Committee's Report*, HC 1129 (<http://www.publications.parliament.uk/pa/cm200304/cmselect/cmenvfru/1129/1129.pdf>)

6 We also received written evidence from Ms Noble (Ev 129)

European Commission's Agriculture and Rural Development Directorate General. Many organisations and individuals also submitted written evidence. We are grateful to all those who gave evidence or otherwise assisted our inquiry.

Some key issues

10. We took as our starting point the Commission's draft legislative proposals of June 2005, which are summarised in the next section (see paragraph 15). The evidence we received raised some potential problems with the Commission's proposals, which some witnesses believed the UK Government needed to address in its negotiations. The issues of particular concern to witnesses included:

- the extent of the proposed price cut
- grower compensation and the way it might be applied
- the disproportionate effect on the UK of merging 'A' and 'B' quota
- the agricultural and environmental impacts of the reforms
- the future viability of the processing and refining industries in the UK.

These issues are addressed in the subsequent sections of the report.

11. We were disappointed that, when the Minister for Sustainable Food and Farming gave evidence, he was so reluctant to confirm whether the issues that other witnesses had identified as being important would be raised by the UK Government in negotiations on the reform package. While we accept the problems that may arise in pursuing its national interests for the Member State that holds the EU Presidency, from the point of view of the growers, processors, refiners and environmentalists, it is important for them to be sure that concerns are being raised from a British standpoint. We return to the issue of the UK Government's role at the end of our report.

2 The Commission's proposals

12. The Commission's current reform package is the culmination of a series of proposals over the last two years, which we set out below.

Commission proposals of 2003 and 2004

13. In September 2003 the European Commission published an Options Paper for reform of the sugar regime. It set out three "possible policy orientations for the EU sugar regime" in order to stimulate debate⁷, as follows:

7 "Commission opens discussion to reform the EU sugar regime", European Commission press notice, IP/03/1286, 23 September 2003

1. An extension of the present regime beyond 2006: This would consist of keeping intact the current regime, based on flexible quotas and price intervention.

2. A reduction in the EU internal price: In this scenario, once the levels of imports and production had stabilised, production quotas would be phased out.

3. A complete liberalisation of the current regime: The domestic EU price support system would be abolished and production quotas would be abandoned.

Our predecessor Committee used the Commission's Options Paper as the basis for its inquiry.

POSITION AFTER 2004 EFRA COMMITTEE INQUIRY INTO REFORM OF THE SUGAR REGIME

In 2004, the Committee concluded that: "Reform of the EU sugar regime is inevitable and long overdue. The changes implemented must be sufficient to allow the Community to honour its existing and future international commitments. Reform of the sugar regime should be consistent with that undergone by other parts of the Common Agricultural Policy".

In its response, the Government said it agreed with this conclusion, noting that it had "consistently made clear that the existing regime is unsustainable in its current form" and that it had "always advocated that sugar reform should be in line with the successful CAP reforms agreed in June 2003".

Update: Nothing has changed: the Government acknowledges this remains its position.⁸

In 2004, the Committee indicated that its "preferred approach to reform" was "broadly consistent with the Commission's second option", in that it envisaged:

- the phasing out of the quota system;
- a reduction in the internal market price; and
- a lowering of the import tariff rate.

In its response, the Government agreed that "lower prices, lower import tariffs and the ending of quotas are all highly desirable objectives for this reform round".

Update: Defra states that it largely supports the Commission's position, as set out in the draft legislative proposals of June 2005, and notes that the representations made to it have done little to sway the Government from this course.⁹

14. On 14 July 2004, the Commission outlined a reform package, for further discussion.¹⁰ This proposed price cuts, mandatory sugar quota cuts, direct income support to growers, a quota transfer scheme and conversion aid for factory closures.

8 Q 265. See also para 16.

9 Q 269

10 Communication from the Commission to the Council and the European Parliament, accomplishing a sustainable agricultural model for Europe through the reformed CAP—sugar sector reform (COM(2004)499 final)

Draft legislative proposals of June 2005

15. The European Commission published draft legislative proposals for reform on 22 June 2005.¹¹ The details are as follows:

- A 39 percent price cut over two years beginning in 2006/07 to ensure sustainable market balance.
- Compensation to farmers at 60% of the price cut. Inclusion of this aid in the Single Farm Payment and linking of payments to respect of environmental and land management standards.
- Validity of the new regime, including extension of the sugar quota system, until 2014/15. There is no provision to review the regime during that period.
- Merging of 'A' and 'B' quota into a single production quota.
- Abolition of the intervention system and the replacement of the intervention price by a reference price.
- Introduction of a private storage system as a safety net in case the market price falls below the reference price.
- Voluntary restructuring scheme lasting four years for EU sugar factories, consisting of a high degressive payment (one that decreases by steps) to encourage factory closure and the renunciation of quota as well as to cope with the social and environmental impact of the restructuring process.
- This payment will be €730 per tonne in year one, falling to €625 in year two, €520 in year three and €420 in the final year.
- A top-up payment for beet producers affected by the closure of factories in the first year for which they have delivery rights.
- Both these payments will be financed by a degressive levy on holders of quota, lasting three years.
- Sugar beet should qualify for set-aside payments when grown as a non-food crop and also be eligible for the energy crop aid of €45 hectare.
- To maintain a certain production in the current 'C' sugar producing countries, an additional amount of one million tonnes will be made available against a one-off payment corresponding to the amount of restructuring aid per tonne in the first year.
- Sugar for the chemical and pharmaceutical industries and for the production of bio-ethanol will be excluded from production quotas.¹²

¹¹ European Commission, COM(2005) 263 final, *Proposal for a Council Regulation on the common organisation of the markets in the sugar sector* (http://www.europa.eu.int/comm/agriculture/capreform/sugar/prop_en.pdf)

The Commission underlined the fact that it was hoping for a political agreement on the proposals at the Agriculture Council meeting to be held 22–24 November 2005.

16. In evidence, Defra witnesses noted that the Commission’s legislative proposals were very much in line with our predecessor Committee’s findings, and were also close to the Government’s desire for “a market-based liberalising reform”, to bring sugar into line with other reformed CAP sectors, and to comply with the EU’s international obligations, particularly in respect of the WTO.¹³

3 Extent and timescale of the proposed price reductions

POSITION AFTER 2004 EFRA COMMITTEE INQUIRY INTO REFORM OF THE SUGAR REGIME

In 2004, the Committee concluded that, in managing the pace of reform, “it would not realistically be possible to move from such a highly managed market to a fully liberalised position in a single step”. “To allow the European Union sugar industry time to adapt to the proposed changes”, the Committee believed it was “desirable for the price reductions to be phased in over time”.

In its response, the Government accepted that a transitional period was “desirable for many sections of the industry, to allow them time to adapt”.

Update: The Commission’s proposals have laid out the extent and timescale of the price reductions that it believes are necessary to achieve a balanced market and the Government appears to agree with the Commission’s position.

The proposed price reduction

17. In presenting her draft legislative proposals, Commissioner Fischer Boel stated categorically that “there is no alternative to a profound reform ... The easy option would be to sit on my hands. But that would mean a slow and painful death for the European sugar sector”.¹⁴ The Commission’s proposals for price reductions are aimed at bringing the European market supply and demand into balance, while allowing additional room for imports from developing countries. The new proposed prices effectively lower the internal EU price of sugar from around three times the level in the world market to twice the level.¹⁵ The extent of these reductions is slightly more severe than had been envisaged by the Commission’s July 2004 communication, although plans for an initial mandatory quota cut were also dropped.

18. Opinions on the severity and timescale of the proposed price reductions were divided. Some witnesses thought the cuts were too severe, with insufficient time being allowed to adapt to the new market conditions. The International Confederation of European Beet

12 “Sugar Reform will offer EU producers long-term competitive future”, European Commission press notice, IP/05/776, 22 June 2005

13 Q 265

14 European Commission, Sugar Reform will offer EU producers long-term competitive future, Press notice IP/05/776, 22 June 2005

15 Ev 103 [Professor Sir John Marsh]; Q 292 [Defra]

Growers (CIBE) argued that “the price reductions go too far and come too quickly”, a sentiment echoed by the Dutch Beet Growers’ Federation (NBF).¹⁶ The NBF felt the Commission’s proposals, as they stood, would be a disaster for the Dutch industry and even for the best areas of EU sugar beet production.¹⁷ The National Farmers’ Union of England and Wales (NFU) also regarded the proposed price reductions as being “unnecessarily severe”, noting that Defra’s own analysis had suggested that the new guaranteed beet price would be insufficient to cover the costs of production of even the most efficient UK growers.¹⁸

19. The ACP London Sugar Group, which represents the interests of sugar cane producers in the African, Caribbean and Pacific countries, felt that “the price cut should not be larger than is strictly required by the outcome of the Doha Round” and argued that a decision on the extent and timing of the price cut should be deferred until after the completion of that round of trade negotiations.¹⁹ Reports from the October EU Farm Council suggested that agriculture ministers from 11 Member States had signed a letter demanding “a price cut less than the proposed 39%, with a longer implementation period than the planned two years”.²⁰

20. Other witnesses took an opposing view on the price reductions, arguing that the proposals did not go far enough. The Biscuit, Cake, Chocolate and Confectionery Association (BCCCA) described the draft legislative proposals as being “very modest”, fearing that the plans might be “too little, too late” for the sugar-using sector in the UK.²¹ The UK Industrial Sugar Users Group (UKISUG) stated that “the current gap between European and world prices has contributed to the loss of 16,000 jobs in the confectionery sector in the last five years”.²² The BCCCA also cited the high price of sugar in the EU as being an “important factor” in the loss of more than 20% of the workforce of its members, as production had shifted to areas of low sugar prices.²³ UKISUG were also concerned to ensure that sugar-containing products would continue to be manufactured in the UK, rather than being made abroad.²⁴

21. On the processing side, Tate & Lyle explained that “the absolute price level of the EU sugar market is not important to the processor or refiner” since it is “the difference between the institutionally fixed raw material purchase price and finished goods sale prices that establishes the margin available”.²⁵ But British Sugar was concerned about the proposed reduction in the minimum beet price, because of its requirement to source enough beet. If prices were driven down too low, then even the most efficient countries

16 Ev 106 [CIBE: *Confédération Internationale des Betteraviers Européens*]; Q 158 [NBF: *Nederlandse Bieten Federatie*]

17 Q 131

18 Ev 42, executive summary; Q 169

19 Ev 136, paras 13, 15

20 “Growing opposition as sugar reform deadline approaches”, *Agra Europe*, 28 October 2005, EP/4–6

21 Evs 22–23, paras 3, 10

22 Ev 20, para 1.1

23 Ev 22, para 2

24 Qq 85, 102

25 Ev 15, para 8

would struggle to get adequate beet supplies. On the other hand, if the price were left too high, then insufficient tonnage would be encouraged out in the restructuring scheme. This would make mandatory quota cuts inevitable, a prospect described by British Sugar as being “disastrous”.²⁶

22. British Sugar described “the key to success of the reform” as “getting the balance right between setting a price which drives as much of the inefficient production out” and “having a price high enough to provide the minimum beet price at a sufficiently high level to source all the beet”.²⁷ British Sugar argued that the price reductions as currently proposed by the Commission were “unnecessarily severe to meet the EU’s objectives”.²⁸ However, British Sugar witnesses were not prepared “or in a position to give” an indication of what they thought the new price should be.²⁹

23. When giving evidence to the Committee on 2 November 2005, the Secretary of State for Environment, Food and Rural Affairs, Margaret Beckett, underlined the Commission’s justification for the extent of the price cut. She said that if the EU had not made a sufficiently substantial price cut to rebalance the market in sugar by 2009, when the Least Developed Countries gained unlimited duty-free access under the ‘Everything But Arms’ initiative, then there would be a need for further reform. The Secretary of State warned that, if this was necessary, then there would be no opportunity of securing any further compensation to ease the burden of that additional change.³⁰

Our conclusions

24. Price cuts are an essential element in bringing the European sugar market into balance. We welcome the Commission’s approach, centring on price reductions and not quota cuts, as this was what the UK industry told us it preferred. A lower internal price for sugar will make the EU market less attractive, not only to the least efficient beet growers, but also to the least competitive sugar producing countries outside Europe. Setting the price low enough to drive out the inefficient producers, but still sufficiently high for the most efficient producers to prosper, is clearly the critical balance that will define the success of the reforms. We welcome the two year period for implementing the price reductions, as this should allow sufficient time for the European sugar industry to adapt to the proposed changes.

25. In the absence of a precise indication from the UK beet industry on what price levels it requires in order to survive, it is difficult to know whether the Commission’s proposals are too severe. It seems certain, though, that pressure will be applied in the negotiations, from other Member States, to dilute the price cuts significantly. If successful, these changes could leave the EU market with an unwanted surplus and

26 Q 233

27 Q 233

28 Q 233; Ev 60, para 4.2

29 Q 277

30 Environment, Food and Rural Affairs Committee, Minutes of Evidence, Wednesday 2 November 2005, *The work of Defra*, HC 642-i, Q 6

necessitate mandatory quota cuts in the future that would adversely affect even the most efficient parts of the beet industry. Therefore, the UK Government's negotiating position must be to support the Commission in minimising any dilution of the price cuts that have been proposed and at the same time ensuring that these proposals do not act adversely on the UK's farmers because of the UK's ratio of 'A' and 'B' sugar.

Other market measures

The intervention price

26. In addition to comments on the specific plans to set new institutional prices within the sugar regime, we also received evidence relating to other ways the market would be managed under the Commission's proposals. Numerous parties expressed concerns over the plans to replace the existing intervention price with a new reference price. British Sugar argued that the reference price mechanism would not work effectively, since experience in other sectors demonstrates that it will not put a definite floor in the market. British Sugar suggested that the intervention price should be retained in the initial years while the restructuring scheme was being implemented and until the EU market re-stabilised, to avoid the risk of "market collapse at worst and serious instability at best".³¹ The Food and Drink Federation (FDF) noted that "the existing reference price system for pigmeat does not work as an indicator of internal market prices", and also questioned whether the reference price system would offer "an effective floor to the internal market".³²

The production levy

27. The NFU was opposed to the retention of the production levy, in future to be called a production charge, which was originally introduced to finance the cost of the sale of quota sugar in excess of EU production. The NFU argued that, as the EU sugar trade balance would shift as a result of the reform, imports would significantly exceed exports of quota sugar, which meant that the production charge would become "unjustified and should be removed altogether".³³ However, the Commission proposals are designed to be "budget neutral",³⁴ and the Commission argues that the €12 per tonne production charge on quota sugar is necessary "to contribute to the financing of the expenditure occurring under the common organisation of the markets in the sugar sector".³⁵

The 'flexibility clause'

28. Another aspect of the proposals that the NFU criticised was the 'flexibility clause' that allows processors to negotiate a further 10% reduction in the price they pay growers for

31 Evs 60-61, paras 4.3, 4.5

32 Ev 101, p ara 4

33 Ev 43, para 1.6

34 Q 285

35 European Commission, COM(2005) 263 final, Proposal for a Council Regulation on the common organisation of the markets in the sugar sector, p 12

their sugar beet. The NFU noted that the rationale for this clause was to enable factories to remain viable in times of adverse market price conditions. However, it was unhappy about the lack of symmetry in the application of the clause, as it did not allow farmers to gain a share in the extra margin when the market price is higher than the reference price.³⁶ British Sugar, however, commented that the provision of the 10% reduction provision would make “little practical difference”, as processors would take “the entire hit” were market prices to fall significantly below the reference price.³⁷

Our conclusions

29. We share the concerns expressed to us about the operation of the reference price, for sugar which is intended to replace the intervention price. Defra should seek further assurances from the Commission that the reference price will provide an effective floor in the market before agreeing to its inclusion in the final reform package. While the retention of the production charge might seem unjustified, given that its original purpose will be superseded, we recognise the argument for its inclusion to help ensure the overall package is budget neutral. There does, however, appear to be little justification for the ‘flexibility clause’ as currently drafted. We therefore recommend that the proposals be amended to recognise the right of growers to benefit from a share in the extra margin when the market price is higher than the reference price.

Will manufacturers and consumers benefit from price reductions?

POSITION AFTER 2004 EFRA COMMITTEE INQUIRY INTO REFORM OF THE SUGAR REGIME

In 2004, the Committee sought increased competition within the UK sugar market and recommended that “the competition authorities conduct an investigation into the UK processing industry”, if the reform did not achieve this aim.

In its response, the Government said increasing competition would be a “major UK negotiating objective”. It also agreed that, if sufficient progress were not made, then “the competition authorities should consider the case for an investigation into the market”.

Update: The Government now wishes to “wait and see” if the reforms will result in a significant liberalisation of the internal market before considering whether to recommend a competition authority investigation into the UK sugar market.³⁸

30. The Commission has said that the reform will result in lower prices at farm and processor level which would normally feed through to lower prices on goods leaving the factory.³⁹ We tried to establish whether manufacturers and consumers would actually receive the full benefit of the significant cut proposed in the price. Initially the scheme will provide no price cuts. This is because under the proposals, the restructuring scheme will be funded by a levy on the holders of quota, lasting three years. This would have the effect of

36 Ev 44, para 1.7; Q 210

37 Ev 61, para 4.4

38 Q 313

39 Ev 82, para 9 [Defra]

delaying the transmission of any price reduction for the first three years of the reforms, as processors will in effect be paying the same price for their raw material, with the difference between the old and new lower price going into the restructuring ‘pot’.⁴⁰ The restructuring scheme could also have an impact on export refunds, which are currently used to make up the difference between world and EU prices. The BCCCA argued that, if these refunds were not calculated on the full reference price, but rather on that price net of the restructuring amount, it would significantly disadvantage manufacturers that export products containing sugar.⁴¹

31. Defra noted that, in the longer term, it was unlikely that the full extent of the 39% price cut would be reflected in the price of products containing sugar. This is because sugar tends to be one of many ingredients, and not necessarily the major one, in many foods.⁴² The UKISUG noted that sugar makes up a widely varying proportion of the factory costs of different products. For instance, sugar would typically make up 60% of the factory price of sugar confectionery, but only 40 per cent of a typical soft drink and only 10% of biscuits and cakes. Furthermore, because sugar is a smaller proportion of the overall purchase price to the consumer than it is to either the retailer or the manufacturer, reducing the price of sugar as an ingredient would reduce the retail price of products containing sugar, but not by the same amount.⁴³

32. Evidence differed as to whether the price cuts would be passed on, once the transitional period is over. The International Confederation of European Beet Growers (CIBE) claimed that the price reductions would be captured by manufacturers of sweets and soft drinks and by distributors.⁴⁴ The NFU told us:

Historical evidence suggests that sugar users are unlikely in the first instance to pass on the cost savings to their customers, instead pocketing the difference to increase their own margins.⁴⁵

33. British Sugar, while arguing (like the NFU) that in the past, price reductions in the EU sugar sector had not been passed on to the consumer, felt that in this case the price reductions were so dramatic that some element would be passed on.⁴⁶ The users of sugar all argued that the competitive nature of the market in which they worked meant that any price cuts which manufacturers received would be passed on, because of the pressure retailers would put on suppliers of products containing sugar.⁴⁷

34. The sugar users expressed concern about whether they would receive an appropriate level of price reduction from the processors in the first place. The UKISUG had “grave

40 Ev 82, para 8 [Defra]; Ev 129, para 2 [Joan Noble]; NFU, Q 182

41 Ev 23, para 11. See also Q 122.

42 Ev 82, para 10 [Defra]

43 Ev 35 [UKISUG]

44 Ev 107

45 Ev 45, para 2.1

46 Ev 61, para 6.1

47 See Ev 26, para 17 [Cadbury Schweppes]; Ev 23, para 13 [BCCCA]; Ev s 20-21, paras 2.4-2.8 [UKISUG] and Qq 101, 117

doubts” about the extent to which any reduction in the official sugar price would actually be reflected in the sugar market, because the reduction in the number of processors would increase the chances of “tacit collusion”. UKISUG defined this as arising from the structure of the sugar market, not from any individual culpable act: “because companies are not in the normal competitive environment, they do not have normal competitive opportunities, the price tends to lift upwards”.⁴⁸ According to UKISUG, the structural rigidity of the EU sugar market was the reason why the price of sugar in the UK was 10% higher than in the rest of Europe.⁴⁹ Our predecessor Committee noted that the high level of concentration in ownership and limited competition had made the sugar sector a focal point for the attention of anti-competition authorities, and recommended an investigation into the UK processing industry.⁵⁰

35. British Sugar denied that the reforms would lead to any reduction in competition among processors. Any concentration of processors would mean “many bigger producers encircling the UK”, with huge surpluses to sell. “On that basis we expect the level of competition in the UK market to increase ... the competitive stakes are increased, not reduced in any way, shape or form”.⁵¹ Both British Sugar and Tate & Lyle emphasized that there was no question of their engaging in any form of price fixing.⁵²

Our conclusions

36. We conclude that, given the highly competitive climate in which manufacturing operates, and the pressure which the large retailers can bring to bear on their suppliers, it is likely that consumers will benefit from some degree of price reduction in the medium to longer term. The Committee believes consumers should benefit in direct relation to the reduction in the sugar price. One of the key determinants of the size of this price reduction will be the extent to which the processors pass on the price reduction to sugar users. We expect the UK’s processors to pass on, to the fullest extent possible, the reduction in the sugar price. We recommend that the competition authorities be asked to investigate the UK processing industry if any evidence emerges that, as a result of over-concentration in the industry, this is not happening. A separate investigation should take into account the current inbuilt premium paid by sugar users in the UK compared to those in the rest of Europe. The export refund scheme should take into account the total market price in the early years of the regime which will include costs for restructuring and compensation.

48 Ev 20, paras 2.1-2.3, Q 95

49 Qq 82, 89

50 HC 550-I, para 51-52

51 Q 248

52 Qq 249 [British Sugar], 62 [Tate & Lyle]

4 Proposed arrangements for compensating EU producers

POSITION AFTER 2004 EFRA COMMITTEE INQUIRY INTO REFORM OF THE SUGAR REGIME

In 2004, the Committee recognised that some form of producer compensation will be required to help farmers adjust to the new market conditions. To minimise market distortion, the Committee felt these payments should be “fully decoupled from production activity, following the principles of the CAP reform agreed in 2003”.

In its response, the Government agreed that “any compensation should be fully decoupled as part of the Single Payment to farmers, which will start in other sectors from 2005”.

Update: The Government continues to support fully decoupled compensation.⁵³ The Commission’s proposals provide that growers should receive compensation of 60% of the estimated revenue loss from the institutional price reduction.

Grower compensation

‘Decoupling’ grower compensation

37. The centrepiece of the reorganised CAP introduced under the 2003 reforms is a single subsidy payment, made to all farms, but no longer connected to the production activity. This is known as the principle of ‘decoupling’. This decoupling—breaking the link between support and the production activity—is desirable on economic grounds, as it allows farmers greater freedom to make their own farming decisions. The Commission has proposed making ‘decoupled’ payments to sugar growers, to compensate them for the loss of income associated with the reduction in prices.

38. In agreeing the 2003 reforms, a compromise was reached which allowed individual Member States the option of retaining some element of coupling within their subsidy systems. Given this historic background, some witnesses were concerned that the option of ‘partial decoupling’ could find its way into the final sugar package as well. The NFU argued that there was a “serious risk” that partial decoupling might be included in the reforms. The NFU insisted that such a compromise in the Council of Ministers must be avoided at all costs.⁵⁴ Reports from the October EU Farm Council seemed to bear out these fears, with the suggestion that it had become increasingly probable that “any compromise reform paper put forward by the Commission in time for the November Council will include the option of partial decoupling for Member States who feel they are worst hit by the price”.⁵⁵

39. If a compromise package did allow Member States flexibility in maintaining an element of coupling with their payments, farmers in countries that exercised this option would be obliged to stay in beet production in order to qualify for the full compensation. Clearly, this

53 Q 269

54 Ev 46, para 4.1

55 “Growing opposition as sugar reform deadline approaches”, *Agra Europe*, 28 October 2005, EP/4–6

would fly in the face of the whole thrust of the reform, which is to ensure production is concentrated in the most efficient areas of the EU and not constrained by artificial policy instruments. Tying aid payments to the continued cultivation of sugar beet would also contradict the aims of the restructuring scheme, which is designed to decommission the most inefficient parts of Europe's sugar producing capacity.

40. Processors would benefit from coupled compensation as it would cushion the reduction in beet supply to factories after reform. In this context, it is interesting to note how British Sugar's thoughts on 'decoupling' have changed over time. In April 2004, it maintained that "compensation should be partly coupled to take account of the interdependent relationship between growers and processors".⁵⁶ But in written evidence to our current inquiry, it changed its stance, arguing against "any suggestion that partial coupling should be permitted at the discretion of individual Member States", since this would "introduce competitive distortions doing particular damage to the UK".⁵⁷

41. This change in British Sugar's approach may reflect an acknowledgement that, if discretion were allowed, the UK Government would choose full decoupling, as a matter of principle, while other countries might not, thereby putting processors in those countries at a competitive advantage. The fact that the Dutch Beet Growers' Federation seemed prepared to consider partial coupling, at least in the first few years of reform, shows the symbiotic nature of the relationship between sugar beet growers and processors.⁵⁸

42. Defra made its position clear, stating that it was "absolutely behind fully decoupled support" and indicating that it intended to implement the English payments in that form.⁵⁹ However, the Minister for Sustainable Farming and Food was initially somewhat reluctant to confirm that the UK would oppose any attempt to introduce the option of partial decoupling into a compromise package.⁶⁰ When pressed, Lord Bach did finally confirm that the UK would "argue pretty strongly for full decoupling".⁶¹

Our conclusions

43. Direct payments to growers must be fully decoupled from production, in order to minimise market distortion. We are pleased that Defra seems so committed to implementing direct payments to English farmers in a fully decoupled form.

44. The UK Government should strongly oppose any attempt to introduce the option of partial decoupling into a compromise package. Such a dilution of the original proposals could frustrate the success of the restructuring scheme and leave UK processors at a comparative disadvantage to processors in other parts of the EU.

56 Environment, Food and Rural Affairs Committee, Twelfth Report of Session 2003–04, *Reform of the Sugar Regime*, HC 550-II, Ev 4

57 Ev 62, para 8.3

58 Q 148

59 Qq 269, 305

60 Qq 297–298

61 Q 299

Application of grower compensation in England

45. Defra's RIA notes that, according to the Commission's paper, Member States would have two options for paying compensation: it could either be paid only to those farmers who have historically grown sugar beet; or to all those who receive the main Single Farm Payment on an area basis.⁶² Defra pointed out that the decision regarding the method of payment is linked to its rationale and duration. If the payment is 'compensation', it would seem reasonable to make the payment on a historic reference basis to growers of beet. However, if payments are made indefinitely, they cease to be 'compensation' and become simply 'support'.⁶³

46. Defra's model for implementing the Single Farm Payment (SFP), introduced under the 2003 CAP reforms, in England was complicated. It involved a combination of individual entitlements based on historic receipts and a flat-rate payment per hectare. Under this model, the individual historic receipts from existing schemes reduce over time, as the flat rate element increases. The proportions of the flat rate and historic elements are set out in Table 1.

Table 1: Proportions of flat rate and historic payment elements of the English SFP

Year	Proportion of flat rate element (%)	Proportion of historic element (%)
2005	10	90
2006	15	85
2007	30	70
2008	45	55
2009	60	40
2010	75	25
2011	90	10
2012	100	0

Source: *Official Report*, 12 February 2004, col 1586

47. Defra calculates in the RIA that incorporating the sugar payments into the existing transitional hybrid system would see their value to an English beet grower diminish to around £10 per hectare by 2012, effectively making the payments time-limited for beet growers.⁶⁴ This contrasts sharply with Defra's estimate of a payment of £400 per hectare if the compensation were paid only to beet growers, entirely on a historic basis.⁶⁵ The Tenant Farmers Association warned against this effect, arguing the importance of ensuring "that

62 Defra, *Partial RIA*, section 9.1.2

63 *Ibid.*

64 This situation is analogous to the experience of English dairy farmers, who will see the value of their dairy premium payments diminish over time, under Defra's CAP implementation model.

65 Defra, *Partial RIA*, section 9.1.2. See also Commission's draft legislative proposals, p 58

any compensation payable remains with sugar producers and does not become dissipated across all Single Farm Payment entitlement”.⁶⁶

48. The NFU suspected the UK Government might favour a transitional hybrid compensation system for sugar that would ultimately lead to a system of fully flat-rate payments.⁶⁷ The NFU is “actively exploring all possible options and outcomes with the aim of establishing a set of principles that will provide UK growers with maximum benefit for as long as possible”.⁶⁸ One such option could be to manage the integration of the sugar compensation into the general SFP, in such a way that the proportion of the historic component is even higher in the first few years of a transition. This would allow sugar growers in England to benefit more and longer from the direct payments.

49. Defra’s RIA does not provide a full analysis of the distributional effects and financial impact on English sugar growers of a move to a purely flat-rate system of payments. Such a lack of analysis, prior to the Government’s decisions in implementing the 2003 CAP reform, was strongly criticised by our predecessor Committee.⁶⁹ The Minister told us that as the proposals were still “under negotiation”, Defra would “not be in a position to take a final view of implementation until the overall package is agreed”.⁷⁰

Our conclusions

50. In deciding how to implement the grower compensation element of the proposals, the Government must balance diverse and sometimes conflicting policy objectives, which include compensation, income support and the provision of environmental benefits. It is vital that Defra conduct a full impact analysis before reaching its implementation decision. Whatever implementation method the Government decides on, it should not allow a system of ‘compensation’ to become simply ‘income support’ in the longer term, as such payments would neither compensate for price reductions nor induce any further compliance with environmental standards.

Level of compensation

51. The Commission proposes that growers should be compensated for 60% of the estimated revenue loss from the institutional price reduction.⁷¹ From 2007 onwards the total amount available for grower compensation will be almost €1.5 billion a year.⁷² This

66 Ev 99, para 11

67 Ev 47, para 4.8

68 Ev 47, para 4.9

69 Environment, Food and Rural Affairs Committee, Seventh Report of Session 2003–04, *Implementation of CAP Reform in the UK*, HC 226-I, para 11

70 Q 296

71 Moving from price policy to direct payments reduces deadweight losses and improves the efficiency of support, making full compensation unjustified.

72 European Commission, COM(2005) 263 final, Proposal for a Council Regulation amending Regulation (EC) No 1782/2003 establishing common rules for direct support schemes under the common agricultural policy and establishing certain support schemes for farmers, p 59

rather dwarfs the €40 million offer of accompanying measures for the ACP states in the first year of the reform.⁷³

52. We received differing views on whether the level of compensation to growers was adequate. Professor Sir John Marsh felt that a 60% rate of compensation might, in practice, be described as “over the top”.⁷⁴ However, the NBF called for a compensation level of “at least 80%” and cited rice as an example of a previously reformed sector that had received 88% compensation.⁷⁵ A more appropriate comparison might be made with the 50% compensation provided to arable farmers for the price reductions in the Agenda 2000 reforms. Indeed, the Commission’s own simulations, based on 50% compensation, forecast an average drop in income per beet holding of only 4%, with some growers being excessively compensated at this level.⁷⁶ Defra also drew attention to the potential ‘risk of overcompensation’ in its RIA, although this analysis overlooks the possible effect of diminishing levels of payments to beet growers, under a transitional hybrid compensation model.⁷⁷

53. Joan Noble noted that, in the Commission’s proposals, “there was no provision to allow a higher level of compensation to farmers in countries who have in the past been paid higher sugar beet prices than the common level”.⁷⁸ We will return to this point when covering the changes to the quota arrangements, later in this report (see paragraphs 60–65 below).

Our conclusions

54. We received insufficient evidence to show conclusively whether the 60% figure proposed by the Commission represented an appropriate level of compensation for beet growers. However, it does seem broadly consistent with reforms in other sectors. Defra’s RIA did not fully take into account the degressive nature of payments over time, as would be experienced by English sugar growers under an implementation model that moved to a purely flat-rate system. We call on the Government to carry out an urgent study to assess the long-term impact on growers of making payments on this basis.

The restructuring scheme

55. The Commission’s original 2004 plan for a compulsory cut in production quotas was replaced in the 2005 proposals by a voluntary scheme under which the Commission would buy up quota, known as the ‘restructuring scheme’. This is designed to lure inefficient sugar processors out of production and compensate for the closure of factories. The sugar

73 Ev 139, para 48

74 Ev 105, para 16

75 Qq 131, 148

76 European Commission, *Reforming the European Union’s sugar policy: Summary of impact assessment work*, (Brussels, 2003), p 30

77 Defra, *Partial RIA*, Box 7: The risk of overcompensation, pp 65–66

78 Ev 129, para 5

beet price will be reduced at a faster rate than the white sugar price, with the extra margin generated for the beet processor being paid into a restructuring fund to finance the claims being made by those producers relinquishing quota. The refiners are excluded from participation in the restructuring fund. Instead of paying money into the fund, like the beet processors, the refiners' extra margin will be paid to suppliers from the African, Caribbean and Pacific (ACP) countries and the least developed countries (LDCs), through a raw sugar price reduction which is slower and less severe than the cut in the minimum beet price.⁷⁹

56. Defra noted that if British Sugar closed and dismantled one or two factories and relinquished 200,000 tonnes of quota sugar in 2008/9, it could claim restructuring aid of around €100m, which it could use to reinvest in its other plants.⁸⁰ However, British Sugar assured us that, as long as the beet sector was not discriminated against in a compromise deal, then it was planning “to continue to operate” and not avail itself of the restructuring scheme, although it did not rule out the possibility of reducing the number of its factories.⁸¹

57. The sugar users were particularly critical of the restructuring scheme. The BCCCA argued that “the proposed restructuring fund is excessively generous, will delay price reductions and will mean that industrial users and consumers of sugar are paying to compensate private shareholders in other countries”.⁸² It noted that the restructuring fund would amount to “a sum in excess of €4bn to help the sugar industry” and suggested it was “worth at least €360,000 per sugar processing employee in the EU”.⁸³

Our conclusions

58. The UK's beet growers will not be directly affected by the restructuring scheme, as British Sugar has stated it plans to continue production of sugar, although it will mean that benefits to manufacturers and consumers in terms of price cuts will be delayed.

59. The Committee calls on the Government to clarify the position over the rights of producers to use quota in the event of British Sugar closing one or more of its existing plants and the redundant plant being operated by sugar beet farmers or another third party.

5 Changes to the quota arrangements

Disproportionate effect on UK of merging 'A' and 'B' quota

60. In an effort to simplify arrangements, the Commission proposes merging 'A' and 'B' quotas into one single quota. The distinction between 'A' and 'B' sugar stems from the origins of the market organisation in the 1960s, when the basic quota allocation was

79 Ev 14, para 6 [Tate & Lyle]

80 Defra, *Partial RIA*, section 5.2.14

81 Qq 213, 242

82 Ev 24, para 19

83 Ev 24, paras 18, 20

supplemented by an additional quantity of sugar, known as ‘B’ quota, intended for export and based on the market disposal potential of each Member State. Over time, however, this ‘B’ quota evolved to become part of the general production, and the export role initially assigned to ‘B’ quota was taken over by ‘C’ sugar. A price differential between ‘A’ and ‘B’ quota still remained because a higher levy was charged on the ‘B’ quota sugar beet to pay for the system of export refunds.

61. The UK imports more sugar than it produces, and is therefore known as a ‘deficit area’ within the sugar regime. This is due to its historic reliance on imports of sugar cane from its former colonies. These imports meant that, when it joined the EU, it received a small proportion of ‘B’ quota in comparison to its ‘A’ quota allocation. Consequently, if, as is intended, the Commission’s proposed price cuts are imposed on the merged quota, countries like the UK, with a smaller ‘B’ quota, will suffer some price disadvantage in comparison to other countries. As producer levies on ‘B’ quota are currently higher than those on ‘A’ quota, the abolition of the distinction between the two is financially advantageous to those countries with large ‘B’ quotas, such as France and Germany.

62. In giving evidence, Defra acknowledged that:

The present regime has a differential pricing structure that rewards ... Member States that are classed as deficit areas or deficit producers of sugar. The change is to abolish that distinction, to merge ‘A’ and ‘B’ quotas and have a new unified quota with a unified price. It follows that in changing from the one system to the other there is a differential impact.⁸⁴

63. The NFU estimates that UK growers are likely to face “an effective price cut of 2.3% over and above the 42.6% proposed by the Commission”. For this reason, the NFU has called on the Commission to “devise an alternative solution that is equitable, taking into account the differing proportion of ‘A’ and ‘B’ quota across the EU”.⁸⁵ British Sugar suggested that the comparative disadvantage to the UK could be compensated for in a commensurate increase in the amount allocated to the UK for grower compensation.⁸⁶ Taking this idea further, the NFU calculated that this envelope needed to be increased by an additional €14 million in 2007, if the UK were to receive fair an equitable treatment in comparison with the other EU Member States.⁸⁷

64. Defra noted that other Member States that are classed as deficit areas had also been making a similar case on behalf of their growers, and that this was “one of the issues that is under active discussion in the negotiations at the moment”.⁸⁸ Defra did, however, underline the fact that the Commission’s proposal are “designed to be budget neutral and

84 Q 287

85 Ev 44, para 1.10

86 Ev 62, para 9.3

87 Ev 46, paras 4.3–4.4 and Ev 50, appendix 2

88 Qq 284–285

the overall package for compensation has to be one that can be accommodated within the financial ceiling for agricultural expenditure”.⁸⁹

65. Joan Noble, an independent consultant, also pointed out another effect of the new quota arrangements that could disadvantage Member States, like the UK, that currently have a small ‘B’ quota. She noted that if future quota cuts were necessary, then they would most likely have an equal impact on all Member States whether they were in surplus or deficit.⁹⁰ This is despite existing provisions that recognise the deficit status of the UK by implementing any necessary quota cuts using a low reduction coefficient. This issue was also highlighted by the 11 dissenting countries that opposed the Commission’s proposals at the October Farm Council. They suggested that production cuts, if necessary, should be applied initially to regions with a surplus of production, rather than to all countries.⁹¹

Our conclusions

66. We are concerned about the unfair impact on the UK of applying the proposed price cut to the new unified quota. The Committee regards this as an important issue and we recommend that the UK Government negotiate for a change in the proposals, so that the UK’s status as a deficit country is adequately recognised in the compensation package. It would not be fair if the price cut for UK growers were amplified by an accident of history. An increase in the amount of compensation for the UK could go some way to reducing the disproportionately negative impact of the proposals on the UK beet sector. Since the proposals are designed to be budget neutral and contained within the financial ceiling for agricultural expenditure, such negotiations will require acceptance from surplus countries that their envelopes will have to be cut by an equivalent amount. Furthermore, if quota cuts are required in the future, they must be made on the current basis, so as not to further disadvantage the UK.

Legal ownership of additional quota

67. The Commission’s proposals envisage that “an additional amount of 1 million tonnes of quota shall be made available to current ‘C’ sugar producing Member States”.⁹² UK companies would have the right to 82,847 tonnes of that amount, with a one-off, per-tonne amount being charged, equal to the level of the restructuring aid in the first year.⁹³

68. The NFU raised some questions regarding the legal ownership of the production rights associated with this additional 82,847 tonnes of sugar quota. The NFU felt that the issue of

89 Q 285

90 Ev 130, para 12

91 “Growing opposition as sugar reform deadline approaches”, *Agra Europe*, 28 October 2005, EP/4–6

92 European Commission, COM(2005) 263 final, Proposal for a Council Regulation on the common organisation of the markets in the sugar sector, p 5

93 *Ibid.*, pp 5, 44

legal ownership would have to be clearly established, particularly if the Government sought to recover the costs of acquiring the additional quota from the processor or grower.⁹⁴

69. When asked about this issue, the Minister was unable to answer the question of whether sugar producers would take legal ownership of quotas they paid for. A Defra official confirmed that, under the existing regime, quotas were not owned but were allocated free of charge to processors, so the question of ‘ownership’ had not arisen before. He confirmed that the proposals envisaged that the processors would be the ones to pay, but admitted that the concept of a processor company paying to acquire new quota was “a novel idea” and there was no “actual legal doctrine on this at the moment”.⁹⁵

Further changes

Quota abolition

POSITION AFTER 2004 EFRA COMMITTEE INQUIRY INTO REFORM OF THE SUGAR REGIME

In 2004, the Committee advocated the phasing out of the quota system, arguing that “competition will be increased more by abolishing quotas than through any other policy change”.

In its response, the Government agreed the ending of quotas was a “highly desirable objective” and shared the analysis that the “current quota system gives rise to major issues of competition policy”. In 2004, the Secretary of State urged a “swifter end” to quotas.

Update: The Government’s ultimate aim remains the abolition of production quotas “in the long run”.⁹⁶

70. The Commission’s draft legislative proposals envisage that the system of supply control through quotas will remain intact until the expiry of the new regime in 2014/15. The inefficiencies of the quota system were much criticised by our predecessor Committee’s report into the EU sugar regime. The Committee summarised the problems associated with the quota system as follows:

Of all the components of the complex sugar regime, the system of production quotas does most to inhibit competition and efficiency. Due to the rigid division of sugar production into national quotas, sugar beet is grown in geographical areas that are climatically ill-suited for this type of agriculture. Production quotas also restrict the ability of the most efficient producers to expand, impose limits on the production of competing products and create barriers for new entrants. The removal of quotas would allow regional specialisation and the exploitation of comparative advantages within the single market. It would thus lead to increased efficiency in growing and producing sugar within Europe, as well as allowing other resources to move to more productive and competitive uses.⁹⁷

94 Evs 47-48, paras 5.8–5.13

95 Qq 308–310

96 Q 311

97 Environment, Food and Rural Affairs Committee, Twelfth Report of Session 2003–04, *Reform of the Sugar Regime*, HC 550-I, para 34

71. The Government's response to that report noted that the Secretary of State had urged "a swifter end to quotas" at the Agriculture Council in 2004.⁹⁸ It also pointed out that the Commission's plans, as contained in the consultation paper of July 2004, "do not envisage the abolition of quotas during the initial phase of reform from 2005–08".⁹⁹ Reference here to an "initial phase" of reform alludes to the original proposal for a mid-term review of the sugar regime in 2008, which was dropped from the Commission's draft legislative proposals, published in June 2005.

72. The Minister told us that the Government's ultimate aim remained the abolition of production quotas, despite there being no provision in the draft legislative proposals for their abolition. He said: "we share the view as a Government that your Committee ... expressed last July, which is that in the long run certainly we would be better off without a quota system at all with this particular commodity".¹⁰⁰

Cross border quota transfers

73. Several witnesses expressed regret that the idea floated in the Commission's communication of July 2004, that quota might be bought and sold by sugar processing companies across national borders, had been dropped. Joan Noble, UKISUG and the NFU were all united in supporting the concept of cross border transfers, so as to allow greater flexibility of the redistribution of production quota in the longer term.¹⁰¹

Our conclusions

74. We are disappointed that the Commission's reform proposals did not include the lifting of quota restrictions as a long-term objective, given the distortions caused by the existing system. We therefore recommend that the Government pursue the abolition of quota restrictions. While quotas do still exist, we believe that transferability between Member States would aid the relocation of sugar production from the least competitive sugar producing regions to the most competitive. The swift establishment of legal certainty on the issue of quota ownership, as well as being desirable in itself, would help facilitate future cross border trade in quotas.

75. The UK Government should negotiate for the reinstatement of the mid-term review clause in the final reform package, as this would provide an opportunity to revisit these important issues. Failure to secure such a clause could lock into the new regime all the distortions of the quota system for another 10 years.

98 Environment, Food and Rural Affairs Committee, Sixteenth Special Report of Session 2003–04, *Reform of the Sugar Regime: Government Reply to the Committee's Report*, HC 1129, p 4. Reports from the Council meeting in November 2004 also suggest that "the UK called into question the long-term viability of quotas". ("Hardliners take initiative over EU sugar reform", *Agra Europe*, 26 November 2006, EP/3–4)

99 HC 1129, p 6

100 Q 311

101 See: Ev 130, para 10; Ev 21, para 4.1; Q 84; Q 172.

6 Implications for agriculture and the environment

76. This section of our report is principally concerned with the impact of the reforms within the UK. However, we also discuss some environmental issues relevant to the rest of the EU, and further afield.

Agriculture

77. In the UK, sugar beet accounts for about 1.5% of agricultural land and for some 2% of gross agricultural output.¹⁰² Around 7,200 farmers contract with British Sugar each year to provide around nine million tonnes of sugar beet, which is grown on around 170,000 hectares. Production is concentrated in the east of England, with 30% located in Norfolk.¹⁰³

78. British Sugar noted that, geographically, the UK is in one of the best areas of Europe to produce beet.¹⁰⁴ The NFU described its growers as being in the top three or four most efficient producers in Europe and suggested that the reforms were likely to increase that efficiency still further.¹⁰⁵

79. The NFU explained that the effects of the proposed reform would include a “material reduction in the area of beet grown in the UK” and a “reduction in the number of holdings on which sugar beet is grown”.¹⁰⁶ Even if the UK continued to produce up to its quota limits, the NFU still envisaged a reduction in labour associated with beet production. If beet became completely unviable, then about 15,000–18,000 jobs would disappear across the whole of the beet industry.¹⁰⁷ Defra’s RIA noted that, under the reforms, “UK beet sugar production is almost certain to fall, yet by how much is difficult to say”.¹⁰⁸ However, the Minister was resolute in the belief “that the British beet industry will survive these reforms”.¹⁰⁹

80. Several witnesses noted the importance of sugar beet as part of an arable rotation, breaking up continuous cropping of cereals and serving a useful role in managing weeds and fertility.¹¹⁰ The NFU described the results of a survey of its members that suggested around 80% of respondents would grow either oilseed rape or winter wheat if sugar beet

102 Ev 105, para 12 [Professor Sir John Marsh]

103 Defra, *Partial RIA*, section 3.1.1

104 Q 254

105 Qq 159–161

106 Ev 42, executive summary

107 Q 203 [NFU]

108 Defra, *Partial RIA*, section 5.2.5

109 Q 292

110 Q 170 [NFU]; Ev 124, para 12 [Agricultural Industries Confederation]

became unviable.¹¹¹ It was particularly concerned that a large-scale shift in land use away from beet could destabilise the markets that exist in those alternative commodities.¹¹²

81. Tom Meikle, a sugar beet farmer from Worcestershire, was keen to draw attention to the danger of basing estimates of the reduction in beet production solely on the relative profitability of alternative crops. He described how there was a yield reduction in the crop that followed sugar beet, due to the “late harvest and the impact of the large harvest machinery used in winter conditions”. This was in contrast to alternative crops, such as beans, oilseed rape and peas, which enhanced the yield potential of the next crop.¹¹³

82. Defra’s RIA noted that the agricultural impact of reform could be tempered if the processors decided that, in order to safeguard an adequate beet supply to its factories, it would pay an additional premium to UK growers, above the EU minimum.¹¹⁴ The NFU believed this would be necessary to keep its growers in business and pointed out that British Sugar’s current profits of about £18 per tonne were £1 per tonne more than the minimum grower price proposed by the Commission.¹¹⁵ The NFU concluded that “to maintain production”, British Sugar would have to “share some of their additional processing margin with the grower”.¹¹⁶

83. British Sugar acknowledged that securing beet supplies was “a key critical issue” and that, under the proposed price, even the most efficient countries, like the UK, would struggle to get adequate beet supplies.¹¹⁷ When pressed on whether this meant it would have to pay a premium, British Sugar responded by saying that “any premium that is paid over and above the minimum beet price is potentially a distortion of competitiveness of the UK industry as a whole”.¹¹⁸

84. The NFU’s evidence also referred to an “imbalance” in the relationship between the single private sector monopoly processor and the diverse grower base.¹¹⁹ It acknowledged the interdependency of that relationship, before calling for a “genuine partnership as we move forward to make sure that the balance of power is equal and the rewards and, equally, the risks are shared a little bit more”.¹²⁰ The Minister noted that the role of the Government was largely in “holding the ring” between the growers and the processors and not to “lay down what the relationship should actually be”.¹²¹ Defra is working towards a new Inter-Professional Agreement between the growers and processors, and as part of this process

111 Q 170

112 *Ibid.*

113 Ev 127, para 2

114 Defra, *Partial RIA*, section 5.2.5

115 Ev 49, paras 6.13, 6.17

116 Ev 49, para 6.17

117 Qq 231, 233

118 Q 225

119 Ev 49, para 6.9

120 Q 210

121 Q 307

the Government will seek new terms that provide for “a proper balance between the parties”.¹²²

Our conclusions

85. The UK Government should ensure that the final reform package allows the UK’s sugar beet industry to exploit its position of relatively high efficiency. It is important that no distortions are allowed into a compromise deal that could discriminate against the UK beet sector.

86. We note the interdependent relationship between the growers and the processors and recommend that Defra work closely with both parties in ensuring that a proper balance between them is achieved in the post-reform era. As British Sugar works so closely with UK farmers, we recommend that it looks at whether it can share some of its processing margin with the beet growers to ensure continuity of beet supply.

Bioethanol and biomass

Bioethanol

87. Cane sugar has long been used in Brazil, which is the world’s largest producer of sugar-based bioethanol, followed by the US. Our predecessor Committee noted the potential for UK-grown sugar beet to provide a feedstock for the production of bioethanol.¹²³ Some evidence to our inquiry also raised this issue. For instance, the Tenant Farmers Association argued that the production of bioethanol from sugar beet, for mixing with oil-based fuels, was a significant area which should be exploited.¹²⁴

88. Others were less convinced that beet sugar would be an appropriate feedstock for conversion into bioethanol. NFU witnesses were “bullish” about bioethanol in principle, but thought that, although there might be an opportunity for using some sugar as feedstock, in UK conditions wheat would be the better crop to use.¹²⁵ In evidence to an earlier inquiry, British Sugar suggested that sugar beet as well as wheat, could be used as a feedstock for bioethanol.¹²⁶ However, despite putting in a planning application for a plant near Kings Lynn that would process sugar beet for bioethanol,¹²⁷ British Sugar stated in written evidence:

Reform of the EU sugar regime should not be seen as providing a significant source of beet sugar feedstock for an emerging bioethanol industry. The volumes that can be

¹²² *Ibid.*

¹²³ HC 550-I, para 49

¹²⁴ Ev 99, para 8; see also Professor Sir John Marsh, Ev 106, para 26

¹²⁵ Q 205

¹²⁶ Environment, Food and Rural Affairs Committee, Seventeenth Report of Session 2002–03, *Biofuels*, HC 929-II, Ev 10

¹²⁷ Official Report, 16 March 2005, col 256W

produced from sugar will be small and significant bioethanol volumes will only come from cereals.¹²⁸

WWF told us that deriving alcohol from beet was not as efficient as the use of agricultural or forestry biomass for direct heat and power production, or of bioethanol derived from sugar cane.¹²⁹

89. The representative of the Dutch Beet Growers' Federation argued that, rather than EU growers seeking to provide feedstock for biofuel production, the least developed countries should be encouraged to do so.¹³⁰ The Development Committee of the European Parliament made a similar point in its report on the proposals:

Bio-ethanol production forms an interesting alternative to sugar production for food purposes and can assist ACP countries in meeting their energy needs, while protecting the environment, making them less dependent on imports and supporting rural livelihoods, and should therefore be mentioned as a key solution.¹³¹

90. The land on which beet is currently grown is not the only resource within the UK sugar industry that might be used for the production of biofuels. Joan Noble argued that there should be scope for those factories which will cease production of sugar under the reforms to convert to biofuel production. "It would be sensible to allow for some form of incentive to encourage the production of biofuels ... from any crop product". She wondered if there was any 'joined up thinking' between the Agriculture and Environment directorates-general of the Commission on this issue.¹³²

Biomass

91. There is more to energy crops than growing sugar beet, or cereals, for the production of bioethanol. Our predecessor Committee, in its report on climate change, noted the potential for greater production of non-food crops within the UK. The Committee noted support for using the new Single Farm Payment scheme introduced under the 2003 reforms of the CAP as a way of encouraging production of biomass crops to be used as an energy source, and encouraged the Government to investigate ways in which the CAP could be used to promote biomass and biofuel production.¹³³ The recent report of the Biomass Task Force has further highlighted the potential for growing more energy crops.¹³⁴ Evidence from WWF, noted in para 87 above, argued that bioethanol production from beet was less efficient than biomass production.

128 Ev 61, para 7.4

129 Ev 114, para 2.11

130 Q 156

131 Report from the Committee on Development, 30 September 2005, A6-0281/2005

132 Ev 132, paras 29–30

133 Environment, Food and Rural Affairs Committee, Ninth Report of Session 2004-05, *Climate Change: looking forward*, HC 130-I, paras 145-46

134 Biomass Task Force, Report to Government, October 2005, executive summary

Our conclusions

92. We are disappointed, on behalf of sugar beet growers, that British Sugar appears to have changed its position, and now regards wheat as being the best source of bioethanol in the UK. We suggest that British Sugar reconsiders its position on the viability of producing bioethanol from sugar beet. Efforts should also be made to explore the feasibility of converting redundant sugar processing factories to the manufacture of biofuels, thus encouraging the increased production of renewable transport fuels.

93. We also support the European Parliament Development Committee’s proposal that bioethanol production should be encouraged in the ACP countries, as this could help support the viability of some ACP countries’ sugar industries, given the increasing worldwide demand for bioethanol.

94. As the Committee has said before, more needs to be done to develop biomass for energy production. We hope that beet growers seeking an alternative crop, following reform of the sugar regime, will consider the potential of energy crops where these are viable on the land in question. The Government, in implementing the reforms in the UK, should ensure incentives (including those referred to in our predecessor Committee’s reports on biofuels) are in place to encourage this kind of diversification.

Environmental impact of sugar production

95. Our predecessor Committee noted that the evidence it had received on the environmental impacts of the current, and proposed, sugar regimes was “sometimes conflicting and largely inconclusive”.¹³⁵ We have had a similar experience in our own inquiry. However, we have sought to identify some general conclusions about the impact of sugar production in the UK, the rest of the EU, and in other countries, drawing on evidence received, and the extensive section on environmental issues in Defra’s partial Regulatory Impact Assessment.¹³⁶

Beet

96. Beet growing occupies less than 2% of crops and grass land in England, according to Defra.¹³⁷ However, it is regarded as having some important environmental benefits. Beet can provide habitats for ground-nesting birds, such as lapwing, skylark and stone-curlew, and the broadleaved weeds associated with it are important for farmland birds as they have more invertebrates associated with them, and they tend to produce seeds more readily used by birds, in comparison with grass weeds. Over-wintering geese also benefit from sugar beet fields.¹³⁸ Because sugar beet is spring-sown, it allows over-wintered stubbles to be left on light land before planting, which can benefit all farmland birds.¹³⁹ Witnesses argued that

135 HC 550-I, para 49

136 We have also noted the criticisms of the RIA brought to our attention in evidence submitted by British Sugar and the NFU. See Ev 59 and Ev 42

137 Defra, *Partial RIA*, section 7.1

138 Ev 127, para 19 [RSPB]; Defra, *Partial RIA*, section 7.1.1

139 Ev 128, para 1 [Tom Meikle]

reforms which led to a reduction in sugar beet production could adversely affect these biodiversity benefits, as farmers would instead grow crops such as wheat, oilseed rape or field vegetables.¹⁴⁰

97. In some parts of the EU, such as Spain and northern Italy, beet is heavily irrigated, essentially because it is grown in areas which are not inherently suitable for its cultivation. The RSPB criticised the irrigation of sugar beet in areas of Southern Europe, arguing that it was one of the crops responsible for directing water away from important wetlands.¹⁴¹ Brooms Barn Research Station noted that, on the other hand, only about 5% of beet crops in the UK are irrigated, and that the amount of water used for sugar beet in England was much less than that used on sugar cane in the tropics and sub-tropics.¹⁴² The RSPB also claimed that sugar beet cultivation in southern Europe required intensive levels of chemical inputs,¹⁴³ but we heard evidence that beet is grown in the UK with comparatively small amounts of pesticide and artificial fertiliser, and that no water quality problems arise in UK sugar beet production.¹⁴⁴

98. The RSPB noted the potential negative impacts of reform on biodiversity, but argued these were not sufficient to “dilute” the reforms. Instead, it argued that they should be addressed through the Environmental Stewardship element of the CAP. An example of this kind of approach is the RSPB’s proposed scheme within the Higher Level Stewardship element of the CAP to encourage farmers in North Norfolk to continue to make provision for the internationally important population of pink-footed geese there.¹⁴⁵ Defra’s RIA also argues that such schemes could encourage alternative crops (including non-sugar beets) as a means of retaining biodiversity and other benefits. The additional cost incurred would be small relative to current market support expenditure, and would be buying a public good, rather than creating market distortions.¹⁴⁶

Cane

99. Sugar cane is seen by many commentators as having had a damaging effect on habitats. WWF argues that “it is quite likely that the production of sugar cane has caused a greater loss of biodiversity on the planet than any other single crop”.¹⁴⁷ The partial RIA notes that habitat loss resulting from clearances affects biodiversity negatively, as do large monocultures, and in general, sugar cane does not offer the same attractions for birds as does sugar beet.¹⁴⁸

140 Ev 129, para 4 [Tom Meikle]; Ev 125, [RSPB]

141 Ev 126, para 15 [RSPB]

142 Ev 119 [Brooms Barn Research Station]

143 Ev 126, para 15 [RSPB]

144 Q 211 [NFU]; Ev 128, para 1 [Tom Meikle]; Ev 120 [Brooms Barn Research Station]

145 Ev 127, paras 21-23

146 Defra, *Partial RIA*, section 7.5

147 WWF, *Sugar and the environment: encouraging better management practices in sugar production and processing*, <http://www.panda.org./downloads/trash/sugarandtheenvironmentwwfreportnov2004.pdf>

148 Defra, *Partial RIA*, section 7.4.1

100. There is particular concern at the damage caused in Brazil by extensive cultivation of sugar cane, which has led to the destruction of tropical rainforests and other habitats.¹⁴⁹ Sugar cane currently accounts for 9% of the 60million hectares of cropped area in Brazil.¹⁵⁰ It has been argued that a reform which leads to increased production of cane sugar in Brazil, at the expense of cane in ACP and LDC countries, and beet in the EU, would lead to further destruction of such habitats. Defra's Partial RIA argues that further expansion of cane would not be at the expense of pristine rainforest, as the main cane-growing areas are in the coastal north-east and in the south, several hundred miles from the rainforest regions. Expansion of production would be more likely in the savannah areas. British Sugar cited research that ecosystems such as the Pantanal wetlands and the Cerrado savannah could be under threat.¹⁵¹ The RIA also argues that a much more significant driver of increased production of cane sugar in Brazil than reform of the EU regime will be the growing demand for bioethanol.¹⁵²

"Food miles"

101. Some commentators have raised the issue of "food miles" in relation to sugar, i.e. the environmental costs of transporting beet and refined or processed sugar. The Partial RIA notes the difficulty of drawing conclusions about the "food miles" associated with different forms of sugar production, suggesting that "many assumptions are required to quantify the comparison". Although the replacement of many short trips of beet-laden goods vehicles on UK roads by a few very long journeys of large bulk ships could well reduce the overall external costs resulting from sugar transport, raw cane may be transported by road to local crushing mills in supplying countries. Therefore an increase in raw cane production could worsen congestion or air pollution in those countries.¹⁵³ The WWF has made similar points.¹⁵⁴

Our conclusions

102. We have found it difficult to draw detailed conclusions about the comparative environmental impacts of different kinds of sugar production in different areas of the world. However, it is clear to us that the UK and the other EU Member States must pay particular attention to the important issue of the environment when considering how to reform and retain a viable European sugar sector. Brazil's questionable track record relating to the environmental impact of its agricultural expansion should be fully weighed in this regard.

149 See supplementary written evidence from RSPB to our predecessor Committee's inquiry [Environment, Food and Rural Affairs Committee, Twelfth Report of Session 2003–04, *Reform of the Sugar Regime*, HC 550-II, Ev 76–77]; Ev 61, para 7.5 [British Sugar]

150 Defra, *Partial RIA*, section 7.4.2

151 Ev 61, para 7.5

152 Defra, *Partial RIA*, section 7.4.2, p 108

153 Defra, *Partial RIA*, section 7.2.1

154 See WWF, *Sugar and the environment: encouraging better management practices in sugar production and processing*, <http://www.panda.org/downloads/trash/sugarandtheenvironmentwwfreportnov2004.pdf>

103. As far as the UK is concerned, we recognise the benefits in terms of biodiversity provided by beet growing. But we believe that these benefits should be secured, and funded, through targeted agri-environmental programmes under the CAP. We therefore recommend that the Government ensure sugar beet farmers have access to appropriate environmental stewardship schemes under the reformed CAP, thus enabling them to continue to provide environmental benefits on their land. In this way, public funding would be used to provide a public good—enhanced biodiversity—rather than to support an outdated element of the CAP.

7 Impact on UK-based processors and refiners

Impact of proposals on UK processing

104. British Sugar is the sole beet processing business in the UK, producing around 1.4 million tonnes of white sugar each year. British Sugar told us it “broadly supports” the Commission’s proposals, which it acknowledged would reduce its annual profits by more than £40 million.¹⁵⁵ However, it thought cost reductions and exploiting new revenue opportunities, including the processing of cane raws, could mitigate this effect.¹⁵⁶

105. British Sugar has rationalised its operations over the last 20 years, reducing the number of factories from 17 to six and quadrupling its productivity through the investment of over £1 billion.¹⁵⁷ It did not rule out the possibility of closing more of its factories, although it stated that it was not planning on entering into the proposed restructuring scheme under which it would receive compensation for such closures.¹⁵⁸

Impact of proposals on UK refiners

106. Around 70% of the raw cane sugar imported into the EU is refined in the UK by Tate & Lyle at its Silvertown refinery in east London. It is the largest refinery in the world, producing around 1.1 million tonnes of white sugar annually.

107. Tate & Lyle argued that the proposals, as they stood, would “seriously threaten the viability” of its refinery operation and put at risk the 3,500 jobs associated with its factory.¹⁵⁹ It also claimed that, as a result of the reforms, its annual operating profits would be cut by £85 million, making it significantly worse off than it would be in a totally deregulated market.¹⁶⁰

155 Ev 59, para 1.2; Q 215

156 “Publication of the European Commission’s proposals for the reform of the EU sugar regime”, Associated British Foods plc press notice, 22 June 2005

157 Q 215

158 Qq 242, 213

159 Ev 1, para 8; Q 15

160 “EU sector reform—potential impact”, Tate & Lyle plc press notice, 23 June 2005; Ev 1, para 8

Balance between beet and cane interests

POSITION AFTER 2004 EFRA COMMITTEE INQUIRY INTO REFORM OF THE SUGAR REGIME

In 2004, the Committee felt that ways had to be found to ensure the cane refining sector was not put at an unfair disadvantage during an interim period when preferential suppliers were adapting to the reform.

In its response, the Government said it would “continue to make the case for fair terms of competition between all operators”.

Update: The Government says it must remain impartial about issues that concern both the sugar beet industry and the sugar cane industry.¹⁶¹

108. The commercial rivalry between British Sugar and Tate & Lyle was apparent from differing evidence we received from them on whether the Commission’s proposals represented a fair balance between the beet and cane interests.¹⁶² Tate & Lyle argued that the reforms would “reduce the cane refining margin by significantly more than the beet processors’ margin”.¹⁶³ British Sugar, however, argued that the burden in cutting production surpluses rested solely with beet sugar sector.¹⁶⁴ It also felt that moves to offer more assistance to cane refiners than was already included in the Commission’s proposals “would be unjustified and would risk severely upsetting the cane/beet balance in the sugar regime”.¹⁶⁵

109. Defra confirmed that it had also received representations from both parties, but told us that it had to “remain impartial about issues that concern both the sugar beet industry and the sugar cane industry”.¹⁶⁶ Tate & Lyle hoped that Defra would follow “the guiding principle which has consistently been used by successive UK Governments in policy formulation”, which was “to ensure the regime permits equitable terms of competition between the beet and cane sectors”.¹⁶⁷

Restrictions on beet factories processing cane

110. One of the issues of contention in the proposals surrounds the protection they would afford to refiners. For the first three years, the import quotas will be allocated entirely to them. Thereafter, the refiners will have initial rights to the quota for the first three months of each marketing year. British Sugar argued that this represented “a major concession to current EU cane refiners”.¹⁶⁸ It suggested that, in the absence of these restrictions, its beet factories could refine sugar cane “highly efficiently”, thus offering “a credible alternative

161 Q 278

162 In addition to the original memoranda from British Sugar and Tate & Lyle, we also received two separate supplementary submissions (see Ev 73, Ev 13, Ev 140 and Ev 142). The main points are summarised in the table in Annex 2 to our report.

163 Ev 2, para 16

164 Q 219

165 Ev 60, para 1.9

166 Qq 274, 278

167 Ev 2, para 15

168 Ev 63, para 10.4

gateway for developing country raw sugar exports to the EU”.¹⁶⁹ British Sugar also claimed that it would be against the interests of the ACP suppliers to be restricted to just one outlet for their sugar cane.¹⁷⁰ Tate & Lyle responded to these suggestions by arguing that it was essential for it to have a guaranteed “base quantity” of cane to keep its refineries going through the period of reform.¹⁷¹ It also thought it would be unfair if beet processors across Europe were able to use the profits earned from their beet margin as a cross subsidy in attempting to compete with Tate & Lyle for its supply of raw sugar.¹⁷²

Refining aid

111. The existing sugar regime includes refining aid payments which are intended to equalise conditions of competition between refineries processing exclusively cane sugar and factories producing beet sugar. This aid, currently paid to refiners at a rate of €29.2 per tonne of white sugar equivalent, was introduced in 1986 to compensate for the difference in margins that had appeared between refineries and beet processors. The Commission’s new proposals plan to abolish refining aid from 2007/08 onwards.

112. Tate & Lyle’s analysis suggested that the combination of changes to the price structure and the abolition of refining aid would reduce its margin to €44 per tonne of sugar. It argued that this would compare with a margin of €100 to €110 in a completely deregulated market. “If the refiners’ margin were to be cut by the same amount as the beet processor’s margin this would result in a margin of €106”.¹⁷³ Tate & Lyle concluded that “a corrective mechanism package of the value of circa €60 per tonne is the only solution to fix this distortion”.¹⁷⁴

113. British Sugar argued in turn that any concession, in the form of some element of refining aid or other assistance for current cane refiners, would “severely upset the cane/beet balance and should be strongly resisted”.¹⁷⁵ It went on to say that “the refining margin afforded by the Commission’s proposals as they stand would be more than adequate to give returns competitive with those in the beet processing sector”.¹⁷⁶

114. Defra appeared to side with Tate & Lyle’s position in its RIA, stating that “the abolition of refining aid in the Commission’s proposal means that the institutional refining margin will be squeezed by a significantly greater proportion than the beet processing”.¹⁷⁷ Defra concluded by saying that “whilst it should not be the objective of a liberalising

169 Ev 63, para 10.2

170 Ev 63, para 10.3; Ev 74, para 3

171 Q 1

172 Qq 5, 48. Tate & Lyle’s argument centres on the potential for beet processors to cover their fixed costs with the profits from beet, and then compete for supplies of raw cane sugar with the comparative advantage of a lower cost base.

173 Ev 13

174 *Ibid.*

175 Ev 63, para 10.4

176 *Ibid.*

177 Defra, *Partial RIA*, section 9.3, p 117

reform to engineer specific outcomes there appears to be little economic justification for differential treatment between beet and cane”.¹⁷⁸

115. The independent sugar experts that submitted evidence to the inquiry also seemed to accept that the refining sector had been unfairly treated in the Commission’s proposals. Professor Sir John Marsh said that “sugar refiners seem to be particularly penalised”.¹⁷⁹ Joan Noble also noted that since adjustment aid had been deemed necessary under the current regime because of the difference in margins between sugar beet producers and cane refiners, now that this difference was likely to increase further, “it seems incongruous to abandon refining aids at this juncture”.¹⁸⁰

Our conclusions

116. The Government must negotiate to ensure equitable terms of competition between the cane and beet sectors in the UK. On the balance of evidence received, we conclude that the cane sector is unduly disadvantaged by the proposals as they currently stand.

117. We were concerned to establish what would be in the best interests of the ACP suppliers. On balance, we thought the continued viability of Tate & Lyle refining operations would be better for them. Therefore, we accept that the proposals to restrict beet processors from refining cane are necessary in the interim period while the ACP suppliers are adapting to reform. We are also sympathetic to the suggestion of retaining some form of refining aid. However, funds for this corrective mechanism would have to be deducted from the package of support for the beet industry in order for the reforms to remain budget neutral.

8 Impact on the ACP countries

POSITION AFTER 2004 EFRA COMMITTEE INQUIRY INTO REFORM OF THE SUGAR REGIME

In 2004, the Committee said that, “in recognising the potential losses to ACP countries resulting from reform, we believe that transitional aid programmes should be set up to assist their economies in diversifying away from dependency upon a European Union commodity regime that has lost its legitimacy”.

In its response, the Government agreed with this recommendation, saying that it had “always stressed the need to take account of the concerns of the current ACP beneficiaries”. It also noted that transitional support would be required, “in some cases to make their sugar industry more efficient, in others to assist the diversification out of sugar”.

Update: The Government says “there is no long-term interest for all ACP countries to necessarily carry on with sugar production provided they are assisted and helped to move into other industries”.¹⁸¹

178 *Ibid.*, p 118

179 Ev 106, para 26

180 Ev 132, para 23

181 Q 317

118. The production of sugar cane is a significant industry in many African, Caribbean and Pacific (ACP) countries. Many of them have a high dependence on sugar exports for contributions to GDP foreign exchange earnings and employment.¹⁸² When the UK joined the European Union in 1973, it secured an agreement allowing the continued importation of raw cane sugar from its traditional suppliers in the ACP countries of the Commonwealth. This agreement allows 1.3 million tonnes of sugar to be imported into the EU each year, at the same prices as the guaranteed internal support price set by the sugar regime, and free of any EU levy.¹⁸³ Their access to the EU market represents around 70% of the revenue of their sugar sectors.¹⁸⁴

119. The ACP London Sugar Group, representing 13 ACP and LDC countries¹⁸⁵, was concerned that the Commission's proposals for "radical" price cuts for sugar would result in significant socio-economic damage in several countries, a point echoed by Tate & Lyle.¹⁸⁶ In particular, the Group believes that it is unfair that compensation will be available to the beet sector in the EU under the proposals, but not to cane growers in the ACP countries.¹⁸⁷

120. The EU Agriculture Commissioner accepts that the reforms will have "knock-on effects" for the ACP countries, but has stressed that the Commission is "fully committed to finding ways to help them adapt to the new market situation they will face after reform".¹⁸⁸ To this end, the reform proposals are accompanied by an 'Action Plan for Accompanying Measures for the ACP'. This includes maintaining preferential access for ACP imports, promoting the diversification of products and markets of ACP regions, and helping producers "prepare for change rather than just cushioning them against it". The Commission has also proposed development assistance to enhance the competitiveness of the sugar sector, where this is sustainable, promote diversification of sugar-dependent areas and addressing broader adaptation needs. The value of the assistance in 2006 has been set at €40 million.¹⁸⁹ A "broad range of support options" is being offered, to be tailored in each country to the needs identified by the stakeholders, and integrated into a long term, comprehensive, sustainable strategy.¹⁹⁰ The Commission envisages that support from national governments, the sugar industry, and/or other sponsors or financial institutions would also be made available.¹⁹¹

121. The ACP London Sugar Group attacked the Commission's proposals in its written evidence, arguing that they would not provide the level of assistance required within the

182 Ev 138, para 31 [ACP London Sugar Group]

183 HC 550-I, para 6

184 European Commission press release IP/05/85, 24.01.2005; EP Development Committee report, 30.09.2005

185 The countries in the Group are: Barbados, Belize, Congo, Fiji, Guyana, Jamaica, Malawi, Mauritius, St. Kitts-Nevis, Swaziland, Tanzania, Zambia and Zimbabwe

186 Evs 135, 138, paras 6, 32 [ACP London Sugar Group]; Q24 [Tate & Lyle]

187 Ev 135, para 5 [ACP London Sugar Group]

188 European Commission press release IP/05/85, 24.01.2005

189 *Ibid.*

190 European Commission press release IP/05/776, 22.06.2005

191 EP Development Committee report, 30.09.2005, A6-0281/2005

requisite time frame and were unnecessarily burdensome and time-consuming. “No monetary value has been placed on the assistance, and there is no timetable for disbursement. No clear linkage has been established between the financial assistance offered, the trade losses which will be sustained and the resources required”. The Group compares these proposals unfavourably with those offered to EU beet growers.¹⁹²

122. The Development Committee of the European Parliament, to which the ACP Action Plan has been referred under the co-decision procedure, has also criticised them. Although it acknowledges that the budget proposed by the Commission for 2006 is of a preparatory nature, it still argues that it should be increased:

The amount provided for in the proposal for a regulation is quite inadequate to enable ACP countries affected by the reform of the EU sugar regime to implement the far reaching adjustment programmes needed in order to successfully adapt to the new market conditions.

The Committee therefore proposes that €80 million—twice the Commission’s proposal—should be set aside for implementation in 2006.¹⁹³ Tate & Lyle, which refines the vast majority of the ACP raw cane sugar imported to the EU, has argued that it is essential that EU assistance to the ACP countries is “wholly adequate, properly targeted, and efficiently delivered in a timely way”.¹⁹⁴

123. The UK Government has stated, in its EU Presidency capacity, that “integral to reform are good, timely, transitional arrangements, which are acceptable to the African, Caribbean and Pacific (ACP) countries and which effectively help them adjust to the reform”.¹⁹⁵ We questioned the Minister about progress in reaching agreement on assistance to the ACP countries. Lord Bach told us that this was “an issue of some concern” at the moment, which Defra, together with the Foreign and Commonwealth Office, the Department of Trade and Industry and the Department for International Development, was working to try and resolve. He noted that the Commission had indicated that “substantially more” than the initial €40 million would be required through the next financial perspective up until 2013. The Minister would not put a figure on what was meant by “substantially”, but told us: “Substantial ... can sometimes mean more than doubling. By substantial we mean really substantial”.¹⁹⁶

124. The Minister, and Tate & Lyle witnesses, stressed that the problems caused for the ACP producers would have to be tackled on a country-by-country basis. Different countries’ industries were at varying levels of viability.¹⁹⁷ Lord Bach noted that some of the ACP countries had developed sugar industries that would never have existed without the

192 Ev 138 para 32 [ACP London Sugar Group]

193 EP Development Committee report, 30.09.2005, A6-0281/2005

194 Ev 3, para 23

195 UK Presidency Priorities, presented to the European Parliament 23 June 2005

196 Qq 314-15

197 Q 314; Q 24 [Tate & Lyle]

“artificial” EU price: “they might well have benefited by having industries in other fields rather than in sugar”.¹⁹⁸

125. We were concerned that the element of the reforms relating to aid for the ACP countries might not be finalised by the time the agricultural package is agreed. The Minister agreed that there was a danger that agreement could be reached on the agricultural aspects of the proposals so far as they affected EU producers before agreement was reached on the support for the ACP countries, but he stated that the UK would prefer them to be agreed in parallel.¹⁹⁹

Our conclusions

126. **We note that Defra, the Foreign and Commonwealth Office, the Department of Trade and Industry and the Department for International Development are all working on the sugar reform’s impact on ACP countries. We believe the various Government Departments which have an interest in reform of the EU sugar regime and its impact on ACP countries must now issue a clear statement outlining the UK’s position.**

127. **We share the concern of the European Parliament’s Development Committee that the assistance to be made available for the ACP countries is insufficient, especially when compared to the €1.5 billion to be made available annually to beet growers within the EU, if they wish to withdraw from sugar production. We urge the UK Government to support the maximum possible increase in the level of assistance for the ACP countries, both in 2006 and in the subsequent years covered by the Commission’s Action Plan. Such assistance should seek to ensure that countries that are currently dependent on income from sugar exports to the EU have a realistic chance of diversifying into other forms of agriculture and land use.**

128. **We further urge the Government, in its Presidency role, to seek agreement on the development aspects of the reforms at the same time as agreement is concluded on the agricultural elements.**

9 The role of the UK government

129. During the UK Presidency of the EU, which runs until the end of 2005, UK Government Ministers will play two roles. Margaret Beckett, as Secretary of State, chairs the Council meetings of Agricultural Ministers, while the UK will still be represented at those meetings by another Minister (for instance, Ben Bradshaw was in the UK seat for the agriculture items on 25 October). Defra will also chair official-level meetings. David Hunter, Defra’s director of EU and International Policy, recently described how the UK Presidency would affect his role, as he takes up the chair of the EU’s Special Committee on Agriculture. “As spokesman, you have the UK interest at the front of your mind ... As

198 Q 316

199 Q 319

chair, you are trying to steer the Member States towards a consensus. It's rather like switching from a seat in the band to a place on the conductor's podium".²⁰⁰

130. Clearly, it is of great importance that the Government uses its Presidency to achieve agreement on the vexed issue of sugar reform. But some witnesses were concerned that the UK's presidency role would mean it had to focus more of its attention on building a consensus amongst other Member States, rather than pursuing the UK's national interests.²⁰¹ Lord Bach sought to re-assure us on this point:

There are comments by people who obviously believe that holding the Presidency may inhibit the extent to which we can argue a national UK case. We believe this is based on some sort of misunderstanding. We are perfectly entitled to put our views from the UK seat ... in the same way that other Member States do from theirs. The difference is that the Chair of the Council has obligations as to the conduct of the debate and the need to seek consensus round the table ... I would argue that that is absolutely consistent with our position both as President and as an individual Member State of the EU.²⁰²

The Secretary of State, Margaret Beckett, also assured us that the concerns of the UK stakeholders were "not being ignored" and were being "raised in the proper way". She also confirmed that the UK had had a trilateral discussion with the Presidency and the Commission, at official level, and that she expected the relevant UK Minister to continue such discussions at the November Agriculture Council.²⁰³ Lord Bach added that one disadvantage of the Presidency role was that the Government concerned could not be quite as forthcoming as it might like to be in public about its position on negotiations.²⁰⁴

Our conclusions

131. Defra Ministers have a difficult hand to play in the negotiations over reform of the EU sugar regime, seeking to achieve consensus while ensuring the UK's interests are accommodated. We were pleased to hear from the Secretary of State that the UK's presidency will not inhibit UK Ministers from pursuing the UK's national interests in the negotiations. We hope that the UK representatives will take fullest advantage of the opportunities provided by meetings with the Presidency and the Commission to put forward the concerns of the UK sugar industry and producers.

132. We hope that, in its role as President, the UK Government will use all its efforts to achieve agreement. The sugar regime has remained unchanged while the rest of the CAP has been reformed. Change is overdue, inevitable and necessary: it would be a great disappointment were the EU to miss this opportunity for reform.

200 "Conductor of the band", *Landscape* (Defra's staff magazine), July 2005, p 13

201 See e.g. Tate & Lyle, Qq 68-69

202 Q 265

203 Environment, Food and Rural Affairs Committee, Minutes of Evidence, Wednesday 2 November 2005, *The work of Defra*, HC 642-i, Qq 6-8

204 Q 275

Conclusions and recommendations

Introduction

1. We were disappointed that, when the Minister for Sustainable Food and Farming gave evidence, he was so reluctant to confirm whether the issues that other witnesses had identified as being important would be raised by the UK Government in negotiations on the reform package. While we accept the problems that may arise in pursuing its national interests for the Member State that holds the EU Presidency, from the point of view of the growers, processors, refiners and environmentalists, it is important for them to be sure that concerns are being raised from a British standpoint. (Paragraph 11)

Extent and timescale of the proposed price reductions

2. Price cuts are an essential element in bringing the European sugar market into balance. We welcome the Commission's approach, centring on price reductions and not quota cuts, as this was what the UK industry told us it preferred. A lower internal price for sugar will make the EU market less attractive, not only to the least efficient beet growers, but also to the least competitive sugar producing countries outside Europe. Setting the price low enough to drive out the inefficient producers, but still sufficiently high for the most efficient producers to prosper, is clearly the critical balance that will define the success of the reforms. We welcome the two year period for implementing the price reductions, as this should allow sufficient time for the European sugar industry to adapt to the proposed changes. (Paragraph 24)
3. In the absence of a precise indication from the UK beet industry on what price levels it requires in order to survive, it is difficult to know whether the Commission's proposals are too severe. It seems certain, though, that pressure will be applied in the negotiations, from other Member States, to dilute the price cuts significantly. If successful, these changes could leave the EU market with an unwanted surplus and necessitate mandatory quota cuts in the future that would adversely affect even the most efficient parts of the beet industry. Therefore, the UK Government's negotiating position must be to support the Commission in minimising any dilution of the price cuts that have been proposed and at the same time ensuring that these proposals do not act adversely on the UK's farmers because of the UK's ratio of 'A' and 'B' sugar. (Paragraph 25)
4. We share the concerns expressed to us about the operation of the reference price, for sugar which is intended to replace the intervention price. Defra should seek further assurances from the Commission that the reference price will provide an effective floor in the market before agreeing to its inclusion in the final reform package. While the retention of the production charge might seem unjustified, given that its original purpose will be superseded, we recognise the argument for its inclusion to help ensure the overall package is budget neutral. There does, however, appear to be little justification for the 'flexibility clause' as currently drafted. We therefore recommend

that the proposals be amended to recognise the right of growers to benefit from a share in the extra margin when the market price is higher than the reference price. (Paragraph 29)

5. We conclude that, given the highly competitive climate in which manufacturing operates, and the pressure which the large retailers can bring to bear on their suppliers, it is likely that consumers will benefit from some degree of price reduction in the medium to longer term. The Committee believes consumers should benefit in direct relation to the reduction in the sugar price. One of the key determinants of the size of this price reduction will be the extent to which the processors pass on the price reduction to sugar users. We expect the UK's processors to pass on, to the fullest extent possible, the reduction in the sugar price. We recommend that the competition authorities be asked to investigate the UK processing industry if any evidence emerges that, as a result of over-concentration in the industry, this is not happening. A separate investigation should take into account the current inbuilt premium paid by sugar users in the UK compared to those in the rest of Europe. The export refund scheme should take into account the total market price in the early years of the regime which will include costs for restructuring and compensation. (Paragraph 36)

Proposed arrangements for compensating EU producers

6. Direct payments to growers must be fully decoupled from production, in order to minimise market distortion. We are pleased that Defra seems so committed to implementing direct payments to English farmers in a fully decoupled form. (Paragraph 43)
7. The UK Government should strongly oppose any attempt to introduce the option of partial decoupling into a compromise package. Such a dilution of the original proposals could frustrate the success of the restructuring scheme and leave UK processors at a comparative disadvantage to processors in other parts of the EU. (Paragraph 44)
8. In deciding how to implement the grower compensation element of the proposals, the Government must balance diverse and sometimes conflicting policy objectives, which include compensation, income support and the provision of environmental benefits. It is vital that Defra conduct a full impact analysis before reaching its implementation decision. Whatever implementation method the Government decides on, it should not allow a system of 'compensation' to become simply 'income support' in the longer term, as such payments would neither compensate for price reductions nor induce any further compliance with environmental standards. (Paragraph 50)
9. We received insufficient evidence to show conclusively whether the 60% figure proposed by the Commission represented an appropriate level of compensation for beet growers. However, it does seem broadly consistent with reforms in other sectors. Defra's RIA did not fully take into account the degressive nature of payments over time, as would be experienced by English sugar growers under an implementation model that moved to a purely flat-rate system. We call on the

Government to carry out an urgent study to assess the long-term impact on growers of making payments on this basis. (Paragraph 54)

10. The UK's beet growers will not be directly affected by the restructuring scheme, as British Sugar has stated it plans to continue production of sugar, although it will mean that benefits to manufacturers and consumers in terms of price cuts will be delayed. (Paragraph 58)
11. The Committee calls on the Government to clarify the position over the rights of producers to use quota in the event of British Sugar closing one or more of its existing plants and the redundant plant being operated by sugar beet farmers or another third party. (Paragraph 59)

Changes to the quota arrangements

12. We are concerned about the unfair impact on the UK of applying the proposed price cut to the new unified quota. The Committee regards this as an important issue and we recommend that the UK Government negotiate for a change in the proposals, so that the UK's status as a deficit country is adequately recognised in the compensation package. It would not be fair if the price cut for UK growers were amplified by an accident of history. An increase in the amount of compensation for the UK could go some way to reducing the disproportionately negative impact of the proposals on the UK beet sector. Since the proposals are designed to be budget neutral and contained within the financial ceiling for agricultural expenditure, such negotiations will require acceptance from surplus countries that their envelopes will have to be cut by an equivalent amount. Furthermore, if quota cuts are required in the future, they must be made on the current basis, so as not to further disadvantage the UK. (Paragraph 66)
13. We are disappointed that the Commission's reform proposals did not include the lifting of quota restrictions as a long-term objective, given the distortions caused by the existing system. We therefore recommend that the Government pursue the abolition of quota restrictions. While quotas do still exist, we believe that transferability between Member States would aid the relocation of sugar production from the least competitive sugar producing regions to the most competitive. The swift establishment of legal certainty on the issue of quota ownership, as well as being desirable in itself, would help facilitate future cross border trade in quotas. (Paragraph 74)
14. The UK Government should negotiate for the reinstatement of the mid-term review clause in the final reform package, as this would provide an opportunity to revisit these important issues. Failure to secure such a clause could lock into the new regime all the distortions of the quota system for another 10 years. (Paragraph 75)

Implications for agriculture and the environment

15. The UK Government should ensure that the final reform package allows the UK's sugar beet industry to exploit its position of relatively high efficiency. It is important

that no distortions are allowed into a compromise deal that could discriminate against the UK beet sector. (Paragraph 85)

16. We note the interdependent relationship between the growers and the processors and recommend that Defra work closely with both parties in ensuring that a proper balance between them is achieved in the post-reform era. As British Sugar works so closely with UK farmers, we recommend that it looks at whether it can share some of its processing margin with the beet growers to ensure continuity of beet supply. (Paragraph 86)
17. We are disappointed, on behalf of sugar beet growers, that British Sugar appears to have changed its position, and now regards wheat as being the best source of bioethanol in the UK. We suggest that British Sugar reconsiders its position on the viability of producing bioethanol from sugar beet. Efforts should also be made to explore the feasibility of converting redundant sugar processing factories to the manufacture of biofuels, thus encouraging the increased production of renewable transport fuels. (Paragraph 92)
18. We also support the European Parliament Development Committee's proposal that bioethanol production should be encouraged in the ACP countries, as this could help support the viability of some ACP countries' sugar industries, given the increasing worldwide demand for bioethanol. (Paragraph 93)
19. As the Committee has said before, more needs to be done to develop biomass for energy production. We hope that beet growers seeking an alternative crop, following reform of the sugar regime, will consider the potential of energy crops where these are viable on the land in question. The Government, in implementing the reforms in the UK, should ensure incentives (including those referred to in our predecessor Committee's reports on biofuels) are in place to encourage this kind of diversification. (Paragraph 94)
20. We have found it difficult to draw detailed conclusions about the comparative environmental impacts of different kinds of sugar production in different areas of the world. However, it is clear to us that the UK and the other EU Member States must pay particular attention to the important issue of the environment when considering how to reform and retain a viable European sugar sector. Brazil's questionable track record relating to the environmental impact of its agricultural expansion should be fully weighed in this regard. (Paragraph 102)
21. As far as the UK is concerned, we recognise the benefits in terms of biodiversity provided by beet growing. But we believe that these benefits should be secured, and funded, through targeted agri-environmental programmes under the CAP. We therefore recommend that the Government ensure sugar beet farmers have access to appropriate environmental stewardship schemes under the reformed CAP, thus enabling them to continue to provide environmental benefits on their land. In this way, public funding would be used to provide a public good—enhanced biodiversity—rather than to support an outdated element of the CAP. (Paragraph 103)

Impact on UK-based processors and refiners

22. The Government must negotiate to ensure equitable terms of competition between the cane and beet sectors in the UK. On the balance of evidence received, we conclude that the cane sector is unduly disadvantaged by the proposals as they currently stand. (Paragraph 116)
23. We were concerned to establish what would be in the best interests of the ACP suppliers. On balance, we thought the continued viability of Tate & Lyle refining operations would be better for them. Therefore, we accept that the proposals to restrict beet processors from refining cane are necessary in the interim period while the ACP suppliers are adapting to reform. We are also sympathetic to the suggestion of retaining some form of refining aid. However, funds for this corrective mechanism would have to be deducted from the package of support for the beet industry in order for the reforms to remain budget neutral. (Paragraph 117)

Impact on the ACP countries

24. We note that Defra, the Foreign and Commonwealth Office, the Department of Trade and Industry and the Department for International Development are all working on the sugar reform's impact on ACP countries. We believe the various Government Departments which have an interest in reform of the EU sugar regime and its impact on ACP countries must now issue a clear statement outlining the UK's position. (Paragraph 126)
25. We share the concern of the European Parliament's Development Committee that the assistance to be made available for the ACP countries is insufficient, especially when compared to the €1.5 billion to be made available annually to beet growers within the EU, if they wish to withdraw from sugar production. We urge the UK Government to support the maximum possible increase in the level of assistance for the ACP countries, both in 2006 and in the subsequent years covered by the Commission's Action Plan. Such assistance should seek to ensure that countries that are currently dependent on income from sugar exports to the EU have a realistic chance of diversifying into other forms of agriculture and land use. (Paragraph 127)
26. We further urge the Government, in its Presidency role, to seek agreement on the development aspects of the reforms at the same time as agreement is concluded on the agricultural elements. (Paragraph 128)

The role of the UK Government

27. Defra Ministers have a difficult hand to play in the negotiations over reform of the EU sugar regime, seeking to achieve consensus while ensuring the UK's interests are accommodated. We were pleased to hear from the Secretary of State that the UK's presidency will not inhibit UK Ministers from pursuing the UK's national interests in the negotiations. We hope that the UK representatives will take fullest advantage of the opportunities provided by meetings with the Presidency and the Commission to put forward the concerns of the UK sugar industry and producers. (Paragraph 131)

28. We hope that, in its role as President, the UK Government will use all its efforts to achieve agreement. The sugar regime has remained unchanged while the rest of the CAP has been reformed. Change is overdue, inevitable and necessary: it would be a great disappointment were the EU to miss this opportunity for reform. (Paragraph 132)

Annex 1: Background to the current regime

In this annex we set out how the regime came into being and why it is now to be reformed.²⁰⁵ In 1967 the sugar sector of the six original EEC members (France, Germany, Italy, Netherlands, Belgium and Luxembourg) was regulated as a common market organisation for the first time. Sugar benefited from a system of support, whose chief elements were:

- minimum prices for white sugar and also for sugar beet;
- import tariffs at levels high enough to deter supply from the world market, and
- export refunds to ensure that EU exports on the world market remained competitive (including refunds on sugar in exports of processed products known as ‘non-Annex 1’)

Production quotas were introduced from the outset, divided into ‘A’ quota (to cover domestic production) and ‘B’ quota (to cover exports). Above-quota ‘C’ sugar could only be exported outside the EC and without any subsidy. A small levy on ‘A’ sugar and a large levy on ‘B’ sugar meant that the cost of exporting quota sugar was said to be self-financing.

This structure has remained largely unchanged, although each enlargement has brought with it additional issues, especially the accession of the UK in 1973. This transferred the British agreement with the Commonwealth on the import of cane sugar into an EU agreement with the African, Caribbean and Pacific (ACP) countries. Under the ‘Sugar Protocol’, selected ACP countries supply 1.4 million tonnes of raw cane sugar to the EU market for refining.

Recent pressures for reform

As noted above, the sugar regime has survived all previous rounds of CAP reform. But recent developments have brought unprecedented pressure on the policy, which has convinced the European Commission that the current system is unsustainable and must be reformed. These developments include wider CAP reform, the ‘Everything but Arms’ initiative and the actions of the World Trade Organisation (WTO).

Wider CAP reform

The CAP reforms agreed in June 2003 sought to minimise incentives to farmers to produce other than what the market demands. These reforms make the unreformed sugar regime anomalous in its structure of high support prices, quotas and export refunds.

²⁰⁵ This section draws extensively on the partial Regulatory Impact Assessment published by Defra in June 2005

'Everything But Arms'

The Everything But Arms initiative was a unilateral decision taken by the EU in 2001 to suspend all customs duties and levies for almost all imports from the 46 Least Developed Countries. In the case of sugar, rice and bananas, duty-free access was deferred until 2009. A quota of raw cane sugar for refining has been allocated, increasing by 15% each year until 2009. From 2006–8, duties are to be phased out, without any volume limits, for all forms of sugar, by 20%, 50% and then 80%. From 1 July 2009, no duties will be levied. The Commission believes that the existing sugar regime will not be able to survive the surge of imports which this will bring.

The World Trade Organisation

The World Trade Organisation (WTO) agreement in Doha in 2001 promised "substantial increases in market access" for agricultural goods. The Doha framework agreement, concluded on 1 August 2004, calls for an end to all forms of export subsidies in all sectors, and reductions in import tariffs, both of which strengthen the need for substantive reform of the sugar regime. Since 2003, Australia, Brazil and Thailand have pursued a case in the WTO against the EU sugar regime. They argued that the EU was only able to export non-quota or 'C'—officially unsubsidised—sugar because of the high prices derived from quota ('A' and 'B') production. The complainants also stated that the EU should include, in the subsidised exports which count against WTO limits, the 1.6 million tonnes currently imported from ACP countries and India—a footnote to the Uruguay Round schedule currently appears to allow the EU to exclude these. The WTO Panel reported in autumn 2004 and upheld both complaints against the EU, and this ruling was confirmed by the Appellate Body in April 2005.

Annex 2: Comparison of the main arguments between British Sugar and Tate & Lyle²⁰⁶

Contested issue	Position of British Sugar (BS)	Position of Tate & Lyle (T&L)
Exclusivity of supply of raw sugar cane for full-time refiners	It is strongly in the interests of all developing countries to be able to sell their raw sugar to as many industries as possible, as this gives them the best terms and prices. A comparison with quotas is not valid as they represent a limit, not a guaranteed volume.	A reduced volume of sugar from a restricted supply of imported cane would render T&L's operations unviable due to the need to maintain capacity to cover fixed costs. Beet processors would have their fixed costs covered by the beet enterprise and would be able to use the factories for cane in those months of the year when beet is not processed. This skews any comparison of the costs incurred by the same factory refining cane. Marginal beet factories which remained in production by refining cane would stifle the aim of the restructuring scheme, to decommission inefficient factories.
Differential impact on margins	T&L's comparison of processor and refining margins is flawed due to the assumptions made on costs and prices. The financial effects of the reform proposal on EU refiners and beet processors are broadly similar, so there is no justification for special treatment for refiners in the form of a refining subsidy.	The refiners' margin would fall by 77% while the beet processors would fall by only 44%. T&L said that the retention of a refining aid payment of around €60 per tonne is the only solution to fix this distortion.
Whether Tate & Lyle could survive in a deregulated market	BS questioned T&L's assertion that it could survive in a deregulated market and argued that if this was the case, then T&L would get better financial returns from the reform proposals than all EU beet processors.	T&L said it is only asking that a company that could compete effectively in a totally deregulated market should be treated equitably in a regime that continues to be based on the desire to artificially support the beet sector.
General balance of current proposals	<ul style="list-style-type: none"> Refiners are protected from cuts in volume as experienced in the beet sector Further concessions for the refiners would tilt the beet/cane balance even more in the refiners' favour 	T&L said that BS has the options of purchasing additional quota or going into the restructuring scheme, neither of which are available to refiners.

206 See para 108.

Glossary

African, Caribbean and Pacific countries	The ACP Group consists of 79 Member States: 48 countries from Sub-Saharan Africa, 16 from the Caribbean and 15 from the Pacific. Fixed quantities of ACP sugar command preferential prices under the terms of the Sugar Protocol.
Bioethanol	A petrol additive or substitute produced from crops such as cereals, sugar cane, sugar beet and fodder beet.
Biomass	Any biological mass derived from plant or animal matter (e.g. timber crops, straw, chicken litter and other waste material) used as a source of renewable heat or electricity.
Decoupling	Breaking the link between support and the production activity: a payment is said to be 'partially decoupled' if a proportion of the support is still based on production.
Degressive payment	A payment that decreases in a stepwise fashion.
Environmental Stewardship	Environmental Stewardship is a new agri-environment scheme which provides funding to farmers and other land managers in England who deliver effective environmental management on their land.
Everything But Arms	EBA is an EU initiative, dating from 2001, to allow duty free and quota free entry for products from 48 (now 50) least developed countries in the world (for sugar, this liberalisation will be phased-in over three years from 2006/07 to 2008/09).
Export refunds	Payments to exporters of goods from the EU to third countries in order to compensate for the difference between high Community and lower world prices.
Flat-rate payments	Equal payments per hectare resulting from the total direct support allocation for a country being spread evenly across all the eligible area.
Flexibility clause	An element of the sugar reform proposals that would grant sugar beet growers and processors the possibility to negotiate the sugar beet price down to 10% below the guaranteed minimum price.
Import tariffs	Taxes levied by a government on goods imported into its country.
Intervention system	Market management tool in which products are bought by the EU or a national government when prices are low and supplies high, and sold when prices have increased and supplies reduced. The

‘intervention price’ is the level at which the public authorities have a support buying commitment. This facility is, however, scarcely ever used within the sugar regime.

Least Developed Countries	A social/economic classification status applied by the United Nations to around 50 of the poorest countries of the world.
Minimum beet price	The price which processors are legally required to pay growers for their sugar beet.
Private storage system	Mechanism for temporarily withdrawing sugar from the market, triggered when the market price falls below the reference price.
Production levy	A levy charged on the beet industry (processors and sugar beet growers combined) to meet the full costs to the EU budget, on an annual basis, of exporting surplus sugar to the world market.
Quotas	Supply constraints, based on historic production references, devised as a means of limiting EU responsibility for supporting sugar.
Reduction coefficient	A numerical factor, based on the proportions of ‘B’ quota, that is currently used to allocate quota cuts amongst the EU Member States.
Reference price	Institutional price establishing the trigger level for private storage.
Restructuring scheme	Element of the Commission’s reform proposals, designed to lure inefficient sugar processors out of production and compensate for the closure of factories.
Single Farm Payment	Single subsidy payment amalgamating a number of existing direct subsidy schemes, introduced as part of the package of CAP reforms agreed in June 2003.
Special Committee on Agriculture	Group comprising permanent representatives of all the EU Member States, which meets to prepare Council decisions on common agricultural policy matters.
Transitional hybrid compensation system	Model adopted by Defra in implementing the Single Farm Payment in England that combines a large element of historically based payments in the early years, but moves, over time, to a fully flat-rate area payment.
World Trade Organisation	An intergovernmental body set up to administer multilateral trade agreements, negotiations on which are ongoing under a round begun at a meeting in Doha, Qatar.

Formal Minutes

Wednesday 9 November 2005

Members present:

Mr Michael Jack, in the Chair

David Lepper

David Taylor

Mr Dan Rogerson

The Committee deliberated.

Draft Report [*Reform of the EU Sugar Regime*], proposed by the Chairman, brought up and read.

Ordered, That the draft Report be read a second time, paragraph by paragraph.

Paragraphs 1 to 132 read and agreed to.

Annexes and glossary agreed to.

Resolved, That the Report be the Second Report of the Committee to the House.

Ordered, That the Chairman do make the Report to the House.

Ordered, That embargoed copies of the Report be made available, in accordance with the provisions of Standing Order No.134.

Several papers were ordered to be appended to the Minutes of Evidence.

Ordered, That the Appendices to the Minutes of Evidence taken before the Committee be reported to the House.

Several memoranda were ordered to be reported to the House.

[Adjourned until Tuesday 15 November at 1.30pm]

Witnesses

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Mark White and Patricia Jamieson, Tate and Lyle Sugars, Europe	Ev 5
Chris Tyas, Anna Lucuk, and Richard Laming, UK Industrial Sugar Users Group	Ev 28

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Wubbo Wage , Dutch Beet Growers' Federation (NBF)	Ev 37
Tim Bennett, Mike Blacker, and Helen Kirkman, National Farmers' Union	Ev 51
Dr Mark Carr, Chris Carter, Simon Harris, and Clare Wenner, British Sugar plc	Ev 66

Wednesday 26 October 2005

Lord Bach, Andrew Kuyk, and Dr Colin Smith, Department for Environment, Food and Rural Affairs	Ev 83
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List of written evidence

1	Tate & Lyle Sugars, Europe	Ev 1, 13, 142
2	UK Industrial Sugar Users Group	Ev 20, 35
3	Biscuit, Cake, Chocolate and Confectionery Association (BCCCA)	Ev 22
4	Cadbury Schweppes plc	Ev 25
5	National Farmers' Union	Ev 42
6	British Sugar	Ev 59, 73, 140
7	Department for Environment, Food and Rural Affairs	Ev 81
8	JP Agronomy	Ev 96
9	Tenant Farmers Association	Ev 98
10	Food & Drink Federation	Ev 100
11	Professor Sir John Marsh	Ev 103
12	Confédération Internationale des Betteraviers Européens	Ev 106
13	Graham Day	Ev 107
14	British Beet Research Organisation (BBRO)	Ev 107
15	B.J. Gooderham	Ev 109
16	Delitzsch UK	Ev 110
17	WWF-UK	Ev 112
18	British Starch Industry Association	Ev 116
19	Broom's Barn Research Station	Ev 119
20	Centre for Holistic Studies, India	Ev 120
21	Agricultural Industries Confederation	Ev 122
24	RSPB	Ev 125
25	Tom Meikle	Ev 128
26	Joan Noble	Ev 129
27	Which?	Ev 133
28	ACP London Sugar Group	Ev 134

List of unprinted written evidence

BCCCA (Two background notes)
 British Sugar (Background note)
 Tate & Lyle Sugars, Europe (Two background notes)
 ACP London Sugar Group (Background note)
 Dutch Beet Growers' Federation (Background note)

Reports from the Environment, Food and Rural Affairs Committee since 2003

The following reports have been produced (Government Responses in brackets):

Session 2005–06

First Report	The future for UK fishing: Government Response	HC 532
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Session 2004–05

Ninth Report	Climate Change: looking forward	HC 130-I (HC 533 05-06)
Eighth Report	Progress on the use of pesticides: the Voluntary Initiative	HC 258 (HC 534 05-06)
Seventh Report	Food information	HC 469 (HC 437 05-06)
Sixth Report	The future of UK fishing	HC 122 (HC 532 05-06)
Fifth Report	The Government's Rural Strategy and the draft Natural Environment and Rural Communities Bill	HC 408-I (Cm 6574)
Fourth Report	Waste policy and the Landfill Directive	HC 102 (Cm 6618)
Third Report	The Work of the Committee in 2004	HC 281
Second Report	Dismantling Defunct Ships in the UK: Government Reply	HC 257
First Report	The draft Animal Welfare Bill	HC 52-I (HC 385)

Session 2003–04

Nineteenth Report	Water Pricing: follow-up	HC 1186 (HC 490 04-05)
Eighteenth Report	Dismantling of Defunct Ships in the UK	HC 834 (HC 257 04-05)
Seventeenth Report	Agriculture and EU Enlargement	HC 421 (HC 221 04-05)
Sixteenth Report	Climate Change, Water Security and Flooding	HC 558 (HC 101 04-05)
Fifteenth Report	The Departmental Annual Report 2004	HC 707 (HC 100 04-05)
Fourteenth Report	Sites of Special Scientific Interest	HC 475 (HC 1255)
Thirteenth Report	Bovine TB	HC 638 (HC 1130)
Twelfth Report	Reform of the Sugar Regime	HC 550-I (HC 1129)
Eleventh Report	GM Planting Regime	HC 607 (HC 1128)
Tenth Report	Marine Environment: Government reply	HC 706
Ninth Report	Milk Pricing in the United Kingdom	HC 335 (HC 1036)
Eighth Report	Gangmasters (follow up)	HC 455 (HC 1035)
Seventh Report	Implementation of CAP Reform in the UK	HC 226-I (HC 916)
Sixth Report	Marine Environment	HC 76 (HC 706)
Fifth Report	The Food Standards Agency and Shellfish	HC 248 (HC 601)
Fourth Report	Environmental Directives	HC 103 (HC 557)
Third Report	Caught in the net: Cetacean by-catch of dolphins and porpoises off the UK coast	HC 88 (HC 540)
Second Report	Annual Report of the Committee 2003	HC 225
First Report	Water Pricing	HC 121 (HC 420)