Measure fiche

Risk Management

Measures 17

Articles 36-39 of Council Regulation (EU) No 1305/2013

This fiche is based on the text of Regulation (EU) No 1305/2013 [EAFRD] and, when relevant, on Regulation (EU) No 1303/2013 [CPR]. Since the Delegated and Implementing Acts supplementing these regulations have not yet been adopted, some modifications to this guidance fiche might be needed after their adoption.

This guidance does not represent a binding legal interpretation of Regulation (EU) No 1305/2013. It is therefore essentially non-binding in nature and complements the related legal acts.

1. RATIONALE OF THE MEASURE

Nowadays, farmers are exposed to increasing economic and environmental risks as a consequence of increased price volatility of global agricultural markets and climate change.

Excessive volatility of prices resulting in insecure income expectations makes it more difficult for farmers to undertake long-term planning, and undertake investments. As a consequence, high uncertainty about the future implies that farmers' competitiveness in the long-run can be compromised. High income fluctuation also means that farmers that in normal years are competitive and efficient may be forced out of business due to one disastrous event, which is often outside their control.

In addition to the 'traditional' sources of uncertainties, such as animal and plant health related risks, the effects from climate change are a growing concern for farmers as the frequency and intensity of extreme weather events is likely to increase, amplifying the volatility of agricultural production because of weather-related supply shortfalls. Even though the ultimate impacts on farm income depend on the interplay of many factors such as the global market and policy support, the higher likelihood of failures in production may lead to increasing instability in the economic situation of farmers affected by extreme climate events.

In that context, effective management of risks should be holistic – involving prevention, response, planning – but sill tailored to the farmers' individual situations. The heterogeneity of risks and agricultural structures throughout the EU favours a more decentralised approach to using those instruments which are best suited to the specificities of particular regions and sectors. Rather than applying a "one size fits all" approach, it is preferable to allow Member States flexibility in addressing risks facing farmers, so that the most appropriate solution may be found.

Therefore, a new risk management toolkit has been introduced under the second pillar of the CAP, which builds upon and takes forward the possibilities that currently exist to support insurances and mutual funds via Member States' national direct payment envelopes. There are clear advantages associated with the introduction of risk management instruments under the EU's rural development policy. First, the strategic approach to rural development allows Member States flexibility in choosing the appropriate instruments, budgetary allocations and beneficiaries on the basis of the needs of different rural areas and farmers. Moreover, the second pillar would provide the framework to combine specific support for risk management with complementary rural development measures, such as knowledge transfer, investments in physical assets, diversification into non-agricultural activities, etc. Furthermore, the co-financing character of the European Agricultural Fund for Rural Development (EAFRD) and the requirement of private contributions constitute an incentive for farmers to engage into better risk management themselves.

In order to ensure that there is equal treatment among farmers across Europe, that competition is not distorted and that the international obligations of the EU, especially towards the WTO, are respected, specific conditions have been provided for the granting of support under these measures (as discussed in the sections below).

The Commission shall present a report on the implementation of the risk management toolkit to the European Parliament and the Council not later than 31 December 2018.

2. WHAT'S NEW IN COMPARISON TO THE PERIOD 2007-2013

The risk management toolkit has been newly introduced under the second pillar of the CAP for the period 2014-2020.

However, it builds upon and takes forward the possibilities that exist under Article 68 of Council Regulation (EC) No 73/2009[1], which provides for support for insurance premia and mutual funds via Member States' direct payment envelopes.

3. CONTRIBUTION TO FOCUS AREAS AND CROSS-CUTTING OBJECTIVES

Promoting risk management in agriculture will be one of the six priorities of the EU's rural development policy post-2013.

In particular, measures under articles 36-39 will address Priority 3:

(3) promoting food chain organisation, including processing and marketing of agricultural products, animal welfare and **risk management in agriculture**, with a focus on the following areas:

[1] COUNCIL REGULATION (EC) No 73/2009 of 19 January 2009 establishing common rules for direct support schemes for farmers under the common agricultural policy and establishing certain support schemes for farmers, amending Regulations (EC) No 1290/2005, (EC) No 247/2006, (EC) No 378/2007 and repealing Regulation (EC) No 1782/2003.

(a) […];

(b) supporting farm risk prevention and management.

4. SCOPE, TYPE AND LEVEL OF SUPPORT

4.1. Relevant definitions

- **"Mutual fund"** means a scheme accredited by the Member State in accordance with its national law for affiliated farmers to insure themselves, whereby compensation payments are made to affiliated farmers for economic losses caused by the outbreak of adverse climatic events or an animal or plant disease or pest infestation or an environmental incident, or for a severe drop in their income;

- **"Economic losses"** means any additional cost incurred by a farmer as a result of exceptional measures taken by the farmer with the objective of reducing supply on the market concerned or any substantial loss of production;

- **"Adverse climatic event"** means weather conditions, such as frost, storms and hail, ice, heavy rain or severe drought, which can be assimilated to a natural disaster (NB. The list is not exhaustive, as the wording “such as” indicates. Therefore, other events may fall under this definition provided that they can be assimilated to natural disasters, e.g. floods);

- **"Animal diseases"** means diseases mentioned in the list of animal diseases established by the World Organisation for Animal Health or in the Annex to Council Decision 2009/470/EC;

- **"Environmental incident"** means a specific occurrence of pollution, contamination or degradation in the quality of the environment related to a specific event and of limited geographical scope. It does not cover general environmental risks not connected with a specific event, such as climate change or atmospheric pollution;

- **"Natural disaster"** means a naturally occurring event of biotic or abiotic nature that leads to important disturbances of agricultural production systems or forest structures, eventually causing important economic damage to the farming or forestry sectors.

- **"Income"** for the purposes of the income stabilisation tool shall refer to the sum of revenues the farmer receives from the market, including any form of public support, deducting input costs.

- **"Pest infestation"** means the occurrence of one or more pest species in an area or location where their numbers and impact are currently or potentially at intolerable levels or a sudden increase in destructiveness or population numbers of a pest species in a given area.

4.2. Types of measures covered by the risk management toolkit (Article 36)

Support under the risk management toolkit shall cover:

(a) financial contributions to premiums for crop, animal and plant insurance against economic losses to farmers caused by adverse climatic events, animal or plant diseases, pest infestation, or an environmental incident;

(b) financial contributions to mutual funds to pay financial compensations to farmers, for economic losses caused by adverse climatic events or by the outbreak of an animal or plant disease or pest infestation or an environmental incident;

(c) an income stabilisation tool, in the form of financial contributions to mutual funds, providing compensation to farmers for a severe drop in their income.

Member States shall ensure that overcompensation as a result of the combination of this measure with other national or Union support instruments or private insurance schemes is avoided.

The re-insurance of insurances or mutual funds is not eligible under the EAFRD.

4.2.1. Crop, animal, and plant insurance (Article 37)

Support under this measure shall only be granted for insurance contracts which cover for loss caused by:

- an adverse climatic event;
- an animal or plant disease;
- a pest infestation;
- an environmental incident;
- a measure adopted in accordance with Directive 2000/29/EC on protective measures against the introduction into the Community of organisms harmful to plants or plant products and against their spread within the Community.

The crisis event shall destroy more than 30 % of the average annual production of the farmer in the preceding three-year period or a three-year average based on the preceding five-year period, excluding the highest and lowest entry. (Please see section below on the use of indexes for calculation purposes).

The occurrence of the crisis event has to be formally recognised as such by the competent authority of the Member State concerned. Member States may, where appropriate, establish in advance criteria on the basis of which such formal recognition shall be deemed to be granted. The formal recognition by the competent authority is a WTO requirement.

As regards animal diseases, financial compensation may only be granted in respect of diseases mentioned in the list of animal diseases established by the World Organisation for Animal Health and/or in the Annex to Decision 2009/470/EC.

MS may decide to pay premium support through private insurance companies or other bodies such as producer organisations or consortia stipulating collective insurance contracts acting as intermediaries in view of reducing the administrative burden and red tape for farmers. However, the key condition to be respected is that the full amount of public support (EAFRD contribution plus national counterpart) is entirely for the benefit of the final beneficiary, i.e. the active farmer, or credited to the farmer's account in case the contribution is transferred directly to an insurance company. Under no circumstances support shall be used to pay potential administrative or management costs e.g. account management, transaction activities borne by any intermediary body acting as a collective contractor. The active farmers shall be those who finally benefit from support to the insurance premia.

4.2.2. *Mutual funds for adverse climatic events, animal and plant diseases, pest infestations and environmental incidents ((Article 38)*

Support under this measure shall only be granted for insurance contracts which cover for loss caused by:

- an adverse climatic event;
- an animal or plant disease;
- a pest infestation;
- an environmental incident;
- a measure adopted in accordance with Directive 2000/29/EC on protective measures against the introduction into the Community of organisms harmful to plants or plant products and against their spread within the Community.

The crisis event shall destroy more than 30 % of the average annual production of the farmer in the preceding three-year period or a three-year average based on the preceding five-year period, excluding the highest and lowest entry. (Please see section below on the use of indexes for calculation purposes).

The financial contributions under this measure may only relate to 3 types of support:

1. the administrative costs of setting up the mutual fund, spread over a maximum of three years in a degressive manner;
2. the amounts paid by the mutual fund as financial compensation to farmers;
3. interest on commercial loans taken out by the mutual fund for the purpose of paying the financial compensation to farmers in case of crisis.

No contribution by public funds shall be made to initial capital stock.

Yet, because reserves may not be enough to cover all losses, especially in the first years following setting up, the fund has the possibility to get reinsurance in the private reinsurance markets. However, unlike interests on commercial loans, expenditure linked to reinsurance shall not be eligible public expenditure under the EAFRD Regulation.

In order to be eligible for support the mutual fund concerned shall:

(a) be accredited by the competent authority in accordance with national law;

(b) have a transparent policy towards payments into and withdrawals from the fund;

(c) have clear rules attributing responsibilities for any debts incurred.

Member States shall define the rules for the constitution and management of the mutual funds, in particular for the granting of compensation payments and the eligibility of to farmers in the event of crisis, as well as and for the administration and monitoring of compliance with these rules.

Member States shall ensure that the fund arrangements provide for penalties in case of negligence on the part of the farmer.

The occurrence of the crisis event has to be formally recognised as such by the competent authority of the Member State concerned. Member States may, where appropriate, establish in advance criteria on the basis of which such formal recognition shall be deemed to be granted. The formal recognition by the competent authority is a WTO requirement.

As regards animal diseases, financial compensation may only be granted in respect of diseases mentioned in the list of animal diseases established by the World Organisation for Animal Health and/or in the Annex to Decision 2009/470/EC.

4.2.3. Income stabilization tool (Article 39)

Support under this measure shall only be granted where the drop of income exceeds 30% of the average annual income of the individual farmer in the preceding three-year period or a three-year average based on the preceding five-year period excluding the highest and lowest entry.

Payments by the mutual fund to farmers shall compensate for less than 70% of the income lost in the year the producer becomes eligible to receive this assistance.

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Member States shall ensure that the fund arrangements provide for penalties in case of negligence on the part of the farmer.

4.3. Beneficiaries

Support shall be limited to active farmers as defined in Article 9 of Regulation (EU) No 1307/2013 (DP).

Especially under article 36, not only individuals, but also groups of farmers, consortia or farmers' associations stipulating collective insurance contracts can be beneficiaries of risk management support. Yet, in case of combination of different risk management instruments, overcompensation must be avoided, especially where contracts cover multiple risks.

4.4. Aid intensity / amount of support[2]

Support under the measures provided for by articles 36-39 shall be limited to the maximum support rates laid down in Annex I to the RD Regulation:

- Insurance payments: 65% of the insurance premium due.

The insurance premia supported will depend on the specific risk related to the production insured and will vary according to individual or collective contracts. Payments shall compensate for not more than the total of the cost of replacing the losses and shall not require or specify the type or quantity of future production.

- Mutual funds: 65% of the eligible costs.

Member States may limit the costs that are eligible for support by applying:

(a) ceilings per fund;

(b) appropriate per unit ceilings.

[2] Subject to final decision of legislators.

When referring to the establishment of further ceilings, “per unit” shall mean per member/affiliate to the fund or per unit of insured production.

- Income stabilization tools: 65% of the eligible costs.

Maximum aid intensities may be fixed not only in percentage terms but also in absolute terms, e.g. max 10,000 EUR per farm, as long as the final amount does not overcome the ceilings imposed by the Regulation when calculated in percentage terms.

4.5. Co-financing rate(s)

The EAFRD contribution rate applicable to this measure is defined in Article 59 of Reg. (EU) No 1305/2013.

5. ADMINISTRATIVE / FINANCIAL MANAGEMENT

5.1. National/regional programmes

According to Article 6 of the RD Regulation, a Member State may submit either a single programme for its entire territory or a set of regional programmes or, in duly justified cases, a national programme and a set of regional programmes.

If a Member State submits a national programme containing one or more measures and/or operations in relation to risk management, and a set of regional programmes, those shall be programmed either at national level or at regional level, and coherence between the strategies of the national and regional programmes shall be ensured.

Such a possibility is particularly relevant in the case of risk management to address potential problems of critical mass. In fact, a minimal critical mass is necessary to constitute an initial capital stock that would be consistent enough to compensate farmers in the event of a crisis and to make farmers' contributions not too costly. Equally, in case of insurances, the higher the number of farmers insured by private companies, the lower the premia to be paid by producers and a better functioning competitive market for private insurers.

At the same time, the necessary coherence between national and regional strategies could still be ensured, since measures within the risk management toolkit clearly contribute to a single focus area (i.e. supporting farm risk management).

However, MS concerned should take into account and address potential bottlenecks. First, establishing an extra national programme alongside regional programmes would impose additional administrative burden in terms of general programming, monitoring and evaluation, clearance of accounts etc. Moreover, from a financial perspective, it may occur that financial resources committed under the national programme remain unutilised in case of low measure uptake, therefore automatically decommitted under the "N + 2" rule.

In relation to the inclusion of types of operations closely linked to an effective and efficient implementation of risk management measures, notably knowledge transfer and information or advisory under articles 14 and 15 of the rural development Regulation, it may be possible to introduce, e.g. specific training on risk management in the national programme and programme other types of operations related to training, i.e. training on other topics, under the same measure in the regional RDPs.

5.2. Minimum and maximum duration of commercial loans to mutual funds

Where the source of the funds for the financial compensation to be paid by the mutual funds referred to in Articles 38 and 39 of the rural development Regulation is a commercial loan, the duration of the loan shall be of between **1 and 5 years**.

5.3. Other issues concerning mutual funds and IST

- Specific **rules on the contribution** that any individual farmer should pay into the fund's capital stock – and at what intervals, e.g. biannual or annual fee - may be established by the competent public authority or by the fund's liable entity if the competent authority establishes so. For instance, the amount the single producer is requested to pay may be modulated depending on an ex-ante risk assessment, the average income, the size of the farm, etc. It is in MS responsibility to ensure proper targeting and tailoring according to its strategic approach based on SWOT analysis / identification of needs. Particular attention should be paid to foster the participation of small farms.

- The tools of mutual fund and IST under articles 38 and 39 may be **operated jointly** by the same fund as long as this is accredited by the competent authority in accordance with national law and the conditions applying to the two instruments are respected. Notably, overcompensation shall be avoided, especially as regards setting up costs.

- A fund set up for the purposes of articles 38 or 39 may take on **other functions,** such as credit provision for associates. Since farmers engage in contributing an annual quota to a collective stock of resources to be used in case of crisis, there could be an incentive for the farmer to contribute an extra top-up in order to constitute an additional pool of collective assets that could be used to make credit to the participants. In this case, any resources allocated to the fund's credit (or alternative) function shall be clearly distinguished (separate accounts) from the capital stock, which would actually be activated in case of crisis - and would therefore be compensated by public aid. Only the amount specifically dedicated to risk management purposes should be ringfenced and would be considered as the basis to calculate public aid intensity, be it in the form of financial compensation or interest on loans. Equally, where support would also be provided under rural development for the initial fund set-up, clear demarcation rules should be established for identifying the costs directly related to the mutual fund for risk management and other potential additional costs deriving from carrying out other complementary functions.

- Under certain circumstances, **private contributions** to the fund's capital stock from private actors other than farmers (e.g. hunters) may be allowed. While being contributors, private actors would not be entitled to receive any compensation or repayment. In this scenario, what is mandatory is that the final beneficiary of public support is an active farmer, while, as far as the inputs into the stock of capital are concerned, no restrictions apply. Additional contributions by public actors cannot be subject to co-financing by the EAFRD and have to respect state aid rules.

- Farmers may be entitled to **recover parts of the contributions** to the fund after a certain number of years if the amounts collected were not used and if this approach has been chosen by the MS/mutual fund. It is in MS / fund's responsibility to establish appropriate rules in this respect.

- Regarding **commercial loans and interests**, support shall be provided only for interests on loans taken after a crisis has taken place and only in order to cover losses for which the amounts collected in the fund were not enough at the moment when the crisis occurred. Support for interests on loans taken to reinforce the capital stock shall not be eligible expenditure.

6. TARGETING AND PRINCIPLES WITH REGARD TO THE SETTING OF SELECTION CRITERIA

Notwithstanding the general rule that Member States should establish selection criteria for the selection of projects, by way of exception risk management related measures are exempted from this requirement in order to foster the widest possible participation of farmers into risk management schemes and create a sufficient critical mass for the instruments to operate efficiently.

7. LINKS TO OTHER RURAL DEVELOPMENT MEASURES

- <u>Restoring agricultural production potential damaged by natural disasters and catastrophic events and introduction of appropriate prevention actions (Article 18)</u>

Under this measure, support can be provided for investments in preventive actions aimed at reducing the consequences of probable natural disasters and catastrophic events, together with investments for the restoration of damaged agricultural land and production potential, e.g. restoration of agricultural land and soil quality; re-establishment or restoration of dikes, drainage systems; flood prevention and management measures (e.g. projects related to coastal and interior flood protection).

- <u>Knowledge transfer and information actions and Advisory services, farm management and farm relief services (Articles 14 and 15)</u>

Support could be given to actions related to training/information on risks and risk management for farmers to help improve awareness of current risks, improve risk management strategies and provide know how. Other operations that could be supported include identification of vulnerable areas and sectors and assessment of needs and opportunities for changing crops and varieties in response to climate trends; building adaptive capacity by awareness raising and provision of salient information and advice on farm management and bio-security strategies to reduce animal health risks.

- <u>Investment in physical assets (Article 17)</u>

Investments aimed at mitigating natural disasters and climatic risks by supporting restructuring and modernisation of physical assets and by promoting innovation could be supported, together with e.g. investments in improved efficiency of irrigation infrastructure and water use technologies; storage and preventive mechanisms against adverse effects of climate-related extreme events (e.g. setting up of hail nets).

- Farm and business development (Article 19)

Farmers may diversify in order to reduce their production and price risk. Favorable results in one activity may help to offset losses in another activity. Diversification may include farm-related activities, but also off-farm employment (other gainful activities) which reduces the household's dependency on a fluctuating income from agriculture.

- Agri-environment-climate (Article 28)

Actions related to environmental services and adaptation to climate change can contribute to preventing risks by protecting and improving the environment in agricultural and forest areas. The reinforcement of the quality of management of these areas offers better prevention against floods, droughts, erosion, landslides, forest fires, storms, climate change, etc. The following operations can be taken as examples of risk management tools: integrated crop and pest management; conservation agriculture and soil management practices (e.g. no or reduced-tillage methods, catch crops, diversified crop rotations); water management and use, including establishment of buffer zones and terraces to target water erosion.

- Animal welfare (Article 33)

The measure shall contribute to encouraging farmers to provide a high standard of animal welfare in animal husbandry which goes beyond mandatory standards. Support can be provided e.g. for housing conditions such as space allowances.

- Co-operation (Article 36) and European Innovation Partnership (Articles 61-63)

Risk management offers plenty of opportunity to develop innovative approaches and fill the gap between research and practical application. In the framework of the EIP, the development of tools for the use of index-based systems for loss assessment in agriculture could be addressed.

8. LINKS TO OTHER LEGISLATION

8.1. CAP's first pillar

A variety of CAP instruments should contribute in a complementary way to attenuating the risks of agricultural production through market measures available under the single Common Market Organisation (sCMO), direct payments and the EU's rural development policy.

Among market measures, intervention/reference prices provide a safety net in times of severe crisis for eligible sectors. In the period 2014-2020, public intervention and private storage will be more responsive to crisis situations and exceptional measures have been streamlined and expanded to include a single provision on animal and plant health diseases and loss of consumer confidence for all animal products in the sCMO, and a general market disturbance provision for all sectors of the existing sCMO. Furthermore, the emergency clause has been expanded to allow for a more flexible application of the provisions.

A reserve for crises in the agricultural sector has been established to provide additional financial means outside the annual ceilings for agriculture in the Multiannual Financial Framework. This crises reserve can be mobilised where the annual budget is not sufficient to finance the needs for public intervention and private storage, export refunds and exceptional measures in the event of crises situations.

Direct payments provide an additional layer of support: while they do not have a risk management objective per se, by ensuring a basic income payment, farmers' income is protected against price variability, thus supporting the longer term economic viability of farms.

Annex I provides an overview of the safety net tools in the single CMO and a comparative table of the different risk management instruments under the first pillar of the CAP.

8.2. State aid

The current State aid rules applying to the agricultural sector[3] will expire on 31 December 2013 and are under revision in the light of the new rules that will be applicable to agriculture and rural development under the MFF 2014-2020. In principle, these provisions have to be coherent with the EU's rural development policy, therefore aligned to those of the rural development Regulation.

However, as all measures co-financed under the EAFRD must comply with the WTO green box, the requirements applicable to the risk management toolkit under the II pillar are stricter than those currently applicable in the framework of state aid rules as regards aid towards the payment of insurance premiums, under which support can be notified by MS as amber box.

In particular, more stringent conditions apply under the EAFRD as concern the loss threshold which triggers compensation payments:

- According to WTO green box rules – and therefore to the rural development Regulation – for **any type of crisis event** that can be covered by insurance schemes (i.e. adverse climatic events, animal or plant diseases, etc.), losses should amount to at least **30%** of the average annual production of the farmer;

- On the other hand, according to state aid rules for SMEs (article 12 of Commission Regulation (EC) 1856/2006), the 30% loss threshold shall be applied only **in case of adverse climatic events which can be assimilated to natural disasters** (with a maximum aid intensity amounting to 80%). In all other cases, i.e. where the insurance policy covers other climatic events, and/or animal or plant diseases, or pest infestations, loss thresholds can be lower than 30% to receive support (with lower aid intensities of 50%).

[3] Commission Regulation (EC) 1856/2006 (State aid to small and medium-sized enterprises active in the production of agricultural products)

MS shall continue notify support under ABER as WTO amber box, as it is currently done also for measures under Article 68 of Council Regulation (EC) 73/2009.

9. FOCUS ON SPECIFIC ISSUES LINKED TO CALCULATION METHODS

9.1. 30% loss threshold

WTO green-box provisions on insurance schemes only establish the minimum loss threshold to receive compensation, i.e. 30%, but there are no specific binding rules on how this should be calculated.

Therefore, while the actual value of 30% shall not be lowered, the calculation of loss can be carried out on a **per type of production**. This will also depend on the terms of the insurance contract the farmer negotiates with the private insurance company in terms of the specific risks associated with different types of productions, cultures or plots or other specific arrangements decided by mutual fund (or imposed by the competent authority).

9.2. Use of indexes

Indexes may be used in order to calculate the annual production of the farmer. The calculation method used shall permit the determination of the **actual loss** of an **individual farmer** in a given year.

The measurement of the extent of the loss caused may be tailored to the specific characteristics of each type of product using:

(a) biological indexes (quantity of biomass loss) or equivalent yield loss indexes established at farm, local, regional or national level, or

(b) weather indexes (including quantity of rainfall and temperature) established at local, regional or national level.

Index-based systems are loss assessment tools that use a common exogenous index for a given area to establish triggers and indemnity payments for insured farmers. Compensations are triggered according to the losses that a farmer experiences against the pre-specified index references for the given area where the farmer is located. Such systems allow therefore providing an alternative to often costly and burdensome field inspections. Index-based products are particularly useful for systemic risks at aggregate level (i.e. risks affecting a big population at the same time) and are best suited for homogeneous areas, where all farms have correlated yields.

A number of advantages are linked to the use of index-based systems:

- <u>Overcoming data availability problem:</u> these systems may prove useful in cases where it is difficult to carry out an assessment of production loss (e.g. permanent pasture, droughts, etc.) or where farm level data are not available, i.e. there is no obligation for small/medium holdings to keep accounts. Current insurance arrangements and practices could co-exist and be kept where successful, e.g. arable crops.

- Reduced moral hazard or adverse selection: the reliance on factors beyond the control of farmers and the presence of independently verifiable indexes reduce the occurrence of moral hazard and adverse selection (e.g. altering farm data and output, or only avail of the insurance when a claim is more likely).

- Lower deductibles: since behavioural problems are reduced under index-based systems, insurance companies would be likely to impose lower deductibles (while still respecting the 30% damage threshold as stipulated by the Regulation in case of support from the EAFRD).

- Low operational costs: index insurance products do not require underwriting and field inspections of individual farms, which can be very costly and time-consuming especially in remote rural areas.

However, a number of *concerns* also exist that could put applicability in the risk management framework of the second pillar into question:

- Area definition: it may prove difficult to define homogeneous areas or apply such systems where farming is more diverse.

- Availability of technology and information: despite fast technological development, it is currently still very difficult to reach single plots or very small farms via combinations of satellite and other types of information in order to establish adequate indexes, e.g. historical data for statistical forecasts, which are often not available. Therefore, lower operational costs may be offset by high initial design costs of the systems. Yet, technological advancements should soon allow detailed observations to be made at local and producer level (up to plots of 100 metres). Some indexes that are currently being developed and refined in a number of EU Member States can be considered as a satisfying proxy for individual production losses (with a limited margin of error of around 2-3%).

Against this background, index-based systems can be used for the calculation of production losses for the purposes of the rural development provisions on insurances and mutual funds (articles 38 and 39 of the draft Regulation), provided that **WTO green-box criteria are respected.** WTO green-box rules (paragraph 8 of Annex 2 to the WTO Agreement on Agriculture) stipulate that public support can be used only to compensate for the *actual* loss of an *individual* farmer. Therefore, index-based systems may qualify as WTO green-box compatible only if the index reflects an **adequate and satisfying proxy for the real individual production losses**, i.e. assuming a very limited margin of error (i.e. correlation close to 1), which is also endemic to the current widespread practice of field investigations. In fact, in case there is a poor correlation between the damages suffered and the index, there is a risk that a farmer who did not suffer damage might potentially benefit from compensation; equally, other farmers might not be fully compensated.

Member States shall ensure that the indexes used are adequate and accurate and the margin of error in assessing actual losses at the level of individual farms is minimal. To this end, a body that is functionally independent from any actor involved in the measures implementation – be it the public authority, the insurance company, any group/consortia acting as intermediary or the mutual fund – should provide a statement confirming these requirements.

9.3. Calculation of income

For the calculation of income, the WTO agreement requires that "income derived from agriculture" (and not "revenues") shall be taken into account.

As the WTO does not specify further the elements of the definition of "income", for the purposes of the newly introduced income stabilisation tool (IST), "income" is defined as "the sum of revenues the farmer receives from the market, including any form of public support, deducting input costs." This is based on Eurostat's Gross Farm Income[4].

In this context, public subsidies shall be included in the income equation, including direct payments alongside coupled support and any form of national subsidy.

The positive or negative variations in the farmer's stocks should also be taken into account when determining the average income, as the correct determination of stocks affects the level of gross production. In particular, the farmer must declare whether portions of the production in a given were not put on sale (placed in storage, set aside for seasoning, etc.) or, on the other hand, stocks of production boosted the overall income level of the farmer. In this case as well the controls are based on information derived from databases on prices and yields. Neither should any changes in stocks of raw materials be overlooked.

Other sources of income indirectly related to agricultural activity such as energy production or rural tourism should be excluded from the calculation for the purpose of the IST.

10. OUTPUT INDICATORS

Reference is to be made to the Working Paper "Elements of strategic programming for the period 2014-2020", Annex IV.

11. VERIFIABILITY AND CONTROLLABILITY

Reference should be made to the *"Guidelines on verifiability and prevention of errors"*

[4] The Gross Farm Income formula is output + subsidies - taxes - total intermediate consumption. "Subsidies" include direct and coupled payments, plus national subsidies; "total intermediate consumption" refers to variable input costs.

Annex I

RISK MANAGEMENT INSTRUMENTS UNDER THE FIRST PILLAR OF THE CAP

Relevant legislation:

- **Fruit and vegetables:** Articles 30-36 of Regulation (EC) No 1308/2013 (CMO)Regulation for post-2013 and Articles 88-90 of Commission Regulation (EC) No 543/2011

- **Wine:** Articles 39-51 of Regulation (EC) No 1308/2013 (CMO) Regulation and Articles 11-16 and 96 of Commission Regulation (EC) No 555/2008

11.1. Comparative table of available instruments for risk management

Type of tool	Sector/beneficiaries	Measure description and eligible costs	Trigger/Conditions	Aid rates and co-financing rates
Insurances	**PO in F&V (Articles 88-89 of R. 543/2011)**	**Harvest insurance actions** to be managed by a PO to contribute to safeguarding producers' incomes where there are losses as a consequence of natural disasters, climatic events and, where appropriate, diseases or pest infestations. Insurance contracts shall require that beneficiaries undertake the necessary risk prevention measures.	MS can decide whether to include crisis prevention and management in their operational programmes. If so, they shall adopt detailed provisions on the implementation of harvest insurance actions.	MS may grant additional national financing but the total public support may not exceed: – 80% of the cost of the insurance premium paid for insurances against losses as a result of adverse climate events which can be assimilated as natural disasters; – 50% of the cost of the insurance premiums paid against losses caused by: – adverse climate events, when including other elements than natural disasters. – animal or plant deceases or pest infestations. Supported insurance payment cannot exceed 100% of the income loss suffered or distort the insurance market.
	Wine (Article 49 of R. 1308/2013 (CMO) and Article 16 of R. 555/2008)	**Harvest insurance** to contribute to safeguarding producers' incomes where there are losses as a consequence of natural disasters, adverse climatic events, diseases or pest infestations. Insurance contracts shall require that beneficiaries undertake the necessary risk prevention measures.	MS can decide whether to include the measure in their national support programme for wine. If so: (a) MS shall adopt detailed provisions on the implementation of insurance measures, including those necessary to ensure no distortion of competition takes place;	Support may be granted in the form of a Union financed contribution from within the envelope assigned to the MS, which shall not exceed: – 80% of the cost of the insurance premium paid for insurances against losses as a result of adverse climate events which can be assimilated as natural disasters – 50% of the cost of the insurance premiums paid against losses caused by:

			(b) producers applying for the scheme shall make their insurance policy available to the national authorities; (c) member States shall fix ceilings on the amounts that may be received for the support. Where appropriate, MS may fix the level on the basis of standard costs and standard assumptions of income loss. Member States shall ensure that the calculations: (i) contain only elements that are verifiable; (ii) are based on figures established by appropriate expertise; (iii) indicate clearly the source of the figures; (iv) are differentiated to take into account regional or local site conditions as appropriate. ***<u>Derogation on payments (art. 96 of R. 555/2008):</u>*** As a derogation to the general rule that payments should be made in full to the beneficiaries, MS may	– adverse climate events, when including other elements than natural disasters; – animals, plant deceases or pest infestations. Supported insurance payment can not exceed 100% of the income loss suffered or distort the insurance market.

			decide to pay insurance support through insurance companies as intermediaries.	
Type of tool	**Sector/beneficiaries**	**Measure description and eligible costs**	**Trigger/Conditions**	**Aid rates and co-financing rates**
Setting up of Mutual funds & Payment of financial compensation to farmers	**PO in F&V (Article 90 of R. 543/2011)**	Support for the administrative cost of **setting up** mutual funds.	MS can decide whether to include crisis prevention and management in their operational programmes. Member States shall adopt detailed provisions for support for the administrative cost of setting up mutual funds.	The contribution is degressive over 3 years as follows: – 10%, 8% and 4% respectively in EU-12, – 5%, 4% and 2% respectively for other MS (Support shall comprise both the contribution from the Union and the contribution from the PO).
	Wine (Article 48 of R. 1308/2013 (CMO) and Article 15 of R. 555/2008)	Support for the **setting up of mutual funds** to provide assistance to producers seeking to insure themselves against market fluctuations.	MS can decide whether to include the measure in their national support programme for wine. If so, Member States shall adopt detailed provisions for support for the administrative cost of setting up mutual funds.	The EU contribution from the wine envelope is degressive over 3 years as follows: – 10%, 8% and 4% respectively in EU-12; – 5%, 4% and 2% respectively for other MS.