

## **WG 3: Incentive water pricing and cost recovery in the WFD**

### **Elements for linking EU Agricultural and Water Policies**

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## 1. Background

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Paper is to be seen in the context of:

- the SSG activities;
- the Ecologic/Warsaw University “policy-oriented research project” (DG research, 6.FP) on CAP&WFD

Builds on the 2000 EU-Communication on water pricing policies, focuses on water pricing in agriculture

Only some key issues to be presented here, opportunity for commenting is given to SSG members

## 2. Aims of paper

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- examine elements of the WFD that may have an effect on water pricing - i.e. the polluter-pays principle, cost-recovery and incentive pricing;
- give some indications on how to set up WFD-water pricing;
- relate them to the payment mechanisms of the CAP;
- identify crucial linkages, synergies and gaps in the joint policy framework of WFD+CAP;
- to provide basis for discussions and further work...

## Water pricing CAP & WFD

Number of WFD-elements could have effects on water pricing  
(focus here: agriculture, but valid also for urban, industrial):

- polluter-pays
- incentive pricing
- adequate cost-recovery

On the other hand:

- CAP payment mechanisms do influence incentives and decision-making in agriculture
- possible social and economic adverse impacts, to be addressed through CAP?

--> what are the links, how to improve them?

## 3. Water pricing in the WFD

Definition of water price is broad (see EU-Communication on water pricing, 2000):

„[...] amount paid by users for all the water services they receive (e.g., water distribution, wastewater treatment), including the environment. Thus, it encompasses elements linked to the quantity of water extracted from the environment and to the pollution emitted to the environment“

- concepts of Art.9 WFD: closely related, but not equivalent:
  - cost recovery: “how much is paid for water”
  - polluter-pays-principle: “who pays for water”
  - incentive pricing: “how is water paid for, what effects does water price have on water users behavior”

## Water pricing in the WFD



## Art. 9 WFD provisions: incentive pricing

**Incentive pricing:** Member States shall by 2010 ensure that:  
 “water pricing policies provide adequate incentives for users to use water efficiently and thereby contribute to the environmental objectives of the Directive”

MS “may have regard to social [...] and economic effects”

--> transparent and in-depth-analysis of options for incentive pricing (and cost recovery) and their effects is needed!

## Art. 9 WFD provisions: cost recovery

**Cost recovery:** Member States shall by 2010:

“take account of the principle of recovery of costs of water services including environmental and resource costs [...] and in accordance in particular to the PPP”

and ensure “adequate contribution of the different water uses, disaggregated into at least industry, households and agriculture, to the recovery of the costs of water services [...] taking into account the PPP”

Finally, MS “may have regard to social [...] and economic effects of the recovery”

--> no full cost recovery needed!

## Art. 9 WFD provisions: polluter-pays-principle

**Polluter-Pays-Principle:**

- part of Art. 9 (incentive pricing and cost recovery need to be in accordance with the polluter pays-principle)
- but also: general principle of the European Environmental Policy (and mentioned twice in Preamble of WFD)

-->of special relevance for agricultural sector: high levels of pollution caused by some agricultural water uses, high percentage of water used in agriculture

## WFD programmes of measures and water pricing

Art.11: “**Program of measures**” needed for every River Basin District”, needs to be cost-effective (meaning: lowest costs for reaching the environmental objectives)

--> need to look beyond traditional water management measures (e.g. new wastewater treatment plants etc.): water pricing, charges and taxes could be options

## Implementation of WFD-water pricing elements

- Clear interpretation of core concepts in practice needed: not easy (e.g. what are environmental & resource costs, what are water uses and services, what is “adequate contribution”, what are “adequate incentives” etc.)
- Adequate contributions to cost recovery: crucial for ensuring sustainability, both for infrastructure & environment
- Sufficient information needed (Art. 5 reports a starting point), e.g. on water consumption, areas cultivated, current cost recovery level, current incentives, value-added from agricultural water use, water price elasticity of water demand

## Implementation of WFD-water pricing elements

- Agricultural practice not (fully) consistent with Polluter-Pays, water pricing one option to improve
- Revision of water tariff schemes using environmental charges and taxes is one option
- Strong potential social and economic implications: need to be kept in mind
- Strong links with other policies/policy interventions, also with effects on incentives, e.g. CAP payments: check for synergies!

## 4. CAP payments and their effects

In order to better understand the relationship of WFD objectives to EU-agricultural policy:

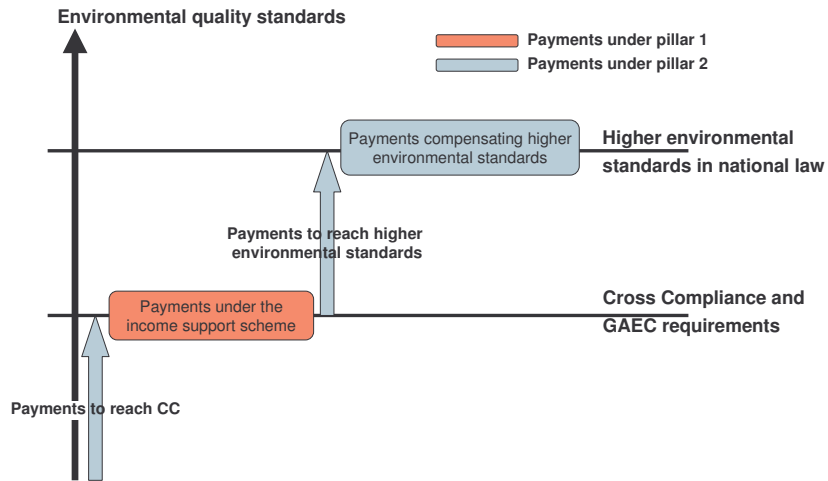
- What incentives related to environmental standards are connected to CAP payments?

Current CAP payments to farmers:

- Market and Income support (Pillar 1)
- Rural development (Pillar 2)

--> Structuring these payments according to their link to environmental quality standards

## CAP payments and environmental standards



## CAP payments and environmental standards

Some observations [categories not clear-cut, depend (also) on national implementation]:

- Payments to reach Cross Compliance standards have rather “low” incentive impact, since
- Payments under the income support scheme: more important (esp. some coupled payments can lead to high volume production)
- Payments for supporting higher standards than CC: “carrots” for rewarding environmentally friendly practices
- Payments for compensating higher environmental standards: tend to reduce the incentives transmitted through the water pricing system

## Role of decoupling for water protection

- “Decoupled” means CAP-payments that are not related to the type of production
- 3 Types of Payments under the income support scheme
  - 1) Coupled payments (e.g. rice)
  - 2) Partially Coupled payments
  - 3) Decoupled payments
- For several products MS can apply 2 or 3
- Decoupled payments provide less incentives for farmers to produce certain products
- Result: changes in production (less incentive/more incentive)

## 5. Main linkages on water pricing between WFD & CAP

Better, more detailed assessment of these linkages is needed, possible key issues:

- **Linkages on incentives:** how strong are the incentives/ distortions of CAP payments on farming decisions, how to transform them towards supporting the WFD objectives?
- **Linkages on proportionality/acceptability** of cost recovery/incentive pricing measures: WFD pricing could lead to social /economic hardship for agriculture, so: need to consider both the objectives and provisions of WFD (criteria for social hardship/disproportionality etc.) and CAP (aiming at providing farmers with a reasonable standard of living) for the evaluation process

## Main linkages on water pricing between WFD & CAP

### Linkages on the compensation function:

social/economic hardship may arise through WFD implementation; compensation through RD regulation most probably not sufficient; additional sources of funding needed

Options (in case water-related green taxes and charges are used):

- a. earmarking revenue from agriculture for agriculture-related measures in the “programme of measures”-WFD (water efficiency measures etc.);
- b. using revenue for financing national contributions to RD payments

--> creating “double divided”: correcting incentives & finance environmentally beneficial measures!

## 6. (Some) Key messages

- Water pricing can be a powerful measure for reaching WFD objectives (internalising environmental costs, incentive function) and for ensuring the viability of agriculture in Europe by e.g. ensuring financing for (maintaining) infrastructure
- At the same time, CAP payments have large influence on decision making and cost recovery aspects in agriculture, therefore better links/less contradictory incentives are needed
- Facing social and economic effects of WFD implementation for agriculture is crucial; so, linking “disproportionate costs” (WFD) with “reasonable standards of living” (CAP) would be beneficial
- Most likely that a new package of additional measures and full implementation of existing EU legislation by member states will be needed

### Leading questions for WG discussion:

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- What is the importance of water pricing incentives and incentives from CAP payments for sustainable water use?
- What are the main potential links on the financial aspects of WFD implementation and CAP reform?
- What options are there for dealing with social and economic hardships resulting out of WFD implementation measures for agriculture?
- [Questions from your side?]