Basic Material

Working Group 7.1

SUPPORT TO SMALL FARMS

Specific objective:

"Encourage diversification of small farms towards alternative crops, added value products and methods of production, innovative market distribution, use of the labels informing consumers on specific production methods and direct marketing, other forms of organisation and activities which could provide additional source of income, in particular for young farmers who wish to develop small and medium-sized farms. Facilitate access to micro financing in order to promote such diversification, entrepreneurship and value added. Develop economic activities for farmers outside agriculture, in particular by supporting rural tourism initiatives in the most promising areas (e.g. landscape, cultural heritage, infrastructures) possibly by initiating a limited number of local pilot projects."

1. Inventory and synthesis of all useful documents and background information

1.1. State of play and general assessment

**Rural development** means a purposeful change in institutional, economic, environmental, demographic, social, cultural, household and other most important factors which determine the areas and directly affect the growth of level and quality of the rural population life and ensures prevention or overcoming of poverty rather than just more comfortable existence under poverty conditions.

Rural development is based on a full exercise of rights of ownership/use, efficient use and control over local resources by local communities.

**Rural family farm** is a way to organise agriculture, forestry, fishery, pasture or aquaculture production which is exercised and managed by a family and based primarily on the labour of family members, both male and female.

The social role of domestic agriculture can be revived by developing the rural family farmer setup, which improves the resistance of the agri-food system to global challenges, fosters development of the competitive environment in the agrarian sector based on equal treatment of business entities, makes rational use of natural resources, increases in household incomes, and reduces poverty in rural areas.

There are 40,700 farms (8,100 [20%] of which cultivate up to 10 ha of land) and 4,200,000 small holdings cultivating 1.5 ha of land on average in Ukraine. They produce more than 50% of gross agricultural produce, including 97% of potatoes, 82% to 85% of vegetables, fruit, and berries, nearly 80% of milk, and more than 40% of meat. While meeting the demand of
the domestic market for labour-intensive and commercially unattractive for other producers of food products; they allow the corporate sector enterprises to boost the production of export-oriented types of agricultural produce. Small holdings and family farms provide job to 80% of people employed in the agriculture sector.

Small holdings (individual homesteads, rural households) are the most common and numerous representatives of family-type entities operating in the agrarian sector of the Ukrainian economy. Although some of them already operate as family farms, there is no legislative framework which would create legal, economic, and social preconditions for transforming them in family farms with the status of agriculture producer. The lack of such a status precludes them from being fully-fledged participants to the agrarian market. In addition, they are not covered by the social protection system, as the period of their operations is not included in the covered service period in terms of the pension system.

Experience of many European countries shows another strong point of family farms: in the production or service rendering process, farmers develop and accumulate relevant professional skills and experience and transfer them to young people. This lays a foundation for stable employment in rural areas and development of the rural economy.

A new type of business entities – rural family farms – should be created on a voluntary basis. Nobody should force small holdings to register themselves unless they are willing to do so on their own for personal considerations and expectations of economic benefits. Another reason for singling out a family farm in the agriculture is that its performance is greatly dependent on natural factors, and this calls for a special (high priority) and ongoing support from the government. Therefore, singling out this form of family farming is objectively necessary and practically significant.

1.2. *Main challenges / main strengths*

Listed below are major hindrances to development of small holdings:

1. Unfavorable institutional environment:
   - unawareness of the socio-economic importance of small agriculture producers for agrarian and rural development cultivation of the idea of the secondary nature and absence of any prospects for small holdings
   - non-observance of the declared principle of equal rights of various forms of business, granting real advantages to large-scale commercial production
   - absence of a stimulating influence of government institutions
   - lack of cohesion among small holdings, inability to influence the agenda of the state agrarian policy

2. Economic discrimination:
   - lack special programmes to support small holdings' competitiveness
   - limited access to existing mechanisms of government support of the agrarian sector
   - complicated access to finance, land and material-and-technical resources, and distribution channels

3. Socio-demographic limitations:
   - low educational and professional level of rural populations
   - exhaustion of the labour potential in rural areas
   - social isolation of rural areas, absence of programmes for developing human and social capital
- lack of motivation among young people to work on family farms

4. Lack of an adequate legislative framework of rural development:
- lack of national, regional or local rural development programmes
- inadequacy of the current legislative and regulatory frameworks (lack of certain laws and regulations or gaps therein, prevalence of dysfunctional clauses that are of general nature, lack or inconsistency of rural development terminology, conflicts of existing laws and regulations, lack of a rural development code etc.)
- lack of special programmes to support small holdings' competitiveness
- failure to regulate matters associated with employment and social protection of small holding members.

Achievements. In the period of market transformations, internal structuring took place in the environment of small holdings. More than 40% of small holdings grow the produce for their own consumption, and one third of them sell some smaller amounts at markets. These farms belong to the subsistence (Subsistence) and semi-subsistence (Semi-subsistence) types, respectively. Nearly 20% of small holdings belong to the category of market-oriented (Commercial) farms with sales of agricultural produce in access of an equivalent $1,000. This category of producers is comprised of about 800,000 to 900,000 small family-type farms. 30-35% of these farms comprise middle-aged and mixed-age persons the lowest proportion of market-oriented farms is among young families without children and pensioners' families. Young families with small children occupy an intermediate position among the abovementioned PPF groups. Since the market-oriented personal peasant farms are concentrated in one of the most active social groups of rural families, which have the greatest need in improving their material welfare, providing them support in increasing production of marketable produce and arranging for its profitable sales, their integration in the market environment of agrarian sector operation could all provide positive results in the short term.

Strengths
- an important role in reducing the incidence of poverty; important contribution to increasing the level of food security, population nutrition and welfare; production of individual foods reflecting the priorities and preferences of domestic consumers
- empowering and social responsibility: more equitable economic opportunities for rural residents, responsibility for oneself and one's family, social interaction (social capital)
- economic base for activity in rural areas: employment, income, local food markets, payments into local budgets, contribution to support of rural infrastructure
- personal interaction with the food system through establishment of direct links with consumers who gain direct access to food flows (short agro-food chains)
- sustainable use of natural resources (including the smallest, irregularly-shaped etc. plots of land); personal interest in protecting the environment and sustainable development
- environmental safety: a more responsible use of natural properties of soil, potable water, and other elements of wildlife, which provides significant environmental benefits to the society
- ensuring the diversity of business patterns, land cultivation systems, use of landscapes, culture, and traditions
1.3. Policy options for reform

**Policy Option 1:** Enhancing the legislative and regulatory frameworks of small holding.

1.1. Develop and adopt the Law of Ukraine "On Agrarian System in Ukraine."

The Law should formalize the existing agrarian system, which is currently represented by three groups of agricultural producers:

- family farms (farm enterprises and personal peasant farms of commercial, semi-subistence, and subsistence types)
- corporate farms (farming companies, private leased enterprises, production co-ops etc., and some farm enterprises set up as private leased enterprises based on lease of land and property of the former collective agricultural enterprises)
- agri-industrial corporations as vertically integrated structures (agricultural holding companies).

It is necessary to clearly set the criteria under which a given business entity shall be referred to one of the three producer groups in order to implement the state policy, which would be differentiated with regard to each of them.

The Law "On the Agrarian System in Ukraine" will primarily protect family (small) economic formats and will bind to create the economic, organisational, and social conditions for their continued development. The Law will secure the family type of economic activity in agriculture as part of the organisational structure of the country's agro-food system. At the same time, it should not infringe on operation of any other economic formations; however, it should set the rules for their economic activity and promote the development of a multifunctional agriculture.

1.2. Amend the Civil Code of Ukraine to legislate rural family farms as a special form of economic activity on land without acquiring the status of a business entity or individual entrepreneur.

1.3. Develop and adopt amendments to the Tax Code of Ukraine with regard to clarifying the status of agricultural producers.

1.4. Introduce a preferential system of social insurance for the individuals employed in rural family farms, which would motivate them to self-identification and registration as farms with a formalized employment of their members. Develop and approve the Law of Ukraine "On Special Features in Social Security of Peasants" or amend and supplement the existing legislation on social security of citizens, which should stipulate the participation of the State in social security of members of rural family farms.

1.5. Develop and adopt the Law of Ukraine "On Groups of Small Commercial Farms and Their Associations in the Agrarian Sector" (must be reconciled with 5.3). Adoption of the Law will create the legal foundations for organisation by rural family farms of groups and nonprofit production associations intended for improving competitiveness of those farms.

**Policy Option 2:** Improve access to production and financial resources for rural family farms.
2.1. The legislative recognition of the right of priority purchase of land for agricultural production by those living on and by the land (include the relevant provisions in the Draft Law of Ukraine "On the Land Market").

2.2. Implement the mechanisms of priority realization of interests of rural family farms in the process of market circulation of agricultural land.

2.3. Set up self-crediting funds of rural family farms:
  * support the information and organisational work to set up self-crediting groups
  * provide subsidies for increasing self-crediting funds.

2.4. Develop and implement a mechanism of subsidies for rural family farms to cover part of their cost of paying interest on loans.

2.5. Ensure access to purchase of equipment on leasing terms.

**Policy Option 3: Implement social programmes for support of rural family farms in order to:**

3.1. Develop certified organic agriculture (payments per hectare).

3.2. Operation in special, difficult natural conditions (compensation payments).

3.3. Remove degraded, low-productivity land from active cultivation and implement environmentally-friendly farming on such land: conservation of land with creation of grassland, planting woodland belts and planted forests (subsidies per hectare).

3.4. Diversify activities: grow alternative crops, improve methods of production, and practice innovative market distribution, use marks of special produce status, green rural tourism etc. (grant per farm).

3.5. Develop animal husbandry (stimulate increased production output with observance of sanitary standards and regulations, technical and technological modernization etc.).

3.6. Train young people as multifunctional specialists able to conduct agricultural production based on family farming (grants for study and business startup).

3.7. Establish a network of slaughterhouses for cattle and poultry based on Public-Private / Public-Community Partnerships.

**Policy Option 4: Stimulate integration of rural family farms into value-added chains based on development of partnerships, collective actions, and cooperation.**

4.1. Create local educational networks and provide support to building the capacity of rural family farms to integrate, create, master, and professionally manage value-added chains.

4.2. Develop economic stimuli to expanding the processes of integration of rural family farms into value-added chains of vertically integrated structures.

4.3. Develop guarantee mechanisms for rural family farms to gain the benefits from market participation in value-added chains.

4.4. Implement the arrangements of stimulating the performance of contracts and obtaining a fair compensation for participation in the chains by all parties.

**Policy Option 5: Strengthen the functions of support of rural family farms in operation of the state agriculture and rural regulatory bodies.**

5.1. Amend the standard statutes of local agribusiness development directorates with regard to a more specific description of their tasks related to organisational support of rural family farms as an important segment of agricultural producers.

5.2. Provide retraining of the staff of local agribusiness development directorates with the aim of arming them with the necessary knowledge, skills, and information for providing support (organisational, technological, advisory etc.) to rural family farms.
5.3. Establish base points and mechanisms of communication between the agribusiness development directorates and rural family farms for providing support at the local level
5.4. Develop training programmes and organise training for improving qualifications of the members of rural family farms.

Policy Option 6: Build a network of non-governmental and other organisations and associations to protect the interests of rural family farms and economic rights of village communities.

6.1. Initiate and support the creation of a network of local and regional associations of rural family farms using the resources of the National Association of Agricultural Advisory Services of Ukraine and the All-Ukraine Association of Village and Settlement Councils.
6.2. Build a national team of experts who will represent the interest of rural family farms before executive authorities, and include such experts in the composition of the Community Board at the Ministry of Agrarian Policy and Food of Ukraine.

Anticipated Results - development of a family-based peasant/farmer system as a fully-fledged part of the domestic agro-food system will bring about positive social, sectoral, and local economic effects.

Social:
- the level of country's food self-sufficiency will be increased, especially in the environment of global natural and economic crises, thanks to that the peasant farms continue operation with significantly lower income than corporate farms
- the agriculture sector will increase its capability of producing such important public goods as food security, support of life in rural areas, reproduction of the rural population as a medium of the national identify and farming culture
- the pace of reduction of the network of rural settlements and decolonization of settled territories will slow down thanks to the preservation of community's control over them.

Sectoral:
- deformations and disparities in the organisational, sectoral, and food structure of agricultural production will be mitigated
- economic competitiveness will be strengthened of business entities in the agrarian sector, which will increase its operational efficiency
- transparency will improve of using the funds for support of the agrarian sector and access to such funds for the entities of various organisational and legal forms and sizes
- opportunities will grow for increasing the agricultural production on the principles of sustainability due to allocating the state support for achievement of the objectives of agricultural development

Local economic development:
- stronger economic base for development of rural communities
- development of local food markets, markets of production and credit resources, information networks etc.
- improved access of rural population to the economic benefits from the agrarian sector growth, higher employment and income of the rural population
- better opportunities for quality renewal of human capital, development of social capital and greater cohesion of village communities.

1.4. Reasons why these actions have not been implemented yet
- Lack of budget funds for the envisaged measures
- Lack of an organised lobby to promote small producers' interests
- Lack of government policies for developing small producers in rural areas


The Coalition Agreement envisages a number of measures which are directly associated with support to small farms, specifically:

- Involving in the organised agrarian market small business entities and the self-employed (small holdings) legislating family farms and granting the agriculture producer status to them; developing small and family farms based on cooperation and association principles;
- Reforming the government support system and mobilizing funding.

The Government Action Plan includes the following measures;

- Support and development of small and medium-sized businesses in rural areas:
  o To draft and pass the Law of Ukraine "On local agrarian markets";
  o To adopt and implement a micro lending programme for small holdings.

3. Link with the EU-Ukraine Association Agreement

The proposals will be reconciled with the areas of cooperation in the sphere of agriculture and rural development under EU-Ukraine Association Agreement (Section V: Economic and Sectoral Cooperation; Chapter 17: Agriculture and Rural Development, Articles 403, 404.

4. Current Legislative and Regulatory Frameworks

The current legislative framework of small holding and family farm development is inadequate. It includes: (1) Law of Ukraine "On high priority of social development of rural areas and agri-industrial complex in the national economy"; (2) Land Code of Ukraine; (3) Tax Code of Ukraine; (4) Law of Ukraine "On a farm"; (5) Law of Ukraine "On a small holding"; (6) Law of Ukraine "On government support of agriculture"; (7) Law of Ukraine "On agriculture census". The current legislation envisages development of small holdings which, however, do not have the agriculture producer status, thus being unable to participate in government programmes for supporting agriculture producers. Farms, in turn, may be set up solely as legal entities which may be founded by a wide range of persons. Free transfer of the ownership of a few (2 to 5) hectares of agriculture land is the only realistic form of government support to small holdings and farms. For the purpose of enhancing the legal status of rural family farms, the draft laws of Ukraine "On amending selected acts of the Ukrainian legislation with regard to stimulating family farm development" and "On amending the Tax Code of Ukraine (with regard to stimulating family farm development" have been developed and sent to the Parliament.
5. References

5.1. Bibliography
Not specified

5.2. List of relevant projects and funding
Not specified

Annexes

1. European approach to define rural areas
2. The management structure of rural development

DISCLAIMER

This basic material has been prepared by the working groups, established by the Ministry of Agrarian Policy and Food of Ukraine, to facilitate the public consultation on the specific objectives of the Strategy for Agriculture and Rural Development 2015 – 2020. The information and views set out in this document reflect solely the opinion of the working group that prepared it and do not necessarily reflect the official opinion of the Ministry of Agrarian Policy and Food. Neither the Ministry of Agrarian Policy and Food of Ukraine nor any person acting on their behalf may be held responsible for the use which may be made of the information contained therein.
Annex

1. European approach to define rural areas

European Commission is using traditionally the methodology with the three level region classification of NUTS\(^1\) system adopted by the Organization of Economic Cooperation and Development (OECD) when planning activities for rural improvement.

Population density, particularly if the figure is less than 150 persons per km\(^2\) is the criteria of NUTS 1 level (land, municipalities, etc., in other words large regions) for rural area. Regarding smaller subdivisions of NUTS 2 and NUTS 3 levels, definition of the territorial membership either to rural or urban is performed by the following classification:

- mainly rural areas, characterized by a predominance of rural population (more than 50% of the population lives in rural area) and high population density (up to 150 person per square meter) and poorly developed social infrastructure, which limits the creation of alternative employment places;
- economically integrated or mixed territories with well-defined rural areas (from 15 to 50% population lives in rural area) that have relatively favorable economic development conditions and are usually located in the areas connected to highways;
- mainly urban or urbanized territories (less than 15% of the population lives in rural area) which are located at a small distance from developed urban centers with its future possible transfer into urban territories and loss of cultural features and natural landscapes.

Despite this methodology not being ideal, in particular regarding density where there is some distortion of the reality, it is the only one internationally recognized and implemented in practice. According to this rural area typology EU conducts its regional policy in the two following strategic areas: first, performance of economic reforms with the definition of state support level; second, intensive performance of diversification production process. Analysis of territorial development level shows that social and economic disparities within EU are quite significant. As a rule, first to feel the mentioned negative effects are under developed rural areas that exist in all mentioned above EU regions.


2. The management structure of rural development

Rural development requires efforts consolidation and coordination of state executive authority activities and local governments, public and SROs, businesses, investors, individuals etc. which in its turn necessitates adequate organizational support. With that purpose number of structural changes should be implemented.

1. At the national level State Agency of Rural Development (hereinafter –Agency) should be created as the central body for State Executive Authority which activity is directed by Cabinet of Ministers of Ukraine. The Agency will be included to the system of state executive authority, should be main in the system of central state executive authority, forming and implementing national policy in rural development sphere on public-private partnership. The Agency will coordinate work of all central state executive authorities, for which rural area is their activity and responsibility regarding implementation of programs and measures in rural development. It should receive functions of

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\(^1\) NUTS – the Nomenclature of Territorial Units for Statistics, developed by European Statistical Office (Eurostat) to ensure single and coherent territorial division structure.
organizational and budget financing (on a competitive basis) of consultancy support for rural development (including in particular social work in rural communities of forming initiative groups, teaching of leaders and activists of rural communities).

2. The functions of working Agency body can be done by the rural development department of Ministry of Agriculture. Through the acquisition of these new functions the Ministry should change its name to Ministry of Agricultural Policy and Rural Development of Ukraine.

3. On the regional level (in the Council of Ministers of AR Crimea and oblast state administrations) and also on the local level (regional state administrations) structural units should be distinguished which are representatives of the Agency locally (hereinafter Representative). They will ensure national policy implementation regarding rural development and will coordinate relevant work of regional and local executive authorities.

4. Regional representatives of the Agency will sign agreements for educational and consultancy service of rural community with certified consultancy advisory services with the purpose to enhance readiness of these communities for self-development (including formation of initiative groups, training leaders and activists of rural communities, search and attraction of investors). They should provide this work through consultants that live and work in rural area on a permanent basis. As a result, there will be a possibility for direct communication of central executive authority with rural communities regarding rural development issues (including control over target fund income allocated for rural development implementation, to the end beneficiary – rural community). This makes a foundation of new institutional framework to combine agricultural and rural development through direct involvement of rural population.

5. Interagency competition commissions will be created at district state administrations to choose projects for local development (hereinafter – Commission) that will apply for organizations on the basis of rural communities to receive financial support from state and local budgets. The Commission should be formed from representatives of local councils, people’s deputies, and local state administrations, employees of agricultural education, science, advisory services, NGOs, village mayors, rural community leaders and potential investors. The total number of Commission members should not exceed 13 persons, from which representatives of rural community should not be less than one third. The Chairman of the Commission is elected by the members of its structure but not from the civil servants. Regulations on commission and the order of local development projects selection are developed by the Agency and approved by the Cabinet of Ministers of Ukraine.

6. In order to achieve objectives of interconnected agricultural and rural development, the agricultural educational system, training and retraining should be reoriented. For this purpose new specialities should be established, teaching methods developed, relevant educational programs created. Teaching and educational process should be combined with practical work in rural communities. Positive aspects of rural life area in modern globalized world should be displayed in secondary school programs.