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REPORT FROM THE COMMISSION TO THE COUNCIL

**Review of the transitional measures regarding the acquisition of agricultural real estate
foreseen in the Accession Treaty 2005**

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SUMMARY

The Accession Treaty signed in 2005 with Bulgaria and Romania¹ establishes a transitional period of seven years (from 2007 to 2014) allowing these Member States to maintain existing restrictions on the acquisition of agricultural and forestry land by natural and legal persons of other EU/EEA countries. It also stipulates that, in the third year after accession, these transitional measures should be reviewed by the Commission.²

The objective of this report is to review these temporary restrictions and their effects in order to report on the potential for shortening or terminating the transitional period ahead of the date stipulated in the Accession Treaty. In view of this objective, a study was commissioned in 2009. The study and this report conclude that:

- There is no total ban on farmland acquisitions in Bulgaria and Romania. Therefore, despite temporary restrictions, a considerable foreign presence (in the form of incorporation of new companies or participation in the resident ones, establishment by EU citizens as self-employed farmers and renting agricultural land) has been accommodated without any visible shock to the system. In the light of limited access to capital and land fragmentation in the two Member States concerned, this foreign investment could even be seen as helping to resolve some institutional restraints. Foreign investors' activities may result in a positive impact on agricultural reform in Bulgaria and Romania, through introducing new technologies, providing much-needed capital for production, rationalising the use of land and enhancing land values.
- The gap in terms of income and land sales' prices in Bulgaria and Romania as compared to the other EU Member States is narrowing over time but is still considerable and well short of complete convergence. However, a narrowing of this gap was neither expected nor was it seen as a necessary condition for terminating the derogations.
- Socio-economic indicators for agricultural production are improving, and this positive trend is expected to continue. However, an important gap between the two new Member States and the other EU Member States in terms of productivity and share of agricultural employment in total employment still remains.

Although the period of time covered in preparation of this report is necessarily short, based on the situation in Bulgaria and Romania, as established in the mid-term review, **the Commission concludes that the time limits for the application of the transitional restrictive measures on farmland acquisitions should not be shortened.**

At the same time, the Commission underlines the importance for these two Member States to put the remainder of the transitional period to good use in fostering the development of the agricultural sector. In the Commission's opinion, considering opening further agricultural markets to foreign investment through moderate measures even before the expiry of the

¹ OJ L 157 of 21 June 2005, page 11.

² Article 3.2 of Annexes VI and VII to the Accession Protocol provides: *"To this effect, the Commission shall submit a report to the Council. The Council may, acting unanimously on a proposal from the Commission, decide to shorten or terminate the transitional period..."*

transitional period would appear beneficial in promoting the competitiveness of the Bulgarian and Romanian agricultural sector. In this regard, certain measures can be recommended to be taken on a voluntary basis:

- allowing EU foreigners, not established in EU2, to freely acquire a certain amount of the country's agricultural area;
- allowing EU foreigners, not established in EU2, to freely acquire a certain amount of farmland, up to a specified maximum amount per transaction, possibly combined in each transaction with a requirement for certain investments in technological innovation to be made;
- permitting EU foreigners not established in EU2 but renting agricultural properties there to freely acquire farm buildings and the land on which they are built.

REPORT FROM THE COMMISSION TO THE COUNCIL

Review of the transitional measures regarding the acquisition of agricultural real estate foreseen in the Accession Treaty 2005

The Commission is presenting this report to the Council in accordance with the Protocol concerning the conditions and arrangements for admission of the Republics of Bulgaria and Romania to the European Union. The Protocol and its Annexes VI and VII contain the conditions foreseen for the application of transitional measures, including the transitional periods during which existing restrictions on the purchase of agricultural land, forests and forestry land by nationals and legal persons of other EU/EEA countries may be maintained. Both Annexes stipulate that a general review of these transitional measures, in the form of a Commission report to the Council, should be held in the third year following the date of accession.

In the light of this obligation, a consultant³ carried out a study⁴, analysing the impact of transitional measures on the agricultural sector in Bulgaria and Romania (hereinafter referred to as EU2).

1. Legal basis for the Commission report

Article 63 TFEU enshrines the fundamental freedom of capital movements⁵ that encompasses, amongst others, a free investment regime for real estate acquisitions⁶.

The Accession Treaty signed with Bulgaria and Romania in 2005 foresees that, in derogation of the Treaty freedom of capital movements, both new Member States are **granted a seven-year transitional period** from 2007 (date of accession) to 2014, during which they may **maintain restrictions** existing in their legislation at the date of signature of the Accession Treaty with respect to the **acquisition of agricultural land, forests and forestry land**.

Article 20 of the Protocol concerning the conditions and arrangements for admission of the Republics of Bulgaria and Romania to the European Union stipulates that the above-mentioned transitional measures are to be applied under the conditions laid down in its Annex VI (Bulgaria) and Annex VII (Romania).

The Annexes state that "*a **general review** of these transitional measures shall be held in the third year following the date of accession. To this effect, the **Commission shall submit a report to the Council**. The Council may, acting unanimously on a proposal from the Commission, decide to shorten or terminate the transitional period...*"

2. The transitional arrangements

In the accession negotiations, similar concerns to those raised by seven of the ten States that joined the EU in 2004, drove Bulgaria and Romania to request a transitional period regarding the acquisition of agricultural land by nationals of other EU Member States and legal persons formed in accordance with the laws of another Member State which are neither established

³ Centre for European Policy Studies (CEPS).

⁴ "Review of the Transitional Restrictions Maintained by Bulgaria and Romania with regard to the Acquisitions of Agricultural Real Estate", hereinafter referred to as CEPS study 2010 http://ec.europa.eu/internal_market/capital/reports.

⁵ See nomenclature of capital movements set out in Annex I to Council Directive 88/361/EEC of 24 June 1988 for the implementation of Article 67 of the Treaty (OJ 1988 L 178, p. 5). Although this Directive was repealed by the Maastricht Treaty, the nomenclature is recognised by the Court of Justice of the European Union as having indicative value.

⁶ The 5-year transitional period granted to Bulgaria and Romania with respect to the acquisition of real estate for secondary residences is not subject to this report.

nor registered in Romania and Bulgaria⁷ (hereinafter referred to as EU foreigners). The main reason for this request would appear to be **a need to safeguard the socio-economic conditions for agricultural activities in the wake of the introduction of the single market and the transition to the Common Agricultural Policy**. The transitional measures are intended to **soften the impact of an open market for agricultural real estate in the EU2** resulting from their relatively low level of land purchase prices and farmers' income compared to the rest of the EU (hereinafter referred to as the EU25). However, since restrictions on foreign investment might have a negative impact on the development of the agricultural sector, and in particular on its productivity, technological innovation and competitiveness, Bulgaria and Romania may only apply their restrictive provisions for a transitional period limited to seven years (2007 to 2014).

3. Objectives of the report

The Commission's objective is to review the impact of accession and temporary restrictions on the agricultural sector in the EU2. It will also consider the ongoing relevance of the concerns that led Bulgaria and Romania to request transitional periods for the free acquisition of agricultural land. This will enable the Commission to assess the need to maintain the transitional measures for the foreseen transitional period and **to report on the feasibility for shortening or terminating it ahead of 2014, the date stipulated in the Accession Treaty**. The Commission's assessment was preceded by a CEPS study 2010 containing a survey and analysis of the developments that took place in the EU2 since their accession negotiations and their comparison with the situation in the EU25.

4. Methodological approach

To understand the current and future impact of the land ownership restrictions, the study focused on two questions: (i) to what extent do the restrictions on foreign ownership affect the efficiency of land exchanges, land allocation and productivity growth, and (ii) to what extent are the factors underlying the Bulgarian and Romanian concerns (that there would be a massive takeover of land by foreigners if the restrictions were not in place) still valid.

The survey focused on the following main issues: a comparative analysis of EU2 transitional restrictions; other factors affecting the markets for agricultural land and land transactions; how agricultural land markets have developed over recent years, in particular in terms of land and rental prices, the development of agricultural income and its degree of convergence with the EU25; and an analysis of some key indicators of agricultural performance in the EU2 compared to corresponding EU25 indicators.

5. Overview of the situation after three years of EU membership

Foreign ownership restrictions and functioning of the land markets

The restrictions introduced by Bulgaria and Romania concern *foreign* (i.e. only non-resident farmers and legal entities) *ownership* (but not renting) of agricultural land. Since the restrictions imposed on farmland acquisitions by foreigners in the EU2 are of a limited nature, it should be stressed that efficient farmland transactions seem to be impeded also by a variety of other factors, for example: (i) constraints and imperfections in *capital markets* resulting in the inevitable necessity for farmers to finance land purchases out of own savings; (ii) *land fragmentation* limiting the sales of farmland since purchasers are more interested in buying consolidated areas; (iii) *high administrative costs* connected to land transactions and protection of property rights.

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According to the explicit wording of the Accession Treaty, immediately after accession all the above-mentioned rules are also directly applicable to EEA nationals and legal entities.

Legal restrictions on the acquisition of agricultural land by foreigners applicable in EU2

The Accession Treaty with Bulgaria and Romania stipulates the possibility to maintain, for a transitional period of seven years after accession, national rules according to which EU foreigners cannot, generally, acquire agricultural land. However, under certain conditions, EU foreigners have been able to acquire agricultural land in EU2 already during the transitional period. Furthermore, in both countries EU foreigners may freely rent agricultural land.

In Bulgaria and Romania, **the acquisition of agricultural land by EU foreigners has been regulated in a similar way:**

(i) **EU citizens** who wish to establish themselves as self-employed farmers and acquire agricultural land in Bulgaria and Romania are neither subject to any restrictions nor to any procedures different from those applicable to nationals; (ii) **Legal entities established in Bulgaria or Romania** can also freely acquire agricultural land in either State, irrespective of the level of foreign participation in their capital.

These investment possibilities for EU foreigners prove that the restrictions applicable in the EU2 are less restrictive than those existing in some of the States that joined the EU in 2004 and asked for a transitional period on the acquisition of farmland (hereinafter referred to as the EU7 countries⁸). The main difference is that Bulgaria and Romania have no restrictions on land acquisitions by legal entities established on their territory, regardless of the foreign participation in the capital of those entities. It should also be underlined that Bulgaria and Romania have established less restrictive conditions to be met by EU citizens before establishing themselves as self-employed farmers and making use of their right to acquire farmland in these countries. There is however no official data on foreign ownership of farmland in Bulgaria and Romania, so that the impact of the restrictions cannot be easily estimated. Nevertheless, information collected from various sources by national land experts participating in the study⁹ suggests that there is substantial foreign ownership of agricultural real estate in both countries. Acquisition of land by foreign investors was clearly boosted as a result of the restitution of land to private owners.

The legal restrictions governing the acquisition of agricultural land by EU foreigners in Bulgaria and Romania illustrate that a strict and total ban on foreign acquisitions is not in place and may therefore not be viewed as essential for the achievement of the objectives pursued by the introduction of the transitional period.

Foreign direct investments

An increase in foreign direct investment (FDI) in agriculture would have an important impact on much needed access to capital, technology and know-how in the sector. Of a total FDI stock in Bulgaria of some €32 billion by 2008 and some €43 billion by 2007 in Romania, FDI that has gone into the agricultural sector in Bulgaria amounts to €166 million and to €280 million in Romania. Although of relatively minor amounts, these investments, together with stimulating (vertical) spill-over effects coming from FDI in related sectors (e.g. in the food sector), have a positive impact on the enhancement of agricultural productivity and land value.

Influence of EU accession on EU2 land markets

Despite the (partial) restrictions on foreign investment covering the agricultural sector, EU accession has already positively influenced the development of this sector. By stimulating

⁸ These are the Czech Republic, Estonia, Latvia, Lithuania, Hungary, Poland and Slovakia.

⁹ See the explanations and examples proposed in section 4 and section 6 of the CEPS study 2010.

foreign investments in the overall economy of the EU2 and by facilitating the growth of the financial sector, EU accession improved access to credit and insurance for farmers, which resulted in an enhancement of agricultural productivity, an increased demand for land and a rise in land values.

Furthermore, subsidies for EU2 farms connected to the Common Agricultural Policy (CAP), although still at a lower level compared to the subsidies available to farms in other EU Member States, account for an important part of farmers' income in the EU2. Since most of the subsidies are linked either to land or to output, they encourage demand for land and stimulate increased productivity.

Changing land markets in EU2

The overall size of the **land sales market** in Bulgaria and Romania is small. In Bulgaria, ca. 140.000 ha agricultural land was transacted through sales by 2008. In Romania, farmland exchanges through sales amounted to ca. 220.000 ha by 2009. However, in both countries, the area transacted through sales for the period 1999 – 2008 increased seven times. Around the accession period, sales of land grew in Bulgaria by 45% (in the period 2006 – 2008) and more than tripled in Romania (in the period 2005-2009).

Although the land sales markets seem to develop in a similar way in the EU2, the **land rental markets** differ considerably. Renting is much less important in Romania than in Bulgaria. Within the EU27, Romania has the lowest renting share¹⁰, although it has increased in recent years. In Romania, as in other countries, land renting is more important for larger legal entities which rent more than one-third of the land they use (36% in 2007). However, in 2007, only around 35% of the total agricultural area in Romania was used by corporate farms while legal entities in Bulgaria held around 53% of the total farmland.

The study used national sources to obtain statistics for **land sales and rental prices**. After accession the overall rental prices increased only moderately¹¹. By contrast, in the years around and after accession, the increase in the land sales prices was considerable.

In the pre-accession period (2004-2006), land sales prices in Bulgaria grew by 24% (to the level of 895 €/ha). After accession, land sales prices in Bulgaria increased by 34% compared to the pre-accession period and reached, in 2007-2008, a level of 1202 €/ha. In Romania, in the pre-accession period (2004-2005), land sales prices increased by more than 200% to around 900 €/ha, with a particularly sharp increase in 2005, the year when the Accession Treaty was signed. After accession, agricultural land sales prices further increased by more than 50% compared to the pre-accession period, to 1400 €/ha in 2008.

As a result of the above-illustrated increase in land sales prices in Bulgaria and Romania, the gap in land prices between these two countries and the EU25 is decreasing. Nonetheless, there is still a noticeable difference between the land prices in the EU2 and those in the EU15 (EU Member States before 1 May 2004). By contrast, land sales prices in the EU2 are now comparable to those in EU7¹².

However, bearing in mind that rental markets are open to foreigners in both the EU2, it should be noted that the convergence in rental prices after accession was not more pronounced than that in land sales prices. This phenomenon could be taken as an indicator that renting

¹⁰ See table 4 on page 20 of the CEPS study 2010.

¹¹ In Bulgaria, where land renting is much more important than in Romania, the post-accession rental price in 2008 was only 17% higher than the pre-accession rental price in 2006.

¹² See figure 11 and table 17 on pages 43-44 of the CEPS study 2010.

agricultural land without a possibility of combining it with the acquisition of land needed for agricultural activities is only of limited attraction to foreign investors.

Socio-economic structure of the agricultural sector

The on-going transformation process of the agricultural sector in the EU2 is already showing positive results. The available data reveal that in 2008, wheat yields in Bulgaria amounted to 70% of the EU25 level and yields in Romania were around 60% of the EU25 level. The gap in labour productivity between the EU2 and the EU25 is also diminishing although large differences still persist. In 2008, the share of value added per agricultural labour input in Romania was around 45% of the EU25 level and in Bulgaria it amounted to 60% of the EU25 level. However, it should be noted that the agricultural labour input has decreased considerably in Bulgaria and Romania (more than 40% from 2000 to 2009)¹³.

Furthermore, while in 2007 the share of employment in the agricultural sector was 18% in Bulgaria and 28% in Romania, it was only 5% in the EU25. The real agricultural income over labour input increased from 2000 to 2008 by about 51% in Bulgaria and 68% in Romania.¹⁴ Nevertheless, although differences between the agricultural income in the EU2 and the EU25 decrease over time, they still remain important. In 2008, agricultural income in Bulgaria was half of the level of the EU15¹⁵ but closer to the average agricultural income in the EU7. However, agricultural income in Romania in 2008 was one fourth of that in the EU15 and, while it was comparable to that in Latvia, Lithuania and Poland, it was still below the average agricultural income in EU7.¹⁶

6. Conclusions

The development of the agricultural sector in Bulgaria and Romania, in particular, enhanced agricultural production, improved productivity, increased agricultural income and land sales prices, shows that, although still present, differences between the EU2 and the EU25 are clearly diminishing over time. Therefore, the concerns expressed during the accession negotiations, notably that the relatively lower income and land prices in the EU2 compared to the EU25 would lead to widespread acquisition of land by foreigners if temporary restrictions on foreign investments in the agricultural sector were not in place, seem now, three years after accession, to be still valid, but only to a certain extent.

The analysis of the present situation in the agricultural sector in Bulgaria and Romania shows that the restrictions do not amount to a total and strict ban on foreign investments in agricultural land. At the same time, there are institutional factors that slow down, to some degree, the progressing agricultural structural reform in the EU2. Among these factors are imperfections in the capital markets, land fragmentation and high transaction costs. It thus seems that the objectives pursued by the temporary restrictions, i.e. the softening of the impact of an open market for agricultural real estate in the EU2, could be better achieved if, during the transitional period, local farmers could also have an unimpeded access to capital. This would allow them to consolidate their land, invest in technology, improve their productivity and would, as a consequence, lead to increased agricultural income and land prices. However, in the situation of capital market imperfections, partly due to the financial crisis, fresh capital is desperately needed for further facilitating and stimulating the

¹³ Source: Eurostat (Economic Accounts for Agriculture, Agricultural Labour Input Statistics).

¹⁴ According to indicator A of the income from agricultural activity (source: Eurostat, Economic Accounts for Agriculture).

¹⁵ In Purchase Power Standard.

¹⁶ See figure 18 on page 54 of the CEPS study 2010.

development of the agricultural sector in EU2. Therefore, the opening of those markets to foreign investments through moderate measures even before expiry of the transitional periods for ensuring the competitiveness of the agricultural sector in the EU2 merits serious thought.

In the context of the above proposal, consideration might be given to introducing the following, albeit moderate, reforms:

- allowing EU foreigners, not established in EU2, to freely acquire a certain amount of the country's agricultural area;
- allowing EU foreigners, not established in EU2, to freely acquire a certain amount of farmland, up to a specified maximum amount per transaction, possibly combined in each transaction with a requirement for certain investments in technological innovation to be made;
- permitting EU foreigners not established in EU2 but renting agricultural properties there to freely acquire farm buildings and the land on which they are built.

It should be borne in mind that a considerable foreign presence in the Bulgarian and Romanian agricultural market already exists through legal entities established in the EU2 and operating with foreign capital, foreigners renting agricultural land without restrictions, and self-employed EU farmers residing in the EU2. Land acquisition by these EU investors has not led to any visible shocks to the system. Their economic activities could even be seen as helping to resolve systemic failures connected to lingering institutional problems that hinder the more efficient use of farmland and so agricultural productivity. Furthermore, great shocks from massive takeovers of land after the end of the transitional period would similarly seem unlikely since future investors are likely to be those who are, in principle, interested in the EU2 agricultural market but not to the extent that they needed to already establish themselves there during the transitional period and to acquire already now farmland at an even lower earlier price. In addition, the development of prices in the already unrestricted rental market also seems to indicate that, even after the end of the transitional period, the gradual movement of land sales prices to the EU25 degree of convergence could continue. Foreign investors are expected to combine their activities of purchasing and renting of agricultural land.

Given the deadlines established in the Accession Treaty of 2005 for the preparation of this report, the period studied¹⁷ is too short to have more extensive empirical evidence on the impact of accession and temporary restrictions on the development of the agricultural market in the EU2. Nevertheless, the Commission study has shown that the gap between the EU2 and EU25 in terms of income and land prices, which was amongst the most pronounced concerns in these two countries at the time of accession, has declined over recent years but is still well short of complete convergence. Thus, complete convergence would neither be an expected nor necessary condition for the termination of the derogations. The CEPS study 2010 has further shown that the EU2 would be well advised to put the remainder of the transitional period to good use in fostering the development in the agricultural sector and preparing for the inevitable end of the temporary restrictions. Since foreign investments appear to be conducive to the process of rationalising farmland use, enhancing productivity, increasing the level of technological innovation and improving the competitiveness of the agricultural markets, it seems appropriate to recommend to the EU2 to consider measures for a further opening of their respective agricultural sectors on a voluntary basis.

Based on the situation in the EU2 in the mid-term review of transitional measures for the acquisition of agricultural land, the Commission does not conclude that the time limits for application of temporary restrictive measures in Bulgaria and Romania should be shortened.

¹⁷ Most of the statistics available at the date of adoption of this report refer to data limited to 2008.