

## SPECIAL REPORT No 4/87

on

Community wine distillation measures accompanied by the Commission's replies

(87/C 297/02)

*(Observations pursuant to Article 206a(4) of the EEC Treaty)*

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## 1. INTRODUCTION

### ORIGINS AND SCOPE OF REPORT

1.1. The present report results from an examination of Community wine distillation measures undertaken by the Court of Auditors as part of its 1985/86 Work Programme. In addition the report takes account of a request to the Court from the European Parliament contained in a letter from its President dated 22 July 1986, to 'examine the risks of frauds or irregularities inherent in the system of management and control of Community wine distillation measures in the Member States'. The report contains observations both about the effectiveness of the measures in general, and about the adequacy and reliability of national systems of implementation and control. The Court's audit did not include the Iberian Member States.

1.2. First introduced in 1962, the Community wine regime was principally directed towards the improvement of productivity and quality, the support of producer incomes and the preservation of balance between supply and demand. The emergence of a structural surplus in the market for table (i.e. lower quality) wines in the 1970's, partly as a result of falling consumer demand, led to the evolution of a variety of ad hoc instruments designed to remove surplus table wine from the market either temporarily or permanently. The regime currently embodies two main types of instrument for this purpose; aid for long-term private storage, and aid for the distillation of table wine and of the by-products of wine-making.

1.3. Another form of Community support which has become increasingly important in recent years is aid for the use of grape must for the enrichment of wines and for the manufacture of grape juice. In addition, a series of structural measures has been in force over recent years the main objective of which has been to reduce the area under vines.

1.4. The common organisation of the market also lays down special provisions relating to 'quality wine PSR' <sup>(1)</sup> (produced in specified regions) providing in particular for certain common rules relating to production but these rules do not involve Community expenditure.

1.5. Although the various measures are inter-related the present report deals with the Community distillation measures only as indicated at paragraph 1.1 above. These measures have, in recent years, accounted for more than two thirds (1986: 461 Mio ECU) of budgetary expenditure on the wine market.

<sup>(1)</sup> The footnotes appear together at the end of the report.

1.6. The audit involved an examination of Community expenditure on distillation measures in the principal producing Member States (namely Italy, France, FR of Germany and Greece) for the marketing years 1982/83 to 1984/85. As mentioned above the audit did not extend to the Iberian Member States which joined the Community on 1 January 1986. Whereas Portugal is subject to special transitional measures, the provisions of the common organization of the market are fully applicable in Spain where only the level of prices is subject to transitional measures.

1.7. The report shows (see Chapters 7 and 8 for details) that:

(a) as regards the effectiveness of the regime:

- (i) the complex series of distillation measures in force lack coherence and succeed in removing surplus wine from the market only by creating unwanted stocks of alcohol (approximately 13,4 Mio hectolitres as at 31 August 1986) at a non-commercial cost;
- (ii) the distillation measures actually perpetuate the present structural surplus by offering attractive prices for table wine of mediocre quality which could not otherwise be disposed of;
- (iii) the recently introduced measures for the compulsory distillation of table wine are unlikely to achieve reductions in yields because of the ease with which producers may transfer their obligations and, thus, escape the financial sanctions contained in the measures;

(b) as regards the administration of the measures:

- (i) weaknesses in the regulations and in some of the control arrangements leave the system open to a serious risk of irregularities or fraud;
- (ii) the greatest risk arises from inadequate provisions governing sample-taking and analysis of wine at the point of entry to the distilleries;
- (iii) the definition of table wine is itself inadequate and this increases the danger that adulterated wine may go undetected;
- (iv) payment based solely on alcohol content is conducive to the fraudulent increase of the alcoholic strength of the wine;

- (v) there is an over-reliance on documentary controls and an inadequate level of physical checks;
- (vi) the risks inherent in the above-mentioned weaknesses are increased by the attractive level of prices available to producers under the distillation measures.
- (c) In addition to their substantial annual budgetary cost, the measures entail a future liability for the Community of 380 Mio ECU in connection with disposal of alcohol resulting from compulsory distillation.

## 2. REVIEW OF THE WINE MARKET 1981/82 — 1985/86

### Community share of world production

2.1. In the Community of ten, wine is produced in important quantities in five Member States — Italy, France,

the FR of Germany, Greece and Luxembourg. In the period under review annual production varied between 140 Mio and 172 Mio hectolitres of wine, representing between 44 % and 48 % of world production. Table wine production, as distinct from quality wine PSR, has averaged 107 Mio hectolitres annually in the Community of ten during the period under review.

### Analysis of Community production

2.2. Table 1 contains the supply balance sheets of the Community wine (including quality wine PSR) market for the years (1 September — 31 August) 1981/82 to 1986/87. The table shows a steady decline in per capita consumption and a consequent situation of oversupply. The area under vines suitable for wine-making in the Community of ten totals approximately 2 260 000 hectares and the number of producers totals approximately 2 285 000.

2.3. Table 2 which is limited to table wine shows that Italy and France together account for the bulk of production and distillation. The respective figures for Greece are relatively stable with the FR of Germany and Luxembourg accounting for marginal production per-

Table 1 — Wine supply balance sheets (EUR 10) — all wines

	Year from September to August					
	1981/82	1982/83	1983/84	1984/85	1985/86 <sup>(2)</sup>	1986/87 <sup>(3)</sup>
Usable production	140 064	171 935	168 243	147 664	142 976	156 703
Stocks at beginning of marketing year	91 436	76 444	89 290	109 766 <sup>(1)</sup>	98 996	96 102
Imports	6 333	5 082	5 209	5 002	4 405	3 750
Total availability	237 833	253 461	262 742	262 432	246 377	256 555
<i>Home uses</i>						
Direct human consumption	123 248	120 462	118 927	112 079	106 303	109 579
Industrial uses of which:	25 620	34 101	46 250	39 257	33 739	35 686
Community distillation <sup>(4)</sup>	(13 903)	(22 913)	(37 153)	(29 929)	(23 823)	(22 910)
Losses	926	963	946	668	663	886
Total home uses	149 794	155 526	166 123	152 004	140 705	146 151
Exports	11 595	8 645	7 758	11 432	9 584	8 978
Stocks end of marketing year	76 444	89 290	88 861	98 996	96 088	101 426
Stock variation	(-14 992)	(12 846)	(-429)	(-10 770)	(-2 908)	(5 324)
Total uses	237 833	253 461	262 742	262 432	246 377	256 555
Degree of self-sufficiency (%)	103	130	130	121	122	127
Consumption per capita, per annum (litres)	45,34	44,24	43,62	41,05	38,87	40,0

Source: COMMISSION, DG VI.

<sup>(1)</sup> The opening stock for 1984/85 is greater by 20,9 Mio hl. than the closing stock for 1983/84. The increased stock figure relates to Italy and results from an enquiry undertaken by the Italian authorities. The difference has not been explained further.

<sup>(2)</sup> Provisional figures as at 26.1.1987.

<sup>(3)</sup> Forecast as at 9.12.1986 (EUR 10). For Spain, production amounted to 35,5 Mio hl while total home uses were 25,4 Mio hl.

<sup>(4)</sup> Quantities include all Community measures.

Table 2 — Table wine: A. Production  
B. Quantities distilled under Community distillation (EUR 10)

(1 000 hl)

Member State	1981/82			1982/83			1983/84			1984/85			1985/86 <sup>(1)</sup>			1986/87 <sup>(2)</sup>		
	A Production	B Distillation	B as % of A	A Production	B Distillation	B as % of A	A Production	B Distillation	B as % of A	A Production	B Distillation	B as % of A	A Production	B Distillation	B as % of A	A Production	B <sup>(3)</sup> Distillation	B as % of A
FRG	141	38	27	1 094	385	35	2 790	2 490	89	1 151	50	4	16	—	—	654	—	—
Gr	5 000	1 023	20	4 237	380	9	4 659	1 300	28	4 588	1 080	24	4 376	625	14	4 125	625	15
F	37 993	3 005	8	44 620	8 326	19	37 932	8 206	22	39 572	10 990	28	39 472	8 870	22	39 629	8 960	23
It	60 881	9 116	15	61 476	10 059	16	70 132	21 999	31	59 389	15 550	26	48 868	10 586	22	61 400	10 000	16
Others	27	—	—	96	—	—	87	—	—	68	—	—	29	—	—	38	—	—
	104 042	13 182	13	111 523	19 150	17	115 600	33 995	29	104 768	27 670	26	92 761	20 081	22	105 846	19 585	18

<sup>(1)</sup> Provisional figures as at 26.1.1987.

<sup>(2)</sup> Provisional figures as at 9.12.1986.

<sup>(3)</sup> Excluding compulsory distillation of table wine and support distillation (not yet performed).

Source: Commission DG VI

Note: Distillation totals relate only to table wine. Distillation of other wines (e.g. wines produced from table grapes) not included.

centages. Interest in Community distillation measures in the FR of Germany is mainly confined to years when bumper harvests are achieved. No Community distillation occurs in Luxembourg.

#### *Main features of production in the Member States*

#### France

2.4. In France, total annual production of wine has averaged 68 Mio hectolitres in the period 1981/82 to 1985/86 inclusive. Table wines, production of which has averaged 40 Mio hectolitres, are produced mainly in the Midi region ranging from the department of Gard through Languedoc-Roussillon to the Spanish frontier.

2.5. An important region for Community wine distillation measures is Charentes where the white wines produced are mainly used for the manufacture of 'eaux-de-vie à appellation d'origine' (i.e. cognac). Community measures provide for the compulsory distillation of wine from this region in excess of 100 hectolitres per hectare of vines planted. Production below this limit which is not used for the manufacture of cognac is classified as table wine and, as such, benefits from and is subject to Community distillation measures. Within the voluntary distillation measures there is an important activity of fortifying the wine for subsequent distillation in Germany and the production of Weinbrand.

2.6. The area under vines in France amounts to 1 048 000 hectares and the number of producers to approximately 685 000, approximately 40 % of whom are members of cooperatives. The average holding is 1,5 hectares, with 36 % of the holdings under 1 hectare and only 3 % over 20 hectares. The average yield per hectare is 65 hectolitres.

#### Italy

2.7. About one fifth of the world's wine production and one third of the world's wine exports are of Italian origin reflecting the suitability of that country for the cultivation of vines. Table wine predominates, accounting for more than 80 % of total production and averaged 60 Mio hectolitres per annum during the period 1981/82 to 1985/86. The bulk of table wine is produced in the South.

2.8. There are approximately 1,2 Mio producers in Italy many of whom are members of cooperatives. There are more than 800 wine cooperatives throughout Italy, mainly in the South. They account for approximately 40 % of total production. The total area under vines is 1 026 000 hectares. The average holding is therefore around 1 hectare. The average yield per hectare is around 75 hectolitres.

2.9. In addition there is an important cultivation of table grapes in Italy, especially in Sicily and Puglia. The total area where such grapes are cultivated amounts to approximately 80 000 hectares. Because of difficulties in marketing the entire quantity produced as table grapes, important quantities are vinified. Community rules require that wine made from table grapes be compulsorily distilled.

#### Greece

2.10. Cultivation of the vine, together with the olive tree, forms an essential part of Greek agriculture. Vines are found both on the mainland and on the islands and the total area under vines extends to almost 200 000 hectares. Only 97 000 hectares, however, are planted with wine-producing varieties, the rest being cultivated as table grapes or as grapes for drying to produce currants.

2.11. There are approximately 310 000 producers of grapes suitable for wine-making in Greece. Wine production is essentially undertaken by the private wineries and recently, by the producer cooperatives. There are some 300 such wineries in the country including approximately 60 cooperatives. Average yields per hectare amount to 54 hectolitres.

#### FR of Germany

2.12. In the FR of Germany, where annual wine production varies considerably, the bulk of production (about 90 %) is classified as quality wine PSR. Yields of approximately 115 hectolitres per hectare are among the highest in Europe reflecting the intensity of cultivation with widespread irrigation of vineyards.

2.13. There are approximately 90 000 producers of grapes suitable for wine-making in the FR of Germany of which more than two-thirds cultivate less than one hectare, mostly on a part-time basis. Approximately 48 000 producers deliver their grapes to cooperatives. Total vineyard area is approximately 90 000 hectares.

2.14. Market prices for German-produced wines are usually higher than the minimum buying-in prices stipulated for Community distillation measures. Hence there is only a marginal interest in those measures except in years of exceptional harvests when prices are depressed by the large volumes. However, an important activity in the FR of Germany is the distillation of fortified wine from the Charentes region of France for the manufacture of Weinbrand. This is a commercial activity which qualifies for Community aid (see paragraph 2.5 above).

2.15. In the FR of Germany there are no defined geographical areas within which quality wines PSR are produced. All wines are capable of being classified as quality wines PSR provided they pass the controls carried out at the bottling stage by the administration of the Länder. If the wine in question fails this quality test it then becomes table wine. This particularity of the German (and Luxembourg) wine production has caused certain difficulties in the past concerning the eligibility of the wines for Community intervention measures.

### *Consumption*

2.16. Direct human consumption of wine in the Community as a whole has shown a steady decline over the past thirty five years. This decline is most marked in the main wine producing Member States where total consumption has declined by approximately 20 % over the past 15 years. Although consumption in the non-producing Member States has increased over the same period this trend has not been sufficient to counteract the declining consumption overall. It should be noted, however, that the sharp decline in quantities of table wine consumed in the main producing/consuming Member States has coincided with an increased consumption of quality wines PSR.

### *Imports and exports*

2.17. As *Table 1* shows, the Community is a net exporter of wine. Italy is the largest exporter of wine in the world (approximately 16 Mio hectolitres per annum) followed by France (approximately 9 Mio hectolitres per annum). Intra-Community trade in wine accounts for a large part of world trade. Exports to third countries have averaged about 9 Mio hectolitres in recent years and imports approximately 5 Mio hectolitres, the major part of which were of Spanish origin.

### *Processing of wines*

2.18. Given the generally diverging patterns between Community production and consumption, processing of wine is important to balance supply and demand. The major part of processing is accounted for by Community distillation measures, especially in years of abundant harvests. Thus in the years 1983/84 and 1984/85 Community distillation measures represented 80 % and 76 % of total quantities processed.

## 3. MAIN FEATURES OF THE COMMON ORGANISATION OF THE MARKET IN WINE

### *The foundations*

3.1. The foundations for the common organisation of the market in wine were contained in Council Regulation No 24 of 4 April 1962 <sup>(2)</sup> which provided for the progressive establishment of the market. In particular it provided for the following:

- (a) the institution of a vineyard register based on a general vineyard census;
- (b) compulsory annual declarations by producers of the quantities of wine and must produced, and by merchants, except retailers, of stocks held;
- (c) annual compilation by the Commission of a forward estimate of Community resources and requirements;
- (d) adoption of rules covering quality wines produced in specified regions ('quality wines PSR');
- (e) the establishment of a management committee.

3.2. The governing regulations were consolidated in 1979 with the adoption of Council Regulation (EEC) No 337/79 of 5 February 1979 <sup>(3)</sup>, together with some 23 related Council Regulations. In March 1987 the governing regulations were consolidated once again with the adoption of Council Regulation (EEC) No 822/87 <sup>(4)</sup> ('the basic regulation').

*The support measures*

3.3. The above-mentioned basic regulation now provides for a series of support measures as follows:

- aid for the private storage of table wine and grape must;
- aid for the distillation of table wine and of the by-products of winemaking;
- a licensing system for regulating trade with third countries and the establishment of export refunds and import levies;
- a price structure;
- aids for the use of grape must;
- buying-in of alcohol from compulsory distillation.

The principal elements and timing of the measures are set out in the Annex.

3.4. Table wine is defined in the regulations as wine, other than quality wine PSR, which:

- is derived from approved vine varieties;
- is produced in the Community;
- has an actual alcoholic strength by volume of not less than 8,5 % vol. and a total alcoholic strength by volume of not more than 15 % vol.;
- has a minimum total acidity content expressed as tartaric acid.

However, the upper limit for the total alcoholic strength by volume may be raised to 17 % vol. for certain wines.

*The price structure*

3.5. Each year the Council fixes a guide price for table wine. This is a notional price intended to reflect a fair

income for producers, on the basis, inter alia, of the average of prices recorded during the two preceding marketing years and the trend of prices during the current marketing year. The minimum buying-in prices for the various distillation measures (see paragraphs 3.9 and 3.10 below) are set at different percentages of this price.

3.6. Every week in respect of each of the six types of table wine, the Commission determines an average producer price from the prices quoted on each representative market and also a Community representative price equal to the weighted mean of the average prices.

3.7. In recent years guide prices for the two main types of table wine in France and Italy have generally been set by the Council above the prevailing representative prices.

*The Community distillation measures*

3.8. The basic regulation <sup>(4)</sup> provides at present for six different distillation measures, three of them being voluntary, at the choice of the producer, and three compulsory. The producer receives from the distiller a minimum price which varies according to the measure and to the type of wine or wine by-product going into distillation. The distiller in turn is entitled to a distillation aid which, in broad terms, is calculated so as to compensate him for the difference between his costs (minimum price for the wine plus distillation costs) and the price of alcohol on the market. This aid is chargeable in full to the Community budget. The market price of alcohol is, for the purposes of these calculations, taken to be 96 ECU per hectolitre (expressed as neutral alcohol at 100 % vol.). As may be seen later, only a fraction of the alcohol produced under the foregoing measures is sold on the open market.

3.9. The voluntary distillation measures comprise:

- (a) preventive distillation: where necessary, having regard to harvest forecasts in order to improve the quality of products put on the market, preventive distillation of table wines and wines suitable for yielding table wines may be decided on in each wine year from 1 September until 15 January. The minimum buying-in price payable to the producer under this measure is 65 % of the guide price. From the 1984/85 marketing year onwards quantity limits per producer have been imposed for this measure and are currently set at 13 % of production for the majority of producers.



(b) distillation supplementary to long-term storage contracts (price support guarantee): this measure is available only to wine producers who have concluded long-term storage contracts, towards the costs of which they are entitled to Community aid. The aim of the measure is to guarantee a disposal price, at the end of the contract, close to 92 % of the guide price. If, when the long-term storage contract ends, additional market support is necessary, with representative prices less than 92 % of the guide price, then the wines in question can either be stored for another period or be distilled. This measure was introduced during the 1976/77 marketing year as a temporary support measure but has now become a permanent feature of support. Price support guarantee distillation is restricted for 1986/87 to 13 % of total table wine production of the holder of the storage contract. The minimum buying-in price payable to the producer under this measure is 90 % of the guide price for white wine and 91,5 % of the guide price for red wine. This is by far the most financially attractive of the distillation measures for producers;

(c) support distillation: this measure which is essentially a remnant of the previously-applied exceptional distillation measure is introduced automatically whenever compulsory distillation is introduced. The measure may also be introduced even in years where there is no compulsory distillation. The measure is limited to five million hectolitres, although in exceptional circumstances the Council of Ministers can increase this quantity limit. Entitlement to support distillation may be restricted to producers who have taken advantage of preventive distillation. The buying-in price for this measure is 82 % of the guide price.

### 3.10. Compulsory distillation measures comprise:

(a) compulsory distillation of the by-products of wine-making: this measure is intended to prevent the overpressing<sup>(5)</sup> of grape marcs and wine lees and the marketing of inferior quality wines with a low natural alcohol content. Certain exceptions are allowed whereby the by-products, instead of being distilled, may be withdrawn and destroyed under supervision. A standard minimum alcoholic strength of the by-products is fixed for each wine year in each wine-growing zone. The price paid is based on the alcohol content of the grape marcs and wine lees;

(b) compulsory distillation of wines other than table wines: this measure applies in France to wines suitable for the manufacture of cognac and armagnac when production is in excess of 100 hectolitres per hectare of vines planted, and throughout the Community to wines made from table grapes or from other grape varieties not recognized as wine-making varieties. The minimum buying-in price payable under this measure is

50 % of the guide price for AI-type wine (one of the commonest types of white wine);

(c) compulsory distillation of table wines: this measure is decided upon by the Commission before 28 February provided:

— the availabilities recorded at the beginning of the wine year exceed normal utilization by more than four months; or

— production exceeds normal utilization by more than 9 %; or

— the weighted average of the representative prices of all types of table wine at the beginning of a wine year is below 82 % of the guide price.

3.11. The measure for compulsory distillation of table wines was first introduced for the 1984/85 marketing year. The quantity to be distilled at Community level is decided by the Commission in order to eliminate production surpluses and thus restore a normal market situation. This quantity is divided between the regions on the basis of the difference recorded between production in the region during the wine year in question and 85 % of the average production in that region for a three-year reference period (1981/82 to 1983/84 inclusive). The distillation obligation of each producer is fixed as a percentage of his production, established on a progressive scale and based on his yield per hectare but with a regional weighting which reflects the different yields in the various production regions of the Community. The quantities already delivered for preventive distillation by a producer may be deducted from the quantities to be delivered by him for compulsory distillation. The minimum buying-in price payable to the producer under this measure is 50 % of the guide price for the first 10 Mio hectolitres and 40 % of the guide price for quantities distilled above that limit.

### *Rules for administering the distillation measures*

3.12. The rules relating to distillation are contained in Council Regulation (EEC) No 2179/83<sup>(6)</sup> and are divided as follows:

— rules relating to the voluntary distillation of wine;

— rules relating to compulsory distillation;

— common provisions.

### *Voluntary distillation*

3.13. The main provisions are:

- (a) a delivery contract must be concluded between a producer and distiller for all such distillation operations. This contract must be sent to the competent intervention agency for approval, by a specified date. The contract must specify at least the quantity, the colour and the actual alcoholic strength of the wine to be distilled;
- (b) to be eligible for voluntary distillation measures producers must provide to the intervention agency proof that they have fulfilled their compulsory distillation obligations for the previous wine year;
- (c) the distiller, to be eligible for aid, must pay to the producer within a specified time, for the wine delivered to him, at least the minimum buying-in price stipulated for the distillation measure in question;
- (d) a quantity tolerance limit of plus or minus ten per cent is specified and a tolerance of 1 % by volume is permitted in the actual alcoholic strength stated in the contract;
- (e) the distiller must, for each producer from whom he has received deliveries of wine under an approved distillation contract, communicate to the competent intervention agency:
  - specific details concerning each wine delivery, indicating the number of the Community-approved transportation document used for the transport of the wine to the distiller's premises;
  - proof that the corresponding quantities of wine have been distilled;
- (f) Community aid is payable to the distiller at a rate fixed per % of alcohol by volume and per hectolitre of the distilled product on the basis of the minimum buying-in price of the wine fixed for the distillation operation in question, standard transport and processing costs, technical losses and the market price for the products of distillation. An advance payment of the aid may be paid on condition that the distiller lodges, for the benefit of the intervention agency, a security equal to 110 % of the aid;
- (g) there are no Community provisions for the buying in of alcohol resulting from voluntary distillation oper-

ations. However, those Member States where production is significantly greater than market needs have consistently bought in such alcohol at their own cost. Given the substantial quantities produced and the limited market outlets, alcohol stocks in these Member States have grown steadily and amounted to some 9,7 Mio hectolitres as at 31 August 1986.

### *Compulsory distillation*

3.14. The main provisions are:

- (a) a distillation contract is not required. Instead producers obliged to distil wine or by-products of winemaking under compulsory distillation measures are simply required to fulfill their distillation obligations. The implementing rules provide that either the producers themselves may be required to calculate their obligations or the intervention agency may make these calculations and notify the results to the producers;
- (b) certain exemptions from the obligations to distil by-products are foreseen namely for Greece and for the Italian islands except Sicily and Sardinia and for the wine-growing regions of Germany and Luxembourg. In such cases the by-products are to be withdrawn under supervision;
- (c) the minimum buying-in price laid down for the operation in question must be paid by the distiller to the producer within specified time limits;
- (d) the aid payable to the distiller is fixed on the basis of a calculation taking account of the elements mentioned at paragraph 3.13 (f) above;
- (e) in order to qualify for the aid the distiller must submit an application to the competent intervention agency within a specified time-limit together with proof of distillation;
- (f) unlike the rules governing voluntary distillation, those for compulsory distillation entitle distillers to sell their product to the intervention agencies provided it is at least 92 % pure alcohol. The buying-in price is fixed at 96 ECU per hectolitre, i.e. the 'market price' for neutral alcohol used in the calculations of distillation aid (see paragraph 3.8). In practice, very little can be sold at that price, and since Community rules forbid disposal at prices or in conditions which would upset the normal alcohol market, stocks have rapidly built up to a level of some 3,7 Mio hectolitres (in addition to the 9,7 Mio

hectolitres held by certain Member States (see paragraph 3.13.(g)). As a result, special measures have been introduced in the hope of disposing of these stocks outside the normal alcohol market;

(g) the buying-in operations described in the foregoing sub-paragraph, are financed in the first instance by the Member States but the division of financial responsibility between Member States and the Community varies with the distillation measure involved. In the case of the measures referred to in paragraph 3.10.(a) and 3.10.(b) the costs of storage are a final charge to the Member States and the only costs chargeable to Community funds are any losses due to special sales outside the normal alcohol market e.g. to the fuel sector. On the other hand, alcohol resulting from the compulsory distillation of table wine (paragraph 3.10.(c)) is treated as public stocks, and is, therefore, for the full charge of the Community, including storage costs and losses on sale. The budgetary impact of compulsory distillation is treated in more detail in Chapter 7 of this report.

- (a) the distillation operations may be carried out only during specified periods;
- (b) the quantity and characteristics of the products delivered for distillation under Community measures must be checked on entering the distilleries. Such checks may be made by sampling;
- (c) the competent authorities in the Member States are required to approve the distilleries for Community distillation measures and to draw up a list of such approved distilleries and forward same to the Commission for publication. A total of 578 distilleries have been approved to date of which 240 are in France, 228 in Italy, 84 in the FR of Germany, 25 in Greece and 1 in the United Kingdom.

#### 4. BUDGETARY EXPENDITURE

4.1. Community expenditure on the wine market for the years 1980-1985 inclusive is set out in Table 3.

4.2. During this period expenditure on distillation of wine ranged between 65 % and 77 % of total expenditure in the wine market. This expenditure reached a peak in 1984 reflecting the impact of two particularly abundant harvests in 1982/83 and 1983/84.

#### Common provisions

3.15. The main ones are:

Table 3 — Community expenditure on the wine market

(Mio ECU)								
Budget line	Description	1980	1981	1982	1983	1984	1985	1986 <sup>(1)</sup>
160	Refunds on products of the wine-growing sector	26,4	25,8	31,9	20,2	18,6	18,8	11,2
1610	Intervention storage of wine and grape must	76,3	90,7	108,4	142,5	135,6	87,6	70,5
1611	Distillation of wine	194,4	314,9	390,5	391,4	852,4	599,0	406,1
1612	Compulsory distillation of the by-products of winemaking	0,1	—	9,0	63,1	88,6	65,3	55,8
1613	Aid for use of must	1,7	27,9	30,8	42,0	126,6	148,2	82,4
1614	Buying-in of alcohol from compulsory distillation	—	—	—	—	—	1,5	3,8
1619	Other interventions	0,6	0,1	—	—	0,8	0,9	0,9
	Totals	299,5	459,4	570,6	659,2	1 222,6	921,3	630,7
	Distillation expenditure as percentage of total wine sector expenditure (1611 + 1612)	65	68	70	69	77	72	73
	Percentage of EAGGF-Guarantee	2,7	4,2	4,6	4,2	6,7	4,7	2,9

<sup>(1)</sup> Including Spain: budget line 160 - 1,4 Mio ECU  
budget line 1613 - 0,1 Mio ECU.

Table 4 — Analysis of distillation expenditure by Member State

Member State	(Mio ECU)														
	1980		1981		1982		1983		1984		1985		1986		
	Measure	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%
FR of Germany:															
– Distillation of wine	—	—	0,3	0,1	3,9	1,0	23,4	6,0	113,7	13,3	7,3	1,2	6,0	1,5	
– Distillation of by-products	—	—	—	—	—	—	—	—	—	—	—	—	—	—	
Greece:															
– Distillation of wine	0,1	—	1,0	0,3	14,8	3,8	26,3	6,7	24,9	2,9	18,9	3,2	7,1	1,7	
– Distillation of by-products	—	—	—	—	—	—	0,2	0,3	0,6	0,7	0,4	0,6	0,2	0,3	
France:															
– Distillation of wine	100,7	51,8	126,9	40,3	78,9	20,2	150,3	38,4	219,2	25,7	196,1	32,7	180,3	44,4	
– Distillation of by-products	—	—	—	—	—	—	42,9	68,0	54,0	60,9	37,3	57,1	32,5	58,2	
Italy:															
– Distillation of wine	93,7	48,2	186,7	59,3	292,9	75,0	191,4	48,9	494,6	58,1	376,7	62,9	212,7	52,4	
– Distillation of by-products	—	—	—	—	9,0	100,0	20,0	31,7	34,0	38,4	27,6	42,3	23,1	41,5	
Community totals:															
– Distillation of wine	194,5	100,0	314,9	100,0	390,5	100,0	391,4	100,0	852,4	100,0	599,0	100,0	406,1	100,0	
– Distillation of by-products	—	—	—	—	9,0	100,0	63,1	100,0	88,6	100,0	65,3	100,0	55,8	100,0	

4.3. During 1985 expenditure was incurred for the first time on the buying-in of alcohol from compulsory distillation. While the sums involved have amounted to only 1,5 Mio ECU in 1985 and to 3,8 Mio ECU in 1986 this reflects the negligible quantity disposed of to date, and the fact that Member States are not reimbursed by the Community prior to disposal. Much more significant costs are likely to arise in future years because of the substantial losses which must be foreseen when the alcohol is disposed of (see paragraph 7.6).

4.4. Table 4 provides an analysis of distillation expenditure by Member State. The quantities distilled are set out in Table 5 for the wine-growing years 1982/83 to 1985/86 inclusive. The latter table shows that price support guarantee distillation for the holders of long-term storage contracts is of major importance in all Member States.

## 5. OPERATION OF THE SYSTEM IN THE MEMBER STATES — AUDIT FINDINGS

### General

5.1. The basic regulation<sup>(4)</sup> provides for harvest, production and stock declarations which serve as a means of controlling both the producers' entitlement to the

voluntary distillation measures and the fulfilment of their obligations under the compulsory distillation measures.

5.2. The administrative organisation of Community distillation measures in the Member States involves the delegation to specialised services of the responsibilities for carrying out key controls in almost all instances. As a result the control activities are widely dispersed and vary significantly from one Member State to another. Detailed audit findings are outlined below for each of the key control areas namely:

- (a) controls over harvest, production and stock declarations;
- (b) approval of distillation contracts for voluntary distillation;
- (c) controls over the transportation of wine destined for distillation;
- (d) use of an indicator in wine destined for distillation;
- (e) controls over products entering the distilleries;
- (f) controls over distillation;
- (g) controls over the fortification of wine for distillation;
- (h) controls over compulsory distillation measures.

5.3. The degree of reliance placed by the authorities in the key control areas outlined above, varies considerably from one Member State to another.

Table 5 — Distillation of wines and of the by-products of wine-making under Community distillation measures — EUR 10<sup>(1)</sup>

(1 000 hl)

Wine growing year	Member State	Total	Compulsory distillation measures	Voluntary distillation measures			
				Preventive	Price support guarantee	Support	Total
1981/82	FR of Germany	38	—	—	23	15	38
	France	3 005	1	81	2 607	316	3 004
	Italy	9 837	721	36	4 138	4 942	9 116
	Greece	1 023	—	2	156	865	1 023
	Total EEC	13 903	722	119	6 924	6 138	13 181
1982/83	FR of Germany	385	—	374	—	11	385
	France	11 903	4 146	2 137	3 057	2 563	7 757
	Italy	10 245	185	4 383	3 555	2 122	10 060
	Greece	380	3	70	160	147	377
	Total EEC	22 913	4 334	6 964	6 772	4 843	18 579
1983/84	FR of Germany	2 490	258	2 203	29	—	2 232
	France	10 810	4 253	2 053	4 504	—	6 557
	Italy	22 503	510	17 369	4 624	—	21 993
	Greece	1 350	21	1 100	229	—	1 329
	Total EEC	37 153	5 042	22 725	9 386	—	32 111
1984/85	FR of Germany	50	2	20	28	—	48
	France	11 650	4 508	1 706	4 398	1 038	7 142
	Italy	17 149	5 051	3 893	7 002	1 203	12 098
	Greece	1 080	235	378	374	93	845
	Total EEC	29 929	9 796 <sup>(2)</sup>	5 997	11 802	2 334	20 133

Source: CEE, DG VI, Wine section, based on communications from the Member States.

Notes: <sup>(1)</sup> Data not yet available for 1985/86 wine growing year.

<sup>(2)</sup> Analysis of compulsory distillation quantities for 1984/85 (only year such data is available) are as follows:  
 Compulsory distillation of wine by-products: FRG — France 2 020 Italy — Greece 61.  
 Compulsory distillation of table grapes or grapes of double classification: : FRG — France 342 Italy 1 599 Greece 24.  
 Compulsory distillation of table wine: : FRG 2 France 2 146 Italy 3 452 Greece 150.

5.4. In the audit observations which follow the assessment by the Court of the adequacy, or otherwise, of the nature and extent of verification work carried out is based both on tests of transactions carried out during the enquiry, and on an analysis of statistics furnished by the national authorities as well as on discussions with the authorities in the Member States and with the services of the Commission.

#### Controls over harvest, production and stock declarations

5.5. The number of on-the-spot checks carried out by the Member States on these declarations was extremely limited mainly due to shortages of staff in the control agencies and to the number of tasks entrusted to them. In view of the importance of these declarations as a means of exercising effective control over the wine market the present level of on-the-spot checks by the Member States gives grounds for serious concern.

#### France

5.6. There is a heavy reliance on documentary controls by means of the stock records maintained by the control authorities themselves. But their effectiveness is diminished by the very limited numbers of physical checks to verify the correctness of the producers' declarations on which the stock records are based.

#### Italy

5.7. Verification work carried out on producers' declarations was inadequate at least for the important wine-producing regions visited during the audit (i.e. Puglia and Sicily). Physical checks are mainly made at the end of each campaign and are more orientated towards establishing conformity of stock records with the declarations than towards the reliability of the declarations

themselves. The available statistics also indicate that the taking and analysis of samples by the control service is quite inadequate.

5.8. Officials of the control service at local level admitted that it is difficult to ensure that all producers make complete declarations. Control difficulties are heightened by the absence of a vineyard register or of reliable statistics at local level pertaining to individual holdings.

#### Greece

5.9. Producers were exempted from making harvest declarations until the 1986/87 wine-growing year. Instead wine makers were obliged to obtain a declaration from the producer who sold them his grapes, stating the yield per hectare for the grapes concerned. The Court found that checks performed on the declarations were very limited and were confined to establishing the correctness of the calculations without any control on the reliability of the data declared. The reliability of producers' declarations will become a matter of particular importance in Greece when the present period of exemption expires, especially in the context of the application of measures for the compulsory distillation of table wine.

5.10. The Court was given to understand that numerous control visits are made each year to wineries and distilleries as well as to retailers and wholesalers of wine. However, no precise statistics on the number of such visits made were available: Nor were details available to indicate the nature, duration and results of the visits. The Court also noted that the records of the distilleries and wineries visited contained no evidence of controls effected.

#### FR of Germany

5.11. The arrangements for checking producers declarations vary from one Land to another. Inaccuracies in the producer declarations, particularly in the yields declared, were only brought to light when the distillation obligations of producers were being calculated by the intervention agency. The Court therefore infers that the arrangements for checking the declarations are inadequate; otherwise the inaccuracies in the declarations would have come to light at an earlier date and the problems of ensuring that producers respected their obligations would have been easier to resolve.

#### *Approval of distillation contracts for voluntary distillation measures*

5.12. The Court found that the procedures were generally satisfactory in this area except for the following:

- (a) in Italy the voluntary distillation contracts are approved on the basis of a solemn declaration by the producer that he has respected his compulsory distillation obligations for the previous campaign, rather than on the basis of an independent certificate to that effect, as stipulated by Community

regulations. This situation is due to the lateness of verification work carried out by the control service;

- (b) in the FR of Germany the certification procedure is not applied contrary to Community regulations.

#### *Controls over the transport of wine destined for distillation*

5.13. The purpose of the Community transport documents is to provide a standard document which can facilitate the control over all physical movements of wine. Properly used, they constitute a valuable additional measure of surveillance over movements of table wine destined for distillation. However, the Court found that the procedures for issuing and controlling these documents and for making physical checks en route were inadequate in many respects. In particular, the following observations arise:

#### France

5.14. Under the French system considerable reliance is placed on establishing documentary control over the production and disposal of wine by means of a stock control system maintained by the authorities. This system is based on the transport documents. Notwithstanding their importance, however, the Court found that a large number of transport documents are issued by:

- (a) either 'auxiliary offices';

or

- (b) the distilleries themselves, especially in the case of the most important distilleries, which are authorised both to issue their own transport documents and to register on these documents the arrival time of the products at the distillery by means of a franking-machine assigned to them by the control service i.e. the distilleries have complete control over all phases of the administrative procedures governing the transport documentation.

5.15. In both cases listed above the proper functioning of the system depends on an adequate level of surveillance by the responsible control services. However, the limited staff numbers available in the service and the wide range of duties imposed on them renders the necessary surveillance difficult, if not impossible.

5.16. The Court also noted that the service responsible for the control of transport documents relies almost exclusively on the system of 'bond notes' and that physical checks during the transportation phase are rare. While such a system ensures that all transport documents issued are accounted for it cannot compensate for an inadequate level of physical checks.

**Italy**

5.17. The audit revealed the controls over the issue of and accounting for transport documents to be inadequate in certain respects. In particular:

- (a) the documents examined contained no evidence of the actual time or date of arrival of the produce at the distilleries, although the Community document provided for this as an optional measure;
- (b) changes in the transportation arrangements were sometimes made without explanation and without approval by a competent authority (e.g. police);
- (c) the documents made available to the control services arrive too late to allow for the carrying out of physical checks during the transport phase. The period allowed for the communication of a copy to the control office is seven working days in the case of wine and one working day in the case of by-products;
- (d) under the present system there is no control to ensure that all documents issued are properly accounted for.

5.18. Discussions with the control services during the audit indicated that interventions by those bodies to effect controls en route of the transport of wine and by-products of winemaking, are superficial in most instances. They rarely, if ever, take samples or even verify the contents of containers against the supporting transportation documentation except in cases where fraud is strongly suspected (e.g. the unauthorized transport of wine or of adulterated wine).

**Greece**

5.19. The Court found that the procedure for issuing transport documents is not standardised. In addition there is no systematic check by officials of the control service that all documents issued are accounted for. The Court also noted that no physical checks are made en route when wine is transported.

**FR of Germany**

5.20. During an examination of transport documents, the Court observed that, in a number of instances, the estimated time of the transport operation was unduly long (up to 3 days on one occasion). It is difficult to justify such a long delivery time, and it is doubtful if, in such circumstances, the responsible control body can be aware precisely when the physical operation is scheduled to take place in order to carry out a physical check en route, if desired.

*Use of an indicator in wine destined for distillation*

5.21. This is an optional provision of the governing regulation. The measure is not used in France or in the FR of Germany where the responsible control services rely on other measures to prevent products from being diverted to other uses.

**Italy**

5.22. Producers are obliged to add stipulated quantities of lithium chloride to the products destined for distillation, before they are transported to the distilleries. However, since the addition of the indicator takes place without official surveillance the effectiveness of the measure is diminished from a control point of view. In addition, the obligation imposed on the distilleries to test the wine received for the addition of lithium chloride does nothing to detect wine which has been diverted on to the market. The addition of an indicator as presently applied weakens rather than reinforces control over the transportation of wine destined for distillation in that there is an over-reliance on the effectiveness of the system with a corresponding reduction in the number of physical controls en route as indicated at paragraph 5.18 above.

*Controls over products entering the distilleries*

5.23. Controls (both physical and documentary) over the products entering the distilleries were frequently inadequate and offered considerable potential for carrying out unauthorised activities.

**France**

5.24. It is difficult to ensure adequate control over the characteristics of wine or of wine by-products entering the distilleries, as required by Article 22 of Council Regulation (EEC) No 2179/83<sup>(6)</sup>, given that there is only a part-time presence in the distilleries of the official body in charge of supervising distillation activities. Although the abovementioned regulation provides that such checks may be carried out by sampling, since officials of the control body are only present on average one day per month in each distillery, adequate checks cannot be carried out on the basis of truly representative samples. In addition, a certain regularity was observed in the series of visits made thus rendering the controls less effective.

## Italy

5.25. While most large distilleries are under quasi permanent surveillance by the control service, sometimes with the collaboration of Guardia di Finanza officials, controls over small distilleries are often sparse and limited to certain days per week. The potential for carrying out unauthorised activities is frequently greater in small distilleries given that internal control is often unsatisfactory with all key functions in the hands of one, or a few persons. In such circumstances, the presence of officials from the control service on designated days in small distilleries may not be adequate to safeguard Community funds.

5.26. In one medium-sized distillery, which was controlled by the part-time presence of an official three times per week, the Court concluded that controls were inadequate in that:

- (a) a delivery of by-products took place during the afternoon of the visit when the official had already left, despite a declaration by officials of the control service that deliveries to the distillery could take place only when an official was present;
- (b) the weighbridge tickets for individual deliveries were not retained;
- (c) while the Court was told that the alcoholic strength of deliveries is systematically determined by means of laboratory analysis at the point of entry, the employees of the distillery were unable to furnish copies of such analysis bulletins;
- (d) numerous sizeable differences were noted in the alcoholic strengths of deliveries as shown on the transportation documents and those recorded as paid for in the company's records (differences were noted in 79 % of the transactions examined. Both positive and negative differences were noted ranging, in general, between 15 % and 65 %. In one case examined a difference of 125 % was noted);
- (e) grave difficulties were encountered by the audit team in attempting to follow the audit trail for transactions selected for testing. The difficulties arose in attempting to reconcile the quantities of wine distilled and the quantities of alcohol produced as stated in the certificates issued by the control authorities with the quantities of wine and the stated alcoholic strength of same as recorded in the approved registers. Of three such reconciliations attempted by the audit team one was achieved after much difficulty but the two others were not possible in the time available, even with the full-time assistance of the responsible officers of the distillery.

## Greece

5.27. While controls were generally good, in view of the permanent presence in the distilleries of control service officials and also of the addition of an indicator under supervision to the products delivered, the Court has the following observations to make concerning the taking and testing of samples:

- (a) officials responsible for controlling the producers rarely take samples although their presence is required to supervise the addition of an indicator to the wine;
- (b) officials responsible for controlling the distilleries take samples not from individual deliveries but from the storage tanks when the total agreed quantity of a contract has been delivered. The taking of samples in this manner would appear to make it difficult to verify the characteristics of the wine against the transportation documents as required by Article 22 of Council Regulation (EEC) No 2179/83 (6).

## FR of Germany

5.28. Controls were generally satisfactory. However, in the case of French fortified wine destined for distillation and for the subsequent production of Weinbrand, the Court encountered difficulties in attempting to reconcile the quantities of wine certified as delivered for fortification in France with the quantities subsequently delivered to the German distillery. The Court noted that under present arrangements the French authorities do not provide a written statement showing the precise make-up of individual deliveries of fortified wine to distilleries in Germany. Such a statement would greatly facilitate the global reconciliation by officials of the intervention agency of the quantities of wine fortified in France with the quantities of such wine delivered to various distilleries in the FR of Germany. Such a reconciliation is attempted at present but proves extremely difficult to complete.

*Controls over distillation*

5.29. Here again the limited presence of the control authorities in certain Member States leads to shortcomings in the controls over distillation. In addition, certain difficulties were encountered in reconciling alcohol produced to wine distilled.

## France

5.30. The alcohol produced is recorded by alcohol meters only whereas in other Member States a second method (i.e. weighing) is considered necessary as a double check.

5.31. Moreover, the limited time available to the control officials and the requirement to reconcile input and output since the last visit to the distillery means that even these on-the-spot controls must necessarily be summary and almost exclusively confined to documentary checks. Yet, even documentary checks



are difficult and need time for their completion, in particular, the reconciliation of individual deliveries of wine or by-products of wine making with the quantities of alcohol produced.

5.32. While the Court accepts that the distillation process is a continuous one, which in itself renders the identification of individual transactions at any stage in the process somewhat more complex, it is essential that the link between individual contracts, or in the case of obligatory distillation, quantities delivered, and the quantities of alcohol produced be more easily identifiable. The problem encountered in this respect stems from the fact that the service responsible for controlling the producers is primarily interested in establishing accounting control over raw materials entering the distillery whereas the documentation required for the intervention agency is primarily orientated towards accounting for the alcohol actually produced and delivered to the latter service. The link between the deliveries of wine or of the by-products of wine making to the distillery and the alcohol produced is somewhat artificial and is not based on accounting records which allows the physical movement of the raw materials to be traced through the distillation process to the finished product.

#### Italy

5.33. See audit remarks at points 5.25 and 5.26 above which are also valid for controls over distillation.

#### Greece

5.34. The Court observed that the responsible control service:

- (a) has not adjusted its procedures and instructions to comply with Community regulations;
- (b) makes practically no use of the documents prescribed by Community regulations.

5.35. In particular, the following observations arise:

- (a) the control service issues its own transport document for each operation involving the movement of wine or the by-products of winemaking and relies almost exclusively on this to the detriment of the Community document. As a result the latter document contains no evidence to indicate that the data contained therein have been verified and found to be in accordance with the facts;
- (b) the control service prepares a protocol document which establishes the relationship between individual deliveries and the total quantities recorded in the approved registers and distilled. Notwithstanding its importance, however, the protocol document is not in standard format, with the result that only part of the details shown on the transportation documents are recorded on certain protocol documents and this gives rise to difficulties in following the audit trail;
- (c) since the exact location of the wine or by-products (e.g. tank number) is not recorded in the registers maintained by the control service, the task of relating alcohol produced to wine

used is rendered more complex than is necessary. There is a risk, therefore, that the control body may have to rely unduly on the declarations of the distillers rather than on their own independent records.

#### *Controls over the fortification of wine for distillation*

5.36. Wine which is to undergo one of the Community distillation operations may be fortified for distillation. The process involves the addition of a distillate to the wine and the product obtained has an alcoholic strength of between 18° and 24° vol. This activity is almost exclusively confined to the Charentes region of France.

#### France

5.37. When wine is to be fortified for distillation under a voluntary distillation measure, a delivery contract, approved by the intervention agency is required. The Court noted that the declaration announcing the intention of an approved processor to fortify wine for distillation makes no reference to the approved contracts covering the operation. In fact, there is no evidence that the control service verifies if the fortification operations are covered by approved contracts. Neither is it indicated in the documents presented to the intervention agency if and when the fortification process took place (see also paragraph 5.32).

#### *Controls over compulsory distillation measures*

5.38. In this area the audit revealed a series of inadequacies in the control procedures in all the Member States as detailed below. In particular, because of structural weaknesses, the control services in certain Member States are not in a position to ensure the respect of these measures.

#### France

5.39. Documentary controls are generally good for all compulsory distillation measures. Once again, however, these controls are weakened by the limited number of physical checks on harvest, production and stock declarations as noted above.

5.40. With regard to the distillation of the by-products of winemaking the Court found that, in the Charentes region, producers who deliver wine for the production of cognac are not

required by the control service to deliver for distillation the small lees which may be contained in the wine. No such exoneration is provided by Community regulations. Also, as certain cognac manufacturers do not allow the small lees to be included in the wine delivered to them, a global exoneration, as granted by the authorities, is inappropriate.

5.41. For the compulsory distillation of table wine in 1984/85 producer groups were allowed to calculate their own distillation obligations (see paragraph 5.4(a) above). The audit revealed an insufficient degree of surveillance by the authorities over these calculations.

### Italy

5.42. Because of structural weaknesses, the control service was not in a position to ensure respect of compulsory distillation measures by producers. The Court concluded that the service does not systematically verify that all producers have satisfied their obligations but waits instead for the request from the producer for a certificate before undertaking the verification work. Officials in some of the provinces and regions visited indicated that the available resources relative to the number of certificates to be issued precluded on-the-spot visits. As a result such documentary verification as takes place cannot achieve more than to ensure that producers have satisfied compulsory distillation obligations only for the production that they have declared. This approach is inadequate to verify the obligations of producers who have not declared or who have underdeclared their production.

5.43. Wineries and distilleries are obliged to maintain approved registers which are subject to periodic inspection by control officials. In the wineries and distilleries visited during the audit the Court found that these registers did not bear evidence of controls effected by the service although the employees of the establishments visited indicated that periodic control visits were made. In one winery visited the audit team found that the entries in the approved register did not correspond to the production and stock declarations made by the winery. Yet the Court was told that the winery had been subjected to a series of control visits by the responsible service and had been issued a certificate by that service testifying compliance with obligatory distillation measures. No satisfactory explanations were given, however, as to the differences noted.

5.44. The Court is particularly concerned about the service's ability to verify respect of the obligation to distil all wine produced from table grapes. In Puglia and in Sicily there is an important production of table grapes which is, in general, considerably in excess of market needs. At the same time the means available to the control service, to ensure that all such wine is distilled, are clearly inadequate and allow only the documentary verification mentioned above. Producers of table grapes are not required to declare their total production and no transport document is required for such grapes transported within a radius of 40 kilometres from where they were grown. The scope for vinification of table grapes and the subsequent unauthorised disposal of the wine on the market or its presentation under more lucrative distillation measures appear to be significant within the present control system.

5.45. With regard to the compulsory distillation of table wine the Italian authorities utilised the provision whereby the producers may be required, in the first instance to calculate their obligations and to submit their calculations to the authorities for verification. Examination of a limited number of these calculations highlighted several cases where the calculations made by the producers were found by the control service to be incorrect. While this is understandable in implementing for the first time such a complicated regulation the number of errors made by producers indicates once again the necessity for the control service to verify the calculation of obligations in good time before the approval of voluntary distillation contracts for the following campaign (see paragraph 5.12(a) above).

### Greece

5.46. In mainland Greece it is foreseen that the by-products of wine-making be withdrawn subject to official supervision. The Court noted a lack of evidence of official supervision of the withdrawal and destruction operations. Likewise there was no evidence that the alcoholic content of the by-products was measured to ensure against overpressing (<sup>3</sup>). On the contrary, in the documentation examined the alcoholic strength was preprinted in the standard protocol form used indicating that a predetermined alcoholic strength is used instead of the actual alcoholic content of the by-products.

5.47. The implementing regulations for the compulsory distillation of table wine contain special provisions for the wine years 1984/85, 1985/86 and 1986/87 in Greece in view of 'administrative difficulties encountered'. The Greek authorities were given a large degree of autonomy in implementing the measure provided that the procedures adopted resulted in the compulsory distillation of between 120 000 and 150 000 hectolitres and were equitable. Approximately 151 000 hectolitres of wine were distilled under the measure in 1984/85. The lack of urgency in taking the necessary steps to overcome the present difficulties (namely difficulties in determining yields per hectare with accuracy) and the danger of these special provisions becoming a permanent feature of the system are matters requiring attention.

### FR of Germany

5.48. In the FR of Germany producers are not obliged to distil the by-products; instead the by-products are required to be withdrawn under official supervision.

5.49. In the case of a wine cooperative visited by the Court control over the withdrawal of by-products was unsatisfactory in that:

- (a) after the grapes had been pressed the resulting grape marcs were stored in an open silo. There was no official supervision of these activities, even on a test basis, nor was there any evidence that the alcoholic strength of the marcs was measured at this stage;
- (b) there was no evidence of physical control over the stored marcs as access to the area was not restricted. Indeed,

according to explanations furnished by the cooperative officials, the members of the cooperative are free to withdraw the marcs from the silo if, and when, they so wish.

5.50. As regards voluntary distillation measures, none of the files examined contained a certificate by an official body that the producer had fulfilled his obligations regarding compulsory distillation for the previous wine growing year although Article 4(1) of Council Regulation (EEC) No 2179/83 <sup>(6)</sup> requires producers to furnish such a certificate.

5.51. During the wine growing year 1984/85, the Community measures for the compulsory distillation of table wine were implemented for the first time. However, the application of this measure in the FR of Germany has been largely unsuccessful due to the refusal of an important number of producers to respect their obligations. The problems encountered in implementing the measures were compounded by the fact that inaccuracies contained in the producers' declarations (upon which they themselves had estimated their obligations) were only detected at an advanced stage in the campaign, when most producers had already disposed of their entire production. Likewise, the imposition of heavy penalties (i.e. the compulsory distillation of 20 % of their production), as provided by Community regulations, met with similar refusals by a relatively large number of producers.

5.52. The exclusion of these producers, from voluntary distillation measures in future years, is not an effective sanction against them, because of their marginal interest in such measures. The difficulties encountered in applying the measure give a further indication of the importance of implementing the certification procedure as explained at paragraph 5.50 above.

#### *Controls over alcohol produced*

5.53. Since there is no common organisation of the market in alcohol, there exist no overall Community provisions with regard to control of the alcohol produced from Community distillation measures. Control of the alcohol is governed by national excise provisions. The Court's audit did not extend to an examination of these controls.

## 6. MANAGEMENT BY THE COMMISSION

6.1. In the wine market the specific responsibilities of the Commission are:

(a) to ensure that complete and accurate management information is received from the Member States in due time according to the governing regulations;

(b) to open the various distillation measures, taking due account of the situation in the market.

6.2. The Commission also has general responsibility:

(a) to oversee the correct implementation of the measures in the Member States;

(b) to monitor the adequacy of Community regulations and propose amendments as necessary.

6.3. The above-mentioned responsibilities imply a need to be aware of developments both in the Member States and in the world markets. However, the Court has observed for the wine market, as it has remarked for other markets in the past, that the Commission services lack sufficiently detailed knowledge of the situation prevailing in the Member States. Thus, at the time of the audit no detailed notes on the control systems in force in the Member States were available within the Commission.

6.4. The Commission services rely for their knowledge of developments almost exclusively on information provided by the national representatives on the management committee. Officials of the market division have little or no possibility to go on-the-spot to learn first-hand of problems and weaknesses, so as to be in a position to take corrective action. In general, on-the-spot visits are only made by the financial services of the Commission, particularly in the context of clearance of the accounts of previous years. Yet, those officials seldom, if ever, have the opportunity to visit the regions and the beneficiaries of Community aid and, in practice, confine their investigations to documentary checks. The Court considers that this approach is inadequate, given the central management role which the Commission services are expected to play and directly leads to some of the weaknesses highlighted below.

6.5. As regards the duties outlined in paragraphs 6.1 — 6.2 above the Court's audit revealed the following:

(a) the reception and exploitation of management information:

(i) the system of reporting market prices (the basis for establishing the representative price) is not functioning efficiently in that numerous important market centres systematically fail to register prices;

- (ii) in the past, problems have been encountered in the establishment of harvest estimates the reliability of which is essential to ensure that appropriate measures are taken in good time to regulate the market. Yet, it was only with Commission Regulation (EEC) No 2396/84 (?) that the Commission took powers to exploit new sources of information;
- (iii) serious problems have also been encountered in establishing final supply balance sheets for wine, especially as regards accurate opening and closing stocks. Such problems relating to the 1984/85 marketing year have yet to be resolved. For the marketing year in question the opening stocks declared by Italy (40,590 Mio hl) were more than double those declared as the closing stocks for the previous marketing year (19,685 Mio hl). The final balance sheet for the marketing year in question was presented by the Commission to the Council on 22 January 1987 with a note indicating the difference between the opening and closing stocks. No satisfactory explanation has been offered as to the source of the increased stocks of approximately 21 Mio hl — over 30 % of the average annual production of table wine in Italy. Nor has a revised supply balance sheet been prepared for the 1983/84 marketing year. Had such a balance sheet been prepared it would at least give an indication as to the source of the additional stocks (e.g. under-declared production, overdeclared consumption, etc.). The scale of the difference, however, casts serious doubts on the reliability of the statistics furnished to the Commission and the usefulness of those statistics for market management. The Court considers that it is essential for the Commission to carry out, without delay, a detailed investigation of these considerable stock differences;
- (iv) the Court observed that a significant amount of important periodic management information (relating, in particular, to the quantities of wine contracted for under the various voluntary distillation measures and also to the quantities delivered for compulsory distillation) is frequently received by the Commission after delays of up to one year; yet the Commission seems powerless to rectify this situation although the governing regulations set down precise deadlines for the communication of data;
- (b) opening of the various distillation measures:
- given the unreliability of management information a decision to open a particular distillation measure has become quasi-automatic rather than being based on a thorough knowledge of the situation in the market;
- (c) overseeing the correct implementation of the measures by the Member States:
- (i) the audit findings outlined in Chapter 5 of this report show that the Member States have not correctly implemented the distillation measures in all instances. The lack of awareness on the part of the Commission services of incorrect interpretations of the regulations by the Member States has allowed such practices to be continued for a number of years;
- (ii) with regard to the control in respect of compulsory distillation measures it was found that there was insufficient surveillance on the part of the Commission. Thus, it was observed that:
- with regard to the distillation of the by-products of winemaking, very little attention appeared to be paid to determining on a systematic basis whether the returns of the Member States were consistent with the respect of the obligations, by verifying for each marketing year the reasonableness of the quantities of by-products distilled in relation to the total harvest;
  - with regard to the distillation of wine produced from table grapes, Commission services have not established, by means of a statement of sources and uses of table grapes, whether the quantities of such wine sent for distillation are reasonable. Yet such a statement of sources and uses is possible and its preparation on an annual basis is especially necessary considering the widespread doubts concerning the fulfilment by all producers of their obligations in this regard;
- (d) monitoring of regulations:
- the Court's audit has brought to light numerous defects in the present regulations, of which the following are particularly important:
- (i) the regulations laying down rules for the establishment of harvest, production and stock declarations are defective in failing to provide for a minimum level of on-the-spot checks of those declarations;

- (ii) Community transport documents would be more effective as a means of controlling the movement of wine destined for distillation if the regulations provided that, when wine enters the distilleries, the precise time and date should be recorded thereon;
- (iii) Article 22 of Council Regulation (EEC) No 2179/83 (6) provides that the characteristics of the products delivered for distillation and in particular quantity, colour and alcoholic strength, shall be checked when the products enter the distillery. The Article allows such checks to be made by sampling, but makes no provisions for any of the following:
- appropriate analyses to detect wine the alcoholic strength of which has been increased by unapproved oenological practices;
  - appropriate analyses to detect adulterated wine;
  - a mandatory minimum level of sampling;
- (iv) the present definition of table wine (see paragraph 3.4) is insufficient in that it only stipulates two quality characteristics (alcoholic strength and total acidity) in contrast to quality wine PSR for which a list of twenty one factors is stipulated to enable such wines to be distinguished. This lack of precision in the definition of table wine constitutes both a difficulty in ensuring adequate testing of wine at entry to the distillery and a danger that adulterated wine presented for Community distillation measures may not be detected;
- (v) there is an urgent need to tighten controls over wine produced from table grapes;
- (vi) the type of proof of payment by the distilleries within the specified time periods allowed of the minimum buying-in prices to the producers varies significantly and, in certain cases examined, was inadequate particularly regarding the payment dates. The regulations lack clarity on this point;
- (vii) the lack of progress in prohibiting the cultivation of vine varieties which were recognised as being unsuitable for wine making, the production of table grapes or the production of special wines, but which were temporarily authorized in application of Council Regulation (EEC) No 347/79 (8), is a further matter requiring attention;

(viii) the definition of 'wine producer' in the present regulations in the case of cooperatives or private wineries has the effect that the measures for the compulsory distillation of table wine are not applied directly to producers of grapes for vinification (see paragraph 7.13);

(ix) above all there is an urgent need to establish a vineyard register which was first proposed as long ago as 1962. The Court considers such a register to be essential to monitor production capacity. While the Council has recently, on the basis of a proposal of the Commission, adopted a regulation (9) for the establishment of such a register a further period of six years is fixed before the register will become operational.

## 7. EFFECTIVENESS OF THE DISTILLATION MEASURES

### *Disposal of surplus wine*

7.1. The wine distillation measures are the principal means of disposing of surplus wine in the Community. The Community structural surplus is about 20 Mio hectolitres annually, i.e. approximately 20 % of total production of table wine, and it seems set to continue if not to increase.

7.2. One of the reasons for the production increases has been the ever-increasing yield achieved by producers, as a result of which wine production continues to increase although the area under vines is being reduced under the influence of Community structural measures (the area diminished by 180 000 hectares between 1981 and 1985). Another important factor, in the Court's view, has been the Community distillation regime, which by providing an assured outlet at a price which is attractive to the producer, has encouraged the continuing production of wine which can find no market outlet and which is consequently produced for distillation.

7.3. As regards the distillation measures the Court wishes to highlight the following:

- (a) the price structure for table wines as established by the Community offers no incentive to improve the quality of table wines. The production of better quality table wine is economically unattractive to the producers because it usually implies reduced yields;

- (b) the subsidy for distillation measures based solely on the alcoholic strength of the wines encourages either the production of wines of high alcoholic content, although the market trend is for lower alcoholic strength wines, or the achievement of high yields to the detriment of quality;
- (c) moreover, the exclusive use of alcoholic strength as a basis for the subsidy is conducive to the fraudulent increase of this element if the wine is destined for distillation;
- (d) in view of the important structural surplus, the minimum buying-in prices established for many of the Community distillation measures are considered by the Court to represent an incentive to produce table wine specifically to take advantage of the distillation measures. This is especially the case for the price support guarantee distillation reserved for the holders of long-term storage contracts. The minimum buying-in price for this measure, set at some 90 % of the guide price guarantees the producer a price significantly in excess of market prices. Furthermore, the Court questions the economics of firstly paying for the storage of the wine for a period of nine months before it is distilled, especially as a large percentage of producers would seem to be interested in concluding private storage contracts only in order to take advantage of these distillation measures to the maximum extent possible.

#### *Disposal of alcohol stocks*

7.4. By converting surplus wine into alcohol the Community is confronted with another problem, namely, the creation of an oversupply situation in the alcohol market. Moreover, this alcohol is extremely costly: by the Commission's calculations <sup>(10)</sup> comparative costs for alcohol from different sources are as follows:

- synthetic alcohol: between 35 and 41 ECU/hl;
- wheat alcohol: between 56 and 63 ECU/hl;
- wine alcohol: approximately 388 ECU/hl.

Because of its cost the majority of alcohol produced from wine has to date been stored, with the result that stocks in the Member States amounted to approximately 13,4 Mio hectolitres as at 31 August 1986. Notwithstanding its non-commercial cost, many distilleries, especially in Italy and to a lesser extent in France, function solely on the basis of such alcohol production and continuously increase their production and storage capacity because they find it profitable to do so.

7.5. The data available to the Commission does not allow a precise calculation of Community distillation aid paid on the current stocks. However, a total of 3 436,3 Mio ECU has been paid as such aid (including that for the by-products of winemaking) during the period 1980-1986 — when the present stocks of alcohol accumulated. By no means all of this has been passed on to the producers of wine in the minimum price paid by the distilleries. In fact, because the aid contains a relatively liberal allowance to cover distillation costs, based on the least efficient operators, the distilleries themselves retained a significant share (estimated by the Court to have been of the order of 650 Mio ECU on the stocks of alcohol as at 31 August 1986).

7.6. The situation with regard to the disposal of the alcohol stocks is as follows:

- (a) of the 13,4 Mio hl of alcohol in stock as at 31 August 1986, the costs associated with the disposal of some 9,7 Mio hectolitres, resulting from voluntary distillation measures, are at the full charge of the Member States whose decision it was to purchase the distillation products. The Italian authorities have recently succeeded in selling a substantial portion of their stocks (5,2 Mio hl) outside the Community at prices ranging between 5 and 9 ECU/hl and for delivery over a two-year period. However, this sale has effectively saturated traditional market outlets for the foreseeable future. In addition the presence of the remaining significant stocks (4,5 Mio hl) overhanging the market inevitably depresses market prices;
- (b) approximately 3,7 Mio hectolitres result from compulsory distillation operations. Because of the Community character of these stocks more recent figures are available. Thus, as at 30 November 1986 the stocks in question had risen to 4,0 Mio hectolitres. Of this, 0,67 Mio hectolitres, resulting from compulsory distillation of table wine (paragraph 3.10.(c)) are regarded as public stocks, the storage and disposal of which falls to be borne by the Community. The balance of 3,33 Mio hectolitres has an intermediate status in that storage costs are at the charge of the Member States as are the costs of disposal on the normal alcohol market. Losses due to disposal on other markets are, however, taken on charge by the Community. In practice, sales on the normal alcohol market have been negligible because, under the provisions <sup>(11)</sup> governing the sales, the alcohol must be offered at not less than the market price (taken to be 96 ECU per hectolitre) in order to avoid perturbations on this market. Recent efforts to dispose of these stocks to the fuel sector were unsuccessful despite a very low offer price. The Commission, in the 1986 Revenue and Expenditure Accounts <sup>(12)</sup> calculates at 95 ECU per hectolitre the potential disposal cost of the alcohol considered as public stocks. Applying the same calculation to the

4 Mio hectolitres referred to above would imply a total disposal cost of 380 Mio ECU.

7.7. Distillation is, therefore, a high cost-adding method of disposing of the wine surplus but one which does not add value to the resulting product.

#### *Compulsory distillation of table wine*

7.8. As a result of agreement reached at the meeting of the Heads of State or of Government held at Dublin in December 1984 measures were introduced providing for the compulsory distillation of table wine based on the yields per hectare achieved by producers. The measures were applied for the first time during the 1984/85 marketing year.

7.9. These measures are generally seen as an effective means of tackling the problem of over-production of wine in the Community by discouraging high yields through their progressive application.

7.10. The Court, while recognising that the measures are a step in the right direction, considers that they are, nonetheless, unlikely to put a brake on production to a significant degree, mainly because:

- (a) the prices offered to the producers, equal to 50 % of the guide price, are still attractive to producers in certain regions;
- (b) the implementing rules adopted by the Commission, by allowing for a system of transferring producers' obligations, render the measures an ineffective censure of high yields, all the more so, because the producer may transfer his obligation to a producer in any other wine-growing region of the Community who may even deliver a different type of wine. The Court considers that the provision of such a transfer system is contrary to the spirit of the European Council agreement which was expressly designed to discourage excessive yields.

7.11. As an illustration of the latter point, the Court noted during its audit that a series of transfers of obligations took place between French and Italian producers, mainly Sicilian, and between Northern and Southern Italian producers. Some transfers also took place between Greece and Italy. It appears that the distilleries acted as 'middlemen' in these transactions and that in Sicily, for instance, an inducement of as little as 200 Lires per alcoholic degree was sufficient for local producers to deliver wine on behalf of other producers subjected to the measure. Of the total of approximately 3,5 Mio hectolitres

of wine distilled in Italy under this measure, transfers accounted for:

- (a) 400 000 hectolitres on behalf of French producers;
- (b) 290 000 hectolitres of Greek wine distilled in Italy to satisfy the obligations of Italian producers.

Precise figures of transfers within Italy were unavailable at the time of the audit but officials of the intervention agency indicated them to be considerable, especially transfers from Northern to Sicilian producers.

7.12. While the transfer procedure may result in the cheapest wine being sent for distillation, nevertheless it provides the producers who achieve high yields with the opportunity to largely diminish the negative financial effects of the compulsory distillation measure. The Court considers, therefore, that the present arrangements for the compulsory distillation of table wine are not sufficient to discourage high yields, and the producers of mediocre wine are protected, through the transfer arrangements, from the commercial consequences of over production.

7.13. Furthermore, the effectiveness of the measures as a discouragement of high yields is largely diminished in the case of Greece because of the manner in which the special provisions were implemented and in the case of cooperative wineries in Italy. In both cases the application of the measures to the wineries rather than to the individual members who produced the high yields of grapes for vinification is a further major weakness. In the case of Greece the restriction of the measures to wineries with a production in excess of 10 000 hectolitres meant that members of small cooperatives who achieved high yields of grapes for vinification escaped the measures.

## 8. OVERALL CONCLUSIONS

### *Risks of irregularities of frauds inherent in the management and control systems*

### *Inadequacies in the provisions of the governing regulations*

8.1. The distillation measures currently in force have arisen from a series of ad hoc decisions rather than from a

global assessment of market requirements. As a result these measures are now a mixture of inducements and disincentives for producers without any clear overall coherence. It is difficult to justify the wide divergence in prices offered for the measures, ranging from a high of 91,5 % to a low of 40 % of the guide price. Such a wide range of prices is in itself an inducement to fraud in that it may encourage producers to seek to participate in the high-priced measures beyond their entitlements to do so (see paragraph 7.3(d)).

8.2. The greatest risk of irregularity or fraud arises directly from the inadequacies in the provisions relating to sample-taking and laboratory analysis of wine destined for distillation at the point of entry to the distilleries. These provisions are inadequate to detect adulterated wine (see paragraph 6.5(d)(iii)).

8.3. The method of calculating the Community aid, based as it is on the alcoholic strength of the wine, presents a temptation to producers to offer adulterated wine for distillation. The temptation is strengthened by the attractive prices offered for distillation and the minimal risks of being detected under the present arrangements. Official surveillance of products which could be used as a basis for the production of artificial wine is sometimes unsatisfactory in the Member States (see paragraph 7.3).

8.4. The present imprecision in the definition of table wine has increased the risk of fraudulent practices (see paragraph 6.5(d)(iv)).

8.5. The absence of a vineyard register twenty-four years after it was first envisaged, together with inadequate Community standards for establishing and verifying harvest, production and stock declarations, means that reliable statistics on production potential are not available in the main producing Member States with the exception of France (see paragraph 6.5(d)(ii)).

8.6. There is also an urgent need to strengthen the arrangements for controlling the vinification of table grapes given the risk that the resulting wine may be presented for distillation as table wine and thereby qualify for a higher Community aid than that foreseen (see paragraph 5.44).

8.7. Lack of detailed knowledge on the part of the Commission leads to weaknesses in administration and errors of interpretation by Member States (see Chapters 5 and 6 for details).

#### *Shortcomings in the control procedures of the Member States*

8.8. The most serious weakness under this heading is the over-reliance on documentary controls and the lack of emphasis on physical controls. The control services of the Member States have a wide range of duties, in addition to

the control of distillation measures, and are inadequately staffed. As a result there is a strong tendency, born of necessity, to concentrate controls on aspects of national importance to the detriment of Community-funded measures (see paragraphs 5.5, 5.13, 5.23, 5.29).

8.9. Particular concern arises as regards the controls over obligatory distillation measures. Attention is drawn to inadequacies in the controls of by-products of wine making and in assuring the obligatory distillation of wine produced from table grapes in certain Member States (see paragraph 5.38).

8.10. The unreliability of statistics furnished by some Member States makes fraud easier and, therefore, more likely, and renders control more difficult. The substantial revision of Italian statistics for 1984/85 should not have been accepted by the Commission without a thorough investigation (see paragraph 6.5(a)(iii)).

#### *Cases of frauds and irregularities reported to the Commission*

8.11. During the period under review the number of cases of fraud and irregularity reported to the Commission totalled 106 of which 12 cases were reported by France, 5 by Italy, 1 by Greece and 88 by the FR of Germany. In July 1985 the Commission wrote to the French and Italian authorities asking for an explanation as to why so few cases were reported by these Member States. The French authorities responded that checks performed by the control authorities normally either detect cases of attempted irregularity or fraud before Community aid is paid to beneficiaries or are followed by immediate action to recover funds incorrectly paid. The Commission has received no response from the Italian authorities to date.

8.12. As regards a fraud recently uncovered in Italy, involving the unauthorised use of methanol for the production of wine, the Commission services are conducting a detailed enquiry in cooperation with the control authorities of the Member State. Details of this enquiry are not, as yet, available.

#### *The structural surplus*

8.13. The main effect of the distillation measures is to transfer the problem of structural surplus from the wine to



the alcohol market. The cost of disposing of this alcohol will add 380 Mio ECU to future Community budgets (see paragraph 7.6(b)).

8.14. The imbalance between supply and demand in the Community wine market is largely due to a fall-off in consumption of table wine (of some 17 Mio hectolitres in 4 years). Yet, the demand side of the wine supply balance sheet has received very little attention. In particular:

- (a) no encouragement is given to producers for improving the quality of table wines by means of a properly differentiated price structure. Consumers' tastes have changed as is evidenced by the increasing per capita consumption of quality wines PSR. Moreover, improved quality normally implies reduced yields;
- (b) insufficient attention is paid to finding new uses either for the grapes prior to vinification or for wine by means of new wine-based products such as blush wines or wine coolers. Indeed, the commercialisation of such products is hindered or prohibited in certain Member States. The present series of aids for use of grape must have, notwithstanding their high cost, failed to make any discernible impact.

8.15. The structural surplus of table wine is also due to the ever-increasing yields. This increase has offset the reductions achieved as a result of Community structural measures<sup>(13)</sup>. As a result the Court sees an urgent need for more effective structural measures to bring about a significant reduction in the area under vines and thereby a reduction in the supply of table wine (see paragraph 7.2).

8.16. The Community distillation measures have created an unwanted stock of alcohol of about 13,4 Mio hectolitres as at 31 August 1986, for which there is no commercial outlet because of its extremely high production cost (see paragraph 7.4).

8.17. The measures have moreover contributed to the structural surplus by providing an assured outlet at excessively attractive prices for table wine which would otherwise not be disposed of. Many distilleries function solely on production of alcohol under Community provisions, and have increased their production and storage capacity (see paragraph 7.4).

8.18. The recently introduced measures for the compulsory distillation of table wine on the basis of yields per hectare are aimed at the consequences rather than the sources of the structural surplus problem. In any event they are unlikely to achieve more than marginal results, because the prices paid can still be relatively attractive. Furthermore the system of transfers allowed by the Commission enables producers to escape the financial sanctions contained in the measures. The volume of such transfers is itself an indication of the attractiveness for some producers of what was intended to be a punitive price (see paragraphs 7.8 — 7.12).

8.19. Alternatives must be sought to distillation measures which are a disguised and expensive method of destruction of surplus wine. There is an urgent need to allow the forces of supply and demand to operate in the Community wine market.

The present report was adopted by the Court of Auditors at Luxembourg at its meeting of 17 September 1987.

*For the Court of Auditors*

Marcel MART

President

(1) Quality wines 'PSR' means wines which satisfy the provisions of Council Regulation (EEC) No 338/79 (OJ L 54, 5.3.1979, p. 48) and those national rules adopted pursuant thereto. For the definition of table wine see paragraph 3.4 of this report.

(2) OJ L 30, 20.4.1962, p. 989.

(3) OJ L 54, 5.3.1979, p. 1.

(4) OJ L 84, 27.3.1987, p.1.

(5) By exerting pressure on the grapes the must is released and is filtered off ready for fermentation. Care must be taken, however, not to exert too much pressure as this might crush the stalks included with the grapes and even the pips of the grapes. Should such an event occur the wine could become harsh, astringent and bitter. The same principle applies to wine lees.

(6) OJ L 212, 3.8.1983, p. 1.

(7) OJ L 224, 21.8.1984, p. 14.

(8) OJ L 54, 5.3.1979, p. 75.

(9) Council Regulation (EEC) No 2392/86, OJ L 208, 31.7.1986, p. 1.

(10) Response to Parliamentary Question No 12/85, OJ C 304, 25.11.1985, p. 3.

(11) OJ L 165, 21.6.1986, p. 14.

(12) Doc. COM(87) 191 Final, Volume 5, Annex, Part B.

(13) See Court's Annual Report concerning the financial year 1984 (paragraphs 5.49 — 5.65), OJ C 326, 16.12.1985, p.1.

## ANNEX

## Principal elements and timing of Community support measures (Other than aid for the use of grape must)

Wine Marketing year  
(1 Sept.-31 August)

Sept.	Oct.	Nov.	Dec.	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.
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RemarksA. *Establishment of harvest estimates*

- First estimates
- Corrected estimates  
(depending on region)

	20.9		15.10	10.11
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B. *Private storage contracts*

- Approval of long term (9 months) contracts
- Approval of re-storage contracts

	15.12	15.2
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	1.8	31.10
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C. *Distillation measures*1. *Voluntary* (see para. 3.9)

Approval of contracts for:

- Preventive distillation
- Price support guarantee distillation

1.9		15.1
	15.9	15.11

- Support distillation

Period set out in implementing regulations  
- normally before 31.3.

*Buying-in price*  
(en % of guide price)

65%  
90% or 91,5%  
82%

The harvest estimates are essential to determine the appropriate support measures at the start of the wine year.

Opening of measure dependent in theory on presence of certain market conditions. In practice, however, the measure has become almost automatic.

Authorised when preliminary indications point to a large harvest which could lead to problems in storing the new wine.

From 1984/85 a quantity limit (currently  $\pm 13\%$  of production) is set per producer.

Original quantity limit of 18% of production was reduced to 15% in 1984/85 and to 13% in 1986/87.

The measure is opened at same time as compulsory distillation under Art. 41 (see below). A total quantity limit is established by Council (up to 5 Mio hl) which is divided between zones and between producers.

2. *Compulsory distillation* (See para. 3.10)

- Distillation of by-products of wine making

No contract required. Respect of measure is subject to surveillance and certification by designated control bodies in the Member States.

Price established annually on basis of alcohol content

In certain zones the producers are deemed to satisfy the measure if by-products are withdrawn and destroyed under supervision.

- Distillation of wine produced from grapes other than those approved for wine making

A time limit for distillation is set usually 31 July of current wine marketing year.

50 %

This measure covers wine produced from table grapes or from grapes classified both as wine-making varieties and as varieties suitable for other uses (e.g. manufacture of eau-de-vie).

- Distillation of table wine

No contract required. Control arrangements as for other compulsory measures above. Council must fix quantities to be distilled before 28 February. Time limits for delivering wine for distillation are:

50 or 40%  
(depending on volumes)

Implementing measures set out how the obligations of individual producers are to be established based on the yields per hectare achieved.

- 31 July if wine delivered to producer of wine fortified for distillation;
- 31 August if wine delivered to a distillery.

## THE COMMISSION'S REPLIES

### I. Preliminary

Wine-growers and dealers have seen a steady decline in the consumption of table wine since 1970. Although the consumption of quality wine produced in specified regions ('psr') has grown overall, consumption has fallen since 1971 at an average rate of 1 % per year, and in fact at a faster rate since 1980. As for production, that of table wine has stabilized, especially in recent years, but that of quality wine psr has increased: in 1971/72, quality wines psr accounted for only 15 % of total production, whereas the figure is now 24 %. It should be noted that among the quantities mentioned by the Court, the quality wines psr and many of the other wines, particularly those intended for the preparation of wine spirits of designated origin, are not eligible for Community intervention (about 28 % of total production). The distillation schemes thus concern 70 % of production, of which, on average, a third has enjoyed support.

Because of the appreciable increase in the table wine surplus from 1980 onwards, various schemes have been organized to cope with an unacceptable situation:

- sharp reduction in areas under vines by the execution of grubbing-up schemes corresponding to about 18 million hectolitres of table wine;
- compulsory action as regards distillation.

As the Commission felt that the voluntary grubbing-up measures were still not sufficient, action to restrict replanting rights for all classes of wine were proposed to the Council in 1986 and the Commission reminded the Council of these proposals when it made its 1987/88 price proposals, stressing the urgent need for action in this field.

Supplementing action already taken, the Commission laid before the Council proposals (COM(87) 1 final) including the following objectives

- that of strengthening compulsory distillation,
- that of creating conditions enabling cheap enrichment to be dispensed with.

The Council then adopted arrangements enabling the Commission to take the transitional measures necessary to avoid difficulties that could pose a threat to the achievement, or the balanced implementation, of compulsory distillation.

The report to be prepared by the Commission on enrichment, originally planned for 1990, will be ready by 1st September 1989, and the Council has undertaken to adopt decisions by qualified majority on the action to be taken in 1990.

In its August 1987 Communication to the Council (COM(87) 410 final), the Commission again stressed its plans to conduct a restrictive policy as regards intervention, with, in particular, a more steeply declining scale of prices for compulsory distillation and the eventual elimination of the wine relocation aid and of the special price support guarantee for longterm storage contract holders.

Also, in order to avoid any expenditure resulting from fraud and its harmful effect on the market, the Commission proposed to the Council that surveillance of the wine sector be tightened up through:

- the introduction by the Member States of a specialized control corps (agency, brigade or other) of a status corresponding to the scale of the wine sector in the relevant country;
- the creation of a limited corps of staff specialized in wine surveillance to be responsible, at Commission level, for ensuring by all necessary means, including participation in verification work carried out in the Member States, the uniform application of Community arrangements.

Discussion on this subject has been deferred until the end of 1987. As it will involve the respective responsibilities of various governments, particular difficulties must be expected.

## II. Observations on the various points mentioned in the report

its powers, the Commission gradually eased down this percentage to 13 % for 1986/87.

### 1. INTRODUCTION

#### ORIGINS AND SCOPE OF REPORT

1.7. As regards the observations under this point, the Commission would refer to the replies made on the corresponding points in the various parts of this Report.

The Commission is aware of the problems mentioned by the Court as regards checks made by the Member States, in particular physical checks. It has drawn the attention of the national administrative staffs to these problems and, as far as possible, has allowed for financial implications. This was the approach it adopted on this point in relevant proposals in connection with the 1987/88 price proposals. In this connection, it proposed the establishment of a specialized surveillance corps of a status corresponding to the importance of the wine sector in the relevant country.

#### 2. REVIEW OF THE WINE MARKET 1981/82 — 1985/86

##### *Main features of production in the Member States*

##### Germany

2.15. Since 1984, the situation has become clearer: German growers must enter on their production declarations, to be made by 15 December, the volume of wine deemed to be table wine and the volume of wine deemed to be suitable to become quality wine. Where a wine suitable for yielding quality wine does not become quality wine, it is no longer eligible for optional Community intervention. The rights to such intervention are based on declared production.

##### *Approval of distillation contracts for voluntary distillation measures*

5.12.(a) If a producer cannot provide proper evidence of having complied with the requirements arising under the various compulsory distillation schemes, he is not eligible for optional distillation schemes in the following year. If, at the time of the conclusion of the optional distillation contract, the producer in question cannot yet, for administrative reasons, provide evidence of having complied with the requirements, any advance payment is subject to security, so that if the evidence is not provided, the advance payment can be recovered.

### 3. MAIN FEATURES OF THE COMMON ORGANISATION OF THE MARKET IN WINE

#### *The Community distillation measures*

3.9.(b) As regards distillation supplementary to long-term storage contracts (price support guarantee), the Council regulation permits delivery of up to 18 % of the production of the preceding year of the producer who concluded a long-term private storage contract. Exercising

5.12.(b) Before allowing a wine-grower to use optional intervention facilities, the Member States must verify the evidence submitted by the grower that he has met the various obligations imposed under Community regulations. Such verification is not necessarily carried out in the same way in all the Member States. The German authorities have confirmed that the obligation in connection with the delivery of by-products (Article 35 of Regulation (EEC) 822/87) is verified on the basis of the registers of the growers concerned, while any obligations in connection with compulsory table wine distillation (Article 39 of Regulation (EEC) No 822/87) are verified on the basis of individual files held by the intervention agency.

5.13-5.52. See introduction to this chapter.

Member States, the uniform application of Community provisions.

### *Supervision of alcohol produced*

5.53. The Commission recalls that it has on four occasions laid before the Council proposals for a market organization for alcohol, the last of which was submitted in 1983 (OJ No C 214, 10.8.1983, p. 7). These proposals have not been adopted by the Council.

The Commission recalls on this occasion the efforts it has made in the past, jointly with Parliament, which regrettably have not found concrete expression in Community regulations.

## 6. MANAGEMENT BY THE COMMISSION

The efforts made to improve equilibrium as regards wine have led to an important set of provisions such as restrictions on planting, discipline as regards replanting rights, an obligation to distil wine produced from table grapes and by-products, limitation on access to optional schemes, compulsory distillation, etc. If results are to match requirements, it is essential to ensure that legislation is properly implemented.

6.3. The various visits made by its staff in connection with accounts clearance work have enabled the Commission to obtain a better picture of the management and control systems operated in the Member States. In this connection, the Commission now has relatively accurate and full information on the purpose, nature and scope of the verification work carried out by the national departments. This documentation is satisfactory as regards France and Germany. For Italy and Greece, the next visits will provide further information for the Commission.

At the present time, verification in the Member States is the responsibility of a wide variety of agencies, having little or no special experience of wine matters. Their effectiveness is definitely restricted by this dispersion, the lack of specific responsibility and administrative fragmentation. Failure to comply with regulations can be detected at the present time only when the EAGGF carries out verification work after the fact. Also, serious difficulties were caused both in 1985 and in 1986 by large-scale fraud (glycol ethylene and methanol in certain wines) and, at least in the short term, this discouraged consumption.

Lastly, the introduction of new Community control methods (systems audit) from 1986 onwards, should enable the Commission to broaden and deepen its knowledge of national control systems and check their reliability.

If expenditure resulting from fraud and its harmful impact on the market is to be avoided, the action started by the Council for the adoption of the regulation on the vineyard register must therefore be supplemented by other measures the purpose of which is:

6.4. Direct contacts on the spots are not one of the market management staff's main tasks. Nonetheless, the officials in these departments obtain information directly from the Member States, where opportunities arise, on the operation of the market organization. Normally, they gather the necessary information concerning the market and the application of the regulations directly from the Member States' departments and wine organizations and through regular discussions in the management and advisory committees, and from wine publications.

The information on the national implementing rules received is regularly checked and placed at the disposal of the Commission's accounts clearance staff.

- to require the establishment by the Member States of a specialized control corps (agency, brigade or other), with a status corresponding to the scale of the wine sector in the relevant country;
- to set up a limited corps of staff specialized in wine verification responsible, at the level of the Commission, for ensuring by all necessary means, including participation in supervision work carried out in the

6.5.(a) (i) The Commission agrees that the market price monitoring system is not completely satisfactory, despite changes in criteria made on a number of occasions. The main problem is that much of the wine marketed is not necessarily covered by the quotations. The Commission is studying this matter and may, as appropriate, propose adaptations proving necessary. Also, the activation of intervention no longer depends solely, as in the past, on quotations reported.

6.5.(a) (ii) Regulation (EEC) No 2396/84 authorized the Commission, in connection with the establishment in

December of a forward estimate, to use information sources other than the Member States' communications.

This clause was adopted following appreciable corrections the Commission had to make in early 1984 in the estimate adopted in December 1983. Since then, the Commission has consulted other sources of information when adopting the forward estimate; these sources have provided data similar to those from the Member States. Also, in marketing years after 1983/84, the estimates made in connection with the various forward estimates have been confirmed by the out-turn.

6.5.(a) (iii) The Commission is now carrying out an investigation in Italy concerning irregularities relating to balance sheets for wine. The audit authorities are kept regularly informed of the progress of procedures. The Commission will act as appropriate in respect of any financial consequences on the basis of the results of the investigation.

6.5.(b) It is not the lack of information which leads to the almost automatic activation of distillation operations but the existence of structural surpluses on the table wine market. The wisdom of these distillation decisions, in terms of overall market equilibrium, has never been criticized after the event.

6.5.(c) (i) See general comments, Chapters 5 and 6.

6.5.(c) (ii) The Commission, having noted that the quantities of by-products distilled did not match production volumes, proposed to the Council, which adopted it in 1982, Article 47 of the basic regulation [now Regulation (EEC) No 822/87], stipulating that before he may qualify for Community schemes the grower must provide proper evidence that he has complied with all the obligations incumbent upon him (including the distillation of by-products).

The Commission is now studying problems connected with the production of wine made from grapes enjoying double classification. It will submit a report, during 1987/88, on the subject, and if necessary, will propose appropriate amendments to the regulations.

6.5.(d) (i) It is true that the Commission believes that a minimum level of physical verification should be defined. However, the lack of vineyard registers in some Member States may render such supervision difficult. It is now reviewing this matter. Obviously, the introduction of a Community vineyard register, the creation of which was agreed in 1986 and which will be phased in over six years, will facilitate verification. The Commission will be ensuring that this work is carried out as promptly as possible within the deadlines set.

6.5.(d) (ii) and (iii) In early 1986, the Commission submitted to the Council a proposal, which is still pending, for amendment of the general distillation rules and providing for tighter verification on entry into the distilleries. The Commission is planning a system of systematic sampling on intake, allowing both of random analyses and of analyses whenever there is evidence that the wine does not comply with Community legislation. It is very likely that this system will provide for a minimum number of such analyses. Also, it is planned to promote at Community level the implementation of the verification method developed by Professor Martin, one advantage of which is that it enables fraudulent enrichment to be detected. In this connection, the Commission may finance the equipment of the wine-growing Member States with the apparatus required for the analyses.

6.5.(d) (iv) Community regulations include not only the definition of table wines but specify very clearly the oenological practices authorized for table wine (Annex VI to Regulation (EEC) No 822/87). The detection of adulteration does not depend, however, so much on the definition as on the number and quality of checks carried out (see reply to point 6.5.(c)(ii)).

6.5.(d) (vi) Because national administrative rules must be accommodated, the definition of the concept of 'proof' is an exclusive responsibility of the Member States. Should the Commission find that in some Member States this 'proof' is not satisfactory, it asks the Member State to modify the definition.

6.5.(d) (viii) and (ix) In certain Member States, it is impossible, in administrative terms, to 'individualize' the production of grapes within a cooperative winery. Here, the obligation to distil applies to all the growers in the cooperative. The vineyard register to be set up should solve this problem.

## 7. EFFECTIVENESS OF THE DISTILLATION MEASURES

### *Disposal of surplus wine*

7.2. As mentioned at the outset, the surplus is not due to an increase in the volumes of table wine produced but is essentially due to a decline in the consumption of this type of wine.

A wine-grower can take part in intervention schemes only in respect of part of his harvest. For example, a table wine grower with a yield per hectare of 125 hl, using all opportunities under the intervention scheme (including the obligations), could send a maximum of 44 % of his production of table wine to distillation, obtaining only an average price of about 69 % of the guide price, an average price well below the present market price.

7.3.(a) (b) and (c) High natural alcoholic strength of a wine is generally regarded as an important indication of its quality, not only because of the alcohol itself, but also, and mainly, because other important qualitative features are associated with strength. High natural alcoholic strength is normally obtained on the basis of low yields. Conversely, low natural strength often correlates with high yields. However, if the prices set for distillation were to give privileged treatment to low strength and high yield wines, this could constitute an incentive to stepping up production of such wines.

The Community regulations stipulate that alcoholic strength can be increased by enrichment with sucrose or with concentrated must the price of which is reduced by an aid at the level of that of sucrose. The Commission has always argued in the Council against this practice since it is an incentive to high yields per hectare.

7.3.(d) As regards market management, since 1984 the Commission has been gradually reducing high price intervention and tightening up the compulsory distillation system, a form of distillation which is carried out not only at low prices but which also tends to penalize high yields: during the 1986/87 marketing year, compulsory distillation was decided for nearly 23 million hectolitres, including the deductible part of the preventive distillation, out of an overall table wine surplus estimated at 36 million hectolitres.

The Commission is acting prudently in this connection. In the light of a joint statement by Parliament, the Council and the Commission, on the occasion of concerted discussion on the revisions of the wine market organization regulations in March 1985, it was recalled that the various intervention measures provided for by the regulations with a view to reorganizing the market must be applied in a balanced manner.

7.4. Wine alcohol disposal machinery is ill-adapted to needs, and this constitutes a greater difficulty than that of cost, although the costs are high.

The present aid is not generous enough to enable a distiller to face himself competition from molasses and synthetic

alcohol, knowing that, in addition, the national intervention agencies operate, with supplementary national aids, prices which are tantamount to a prohibition on the distiller to sell directly (see the question raised by the Court at point 7.6.(b), 'intermediate status').

7.8 to 7.12. The obligation upon each grower, under the compulsory distillation procedure, is calculated on the basis of his yield per hectare and on the basis of the volume of table wine produced, regardless as to whether there is an application for delivery to another producer (transfer). A grower will take the decision to make a transfer only if the price offered for his wine on the market is higher than elsewhere: in other words, if he has found an outlet for his own wine. On the assumption that the price is lower, for example in Sicily, there will be, for this wine, a demand in connection with the transfers and consequently wine prices in Sicily will increase and come closer to the other prices in the Community; this has been confirmed, in particular in 1984/85 in Sicily. Accordingly, the transfers will automatically come to an end and the wine price in Sicily will be more consistent with the other prices than before.

The transfers also dispel, at least in part, the difficulties connected with the fact that the 'Dublin' rule places an obligation on growers on the basis of yields obtained, regardless of the price they obtain for their wine on the market. A grower whose table wine is at a price higher than the guide prices (this is true for all wines of certain growers in other regions) would be forced, without the transfers, to deliver wine which is popular on the market. Certain good wines would thus be withdrawn from the market while the less popular ones would stay on it. It is obvious that the transfers also have disadvantages. The Commission, on the basis of experience gained, will review the various aspects before reaching a decision as to the possible termination of the transfer scheme.

#### *Compulsory distillation of table wine*

7.13. Greece has specific administrative problems which have been allowed for in the regulations

## 8. OVERALL CONCLUSIONS

The Commission agrees with the Court on the problems raised by the wine sector and, more particularly, as regards

Community distillation measures. Like the Court, it has pinpointed weaknesses which it has been endeavouring to eliminate for years. Proposals along these lines have been laid before the Council, in particular as regards the last two major reorganizations, on the occasion of the proposals for prices and related measures for 1986/87 and 1987/88. Many of these proposals are still pending in the Council.

The Commission confirms its commitment to strengthen the drive against fraud and irregularities. This is now being

done with the right degree of firmness as far as funds available allow and within budgetary constraints. Commitments at the highest level have been entered into in this field. They will be reflected in practical proposals to be made without delay.

As the Commission has stated in its reply, certain grave irregularities have been detected. They will be the subject of procedures conducted diligently; the supervisory authorities will be kept regularly informed.



COMMISSION OF THE EUROPEAN COMMUNITIES

THE SINGLE ACT:

A new frontier

PROGRAMME OF THE COMMISSION FOR 1987:

Statement by Jacques Delors, President of the Commission, to the European Parliament,  
Strasbourg, 18 February 1987

*Bulletin of the European Commission. Supplement 1/87*

*The Single Act: A new frontier for Europe*

The signing and forthcoming entry into force of the Single European Act and the accession to the Community of Spain and Portugal (following that of Greece in 1981) have brought with them fundamental changes in the structure of the Community and the obligations of the Member States. The Single European Act improves significantly the institutional system and sets new objectives for the Community, notably the completion of the internal market by 1992 and the strengthening of economic and social cohesion.

If it is to succeed in its new responsibilities, the Community must first complete the reforms undertaken, especially since 1984, with the aim of adapting old policies to new conditions: reform of the common agricultural policy, reform of the structural Funds, and reform of the financing system. Once these reforms have been implemented, the Community will have to be given the resources needed to achieve the objectives of the Single act.

By amending the Treaty of Rome in this way, the Member States have set a new frontier for European integration. They have made a qualitative leap forward which must be turned to good account to equip our economies so that they can meet the challenges from abroad and return to more vigorous, job-creating growth.

For this reason, the Commission feels that it should set out the conditions to be met if this great venture is to succeed. This is the thinking behind the proposals it is laying before the Council and Parliament. They are set in a medium-term context, looking towards 1992, the deadline for completion of the large frontier-free market.

*Programme of the Commission for 1987*

This Supplement also contains the Commission's programme for 1987, as presented to Parliament by Mr Delors in February 1987.

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