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94/C 12/01

Special Report No 4/93 on the implementation of the quota system intended to control milk production together with the Commission's reply

1

I

(Information)

COURT OF AUDITORS

SPECIAL REPORT No 4/93

on

the implementation of the quota system intended to control milk production
together with the Commission's reply

(94/C 12/01)

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

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1. INTRODUCTION

Seeking to restore balance to the market in milk products

1.1. The Community market in milk products is characterized by a tendency towards an imbalance between supply and demand which leads to structural surpluses. These surpluses have to be disposed of by means of various Community aid measures and subsidies whose financing requires considerable budgetary appropriations. In 1977, the Community established a more direct link between milk production and the cost of its disposal by introducing the linear levy, also called the co-responsibility levy. This levy, which is proportional to production, is not a true own resource within the meaning of Article 201 of the Treaty in the same way as the levies provided for as part of the common organization of the market in the sugar sector. It was introduced in order to make producers responsible for their surpluses and, by being incorporated into the system of aid measures provided for under the common organization of the market in milk and milk products, corresponds in practice to a reduction in the net prices paid to producers. In 1984, the Council found that, despite the imposition of the co-responsibility levy, the quantities of milk produced were continuing to increase at an unacceptable rate. In order to avoid choosing a measure which would have a drastic effect on farmers' incomes, such as a substantial reduction in intervention prices or other measures with a similar effect, the Council decided to impose a kind of strait-jacket on milk production by introducing a quota system ⁽¹⁾ which included, in the event of the quota being exceeded, a heavy penalty, the additional levy.

Previous work by the Court of Auditors

1.2. In its Special Report No 2/87 on the quota/additional levy system in the milk sector, adopted on 15 July 1987 ⁽²⁾, the Court found that the objective of improving the balance between supply and demand had not been achieved because the quotas had been fixed at too high a level initially and because the dissuasive effect of the levy had itself been weakened by the interaction of the

amendments described below (see paragraph 4.18), thus leading to a watering-down of the penalty. The system itself gave rise to considerable inequalities between producers, which were compounded by the failure on the part of various Member States to comply with the regulations.

1.3. Subsequently, in its Annual Report concerning the financial year 1988 (paragraphs 5.33 — 5.38) ⁽³⁾, the Court highlighted the practices intended to modify *ex post facto* the regulations governing quotas in order to regularize the cases where some Member States had failed to comply with the rules. These resulted in adverse financial consequences for the Community budget and unequal treatment of producers and Member States.

The aims of the Court of Auditors' audit

1.4. Bearing in mind the changes detailed elsewhere, some of which have already been described in the Court's 1987 Special Report, and in view of the fact that since the beginning of the financial year 1990 the market in milk products, one of the largest common market organizations (CMO), has once again been showing a worrying imbalance, the Court has conducted a new audit in order to assess the extent to which the revised system for controlling milk production is suited to the task of meeting the set objectives. The system has been examined from the point of view of not only effectiveness but also efficiency and economy. The common organization of the market in milk and milk products has also been examined from the point of view of the consequences of applying a quota system. This scrutiny has focused on the application of the large number of measures provided for in the regulations.

1.5. The Court of Auditors' observations are based on its investigations in the Commission and in the eleven Member States governed by the system for controlling milk production, application in Portugal of the common organization of the market in milk and milk products having been postponed by the Act of Accession until 1 January 1991. The audit inquiries concern the balance between supply and demand in the milk sector, the systems set up for applying the measures and the changes in the regulations which have tended to make the system more complex and more difficult to manage.

⁽¹⁾ Council Regulation (EEC) No 856/84 of 31 May 1984 (OJ L 90, 1.4.1984, p. 10) introduces an additional levy on quantities of milk delivered or sold direct for consumption over and above a guaranteed threshold, i.e. the reference quantity. This scheme is usually known as the quota system.

⁽²⁾ OJ C 266, 5.10.1987.

⁽³⁾ Annual Report concerning the financial year 1988 together with the replies of the institutions, OJ C 312, 12.12.1989, p. 64.

2. THE MARKET IN MILK AND MILK PRODUCTS

Milk and how it is used

2.1. Milk consists of a large number of components whose proportion may vary considerably depending on the breed and age of the animal and on the quantity and quality of the feed consumed. For cows' milk, whose density is 1,03 kg/l, the main components, apart from water, are fat (between 30 and 48 g/l or between 2,9 % and 4,7 %), lactose (between 47 and 54 g/l), and proteins such as casein (between 27 and 33 g/l) and albumin (between 4 and 6 g/l). The proportion in which these components are found in the milk has a direct influence on the profitability of the dairy industries. For example, in most countries the price paid to the producer for the milk depends on certain quality criteria such as the milk's fat content, protein content, acidity, etc..

2.2. Milk is either used on the farm or else is marketed. On the farm it may be used for animal feed, human consumption or processing into farm cheese or butter.

2.3. Milk which is marketed, except for small quantities of raw milk sold direct to the final consumer, is treated or processed by the dairy industry. Where these treatments make use of all the solid components of the milk at the same time, except for a variable proportion of the fat, the main final products are pasteurized milk, sterilized milk, UHT milk, concentrated milk and milk powder.

2.4. The components of milk may be used separately, by means of skimming or coagulation. Skimming separates the cream, which is churned to produce butter and buttermilk, and the skimmed milk, which may be broken down into caseins, milk wheys and skimmed-milk powder; by coagulating the milk, curdled milk is obtained, which is used for making cheeses.

World production and world price trends

2.5. On the world market, the Community and the former USSR are the two main milk producers. In 1990, Community production stood at 109 million tonnes and represented 22 % of world production, which in the same year, after a decade of low but steady growth, reached a

record 476 million tonnes. An examination of the main geographical areas shows that in the Eighties milk production increased in the Third World and in the former USSR (109 million tonnes in 1990 or 22 % of world production), whereas in North America (85 million tonnes in 1990 or 18 % of world production) and in Oceania (14,5 million tonnes in 1990 or 3 % of world production) it levelled off and in Europe, particularly in the Community, it decreased.

2.6. Data on trading on the world market point to a downward trend in prices during the first half of the Eighties. This trend was then reversed, with prices picking up sharply in 1987, and this continued in 1988 and 1989.

2.7. In 1990 and 1991 there was a slight downturn in world prices of butter and skimmed-milk powder, but these prices were nevertheless still much higher than pre-1988 levels.

2.8. Even though the prices of butter and skimmed-milk powder on the world markets have virtually doubled from their 1986 level, they are still markedly lower than Community intervention prices. For butter, the intervention price (see paragraph 3.5) is in fact almost three times the world price.

Changes in milk production in the Community

2.9. Milk, which, in terms of value, accounted for 15,8 % of the Community's final agricultural production in 1991, is by far the most important agricultural product. There are one and a half million farmers in the Community producing milk.

2.10. Within the Community, the importance of milk varies considerably from one country to another: in the northern Member States, the share of the milk sector corresponds roughly to one fifth of final agricultural production, the highest proportions being in Ireland (31,7 % in 1991) and Luxembourg (47,3 % in 1991), whereas in the Mediterranean Member States the share of this sector is below 15 % (see Annex XVIII).

2.11. The Member States which are the main producers are France and Germany with a 1990 production of 26,5 million tonnes and 23,6 million tonnes respectively (excluding the former German Democratic Republic's milk production estimated at 4,9 million tonnes), i.e. 46 % of the Community's milk production.

2.12. Since 1983, the milk production of the Community, calculated for the Community of Twelve, has decreased from 118,8 million tonnes to 109,0 million tonnes in 1990, which is equivalent to a fall of 8,2 % during the period of application of the system for controlling milk production (see Annex VI). This reduction applies to most of the Member States. The fall in milk production was low in Ireland and Luxembourg. From the outset, these two countries received an additional quota deducted from the Community reserve because of the important role played by milk production in these two Member States (see Annex VII). It is difficult to evaluate the variation in production in Italy and Greece ⁽¹⁾ where the incomplete application of the system has stripped it of its dissuasive nature, thus making it ineffective. In Spain, the Court was not able to determine the true trend in milk production, which, according to the statistics sent to the Commission, remained below the guaranteed total quantity. In the absence of the statements stipulated ⁽²⁾, the Court was not able, during the inquiries it conducted in 1991 and early 1992, to obtain from the Spanish authorities the data which would have enabled it to verify whether the milk production exceeded the guaranteed total quantity.

2.13. Excluding the small quantities of milk consumed on farm, all the milk and milk products produced are either delivered to a dairy (about 90,5 % of milk production) or sold direct to consumers (about 3 % of milk production). Deliveries to dairies thus represent by far the main use of milk production and they are the use for which the most reliable data are available. According to the statistics available, the proportion of deliveries in relation to the total milk production shrank between 1983 and 1990, falling from 92,1 % to 90,5 % for the Community of Twelve.

2.14. In the Member States with the most efficient milk production, direct sales account for a negligible percentage

(1) Since Greece is not self-sufficient in milk products, when its authorities thought that milk production was going to reach the level of the guaranteed total quantity, they requested an increase in the latter of around 20 %. — Written question No 1084/91 of Mr Filippou Pierros to the Commission, OJ C 311, 2.12.1991, p. 23.

(2) Commission Regulation (EEC) No 1546/88 of 3.6.1988 laying down detailed rules for the application of the additional levy referred to in Article 5c of Regulation (EEC) No 804/68, Articles 15 and 16, OJ L 139, 4.6.1988, p. 12.

of the production. Where statistics are available, which is not always the case, they show that direct sales are, to varying degrees, declining rapidly in all the Member States. If, in the case of those Member States which have not declared their direct sales, the guaranteed total quantities referred to in Regulation (EEC) No 857/84 are taken as the reference basis, it may be estimated that between 1985 and 1990 direct sales decreased from 3,5 % to 2,8 % of the Community's milk production, Portugal excluded.

2.15. On-farm own consumption is not included in the statistics. It is, however, possible to put a figure on it by calculating the percentage of the sum of deliveries and direct sales in relation to total production. Since this percentage fell from 94,8 % in 1985 to 93,4 % in 1990, own consumption has probably increased proportionally in relation to total production. It is likely even to have increased in absolute terms, rising from 5 970 000 to 7 089 000 tonnes (see Annex IX). The increase has probably been particularly high in Germany and the Netherlands, whereas in the Member States which have not implemented the quota system (Spain, Greece, Italy), own consumption is likely to have stayed at the same level as before the introduction of the quota system.

2.16. The figures in the table in Annex IX, estimated as described below, show that on-farm consumption by humans increased by around 20 % (+ 0,114 million tonnes), whilst the number of farms fell by 10 % between 1985 and 1987. This trend, which in all probability continued after 1987, is difficult to reconcile with farmers' tendency to make greater use of packaged milk products. One explication of this disparity may be that the declared quantities for direct sales are perhaps lower than is in the fact the case. Since some Member States do not have specific statistics for direct sales, it is difficult to investigate this aspect any more thoroughly.

Changes in the consumption of milk and milk products

2.17. Only about a quarter of milk production is consumed in the form of fresh products (milk for direct consumption, cream, yoghurt, etc.). The rest is processed into products which can be kept and stored more easily: butter (36 %), cheese (23 %), milk powder (5 %) and condensed milk (2 %).

2.18. Consumption of milk and milk products in the Community has been on the decline since 1987, decreasing

from about 95 million to 91 million tonnes in 1990, whereas the amount produced and marketed still stood in 1990 at around 102 million tonnes. This imbalance between production and consumption is all the more worrying in that consumption includes large subsidized sales of butter and skimmed-milk powder for animal feed.

2.19. In the EEC, per capita consumption of all milk products expressed in whole milk equivalent currently stands at around 310 kg per year, whereas ten years ago it stood at only 300 kg ⁽¹⁾. In general, consumption of milk products has increased in the Mediterranean countries, where consumption of milk products has always been lowest, and it has declined in the Member States where it was highest, particularly in Ireland, Denmark and the United Kingdom.

2.20. These changes in consumption are influenced not only by the prices of milk and milk products in relation to substitute products, but also by the alteration in consumer habits and by the availability of milk substitutes. Detailed examination of these changes shows a slight increase in the consumption of milk and fresh products (+ 10 % between 1983 and 1990), a rather larger rise in the consumption of cheese (+ 19,5 % between 1983 and 1990 — see Annex XII) and a sharp decline in the consumption of skimmed-milk powder (− 50 % between 1983 and 1990 — see Annex XI). Despite Community measures to promote the consumption of butter, the main milk product, the downward trend has speeded up during the last few years (− 12,7 % between 1987 and 1990 — see Annex X). The downturn in butter consumption is largely attributable to changes in the behaviour of consumers, who are tending to buy more competing products, such as margarine, reduced-fat butter and blends of milk fats and non-milk fats. These new products competing with certain milk products are continually appearing on the market; their market share is as yet quite small, but it is likely to expand to an extent which it is difficult to foresee.

Changes in exports and imports

2.21. Exports in terms of milk equivalent, after peaking at 16,5 million tonnes in 1988, of which about seven million tonnes of milk equivalent were exported to the former USSR in the form of butter, went down again to 12,8 million tonnes in 1990.

⁽¹⁾ The apparent paradox of declining total consumption (see paragraph 2.18) and rising per capita consumption may be explained by demographic variations in the population of the Community.

2.22. During the period following the introduction of the quota system, the Community saw its share of world trade rise from 42,9 % in 1985 to 48,1 % in 1990 in relation to a relatively stable total of between 27 and 30 million tonnes.

2.23. In 1990, imports of milk products into the Community may be estimated at over four million tonnes. Butter (88 728 tonnes in 1990, i.e. about 1,6 million tonnes of milk equivalent) is imported almost exclusively by the United Kingdom (62 159 tonnes in 1990). With regard to cheese, in 1990 Italy (36 787 tonnes), the United Kingdom (20 062 tonnes) and Germany (17 956 tonnes) accounted for two thirds of the 113 106 tonnes imported (more than one million tonnes of milk equivalent).

2.24. Even though some traditional flows of imports of milk products into the Community, particularly the United Kingdom's butter imports, have to date survived the Community preference as a result of international agreements, total imports from third countries account for only a very small proportion of Community consumption of milk products (about 4 %).

Food aid

2.25. Part of Community exports (about 10 %) can be attributed to food aid measures. In 1990, food aid to assist — usually the poorest — developing countries involved 8 885 tonnes of butteroil and 74 647 tonnes of skimmed-milk powder. This aid has shown a downward trend since 1982, with Community food aid programmes decreasing from 150 000 tonnes of skimmed-milk powder (about 1,6 million tonnes of milk equivalent) and 45 000 tonnes of butteroil (around 1,1 million tonnes of milk equivalent) to 94 100 tonnes of skimmed-milk powder (about 1 million tonnes of milk equivalent) and 18 000 tonnes of butteroil in 1990 (around 0,5 million tonnes of milk equivalent). In total, food aid exports have decreased from about 2,6 million tonnes to about 1,4 million tonnes of milk equivalent (see also paragraph 3.10). Budgetary expenditure to finance this food aid fell from 378,8 Mio ECU in 1984 to 103,3 Mio ECU in 1990 (see Annex XV).

Imbalance in the market in milk and milk products

2.26. In order to assess to what extent the market is in balance, it is necessary to look at various factors, namely the Community's degree of self-sufficiency in milk products, changes in Community stocks and developments in exports of milk products, including food aid.

The Community's degree of self-supply in the various milk products

2.27. For the three main milk products which are traded internationally, namely butter, skimmed-milk powder and cheese, the Community has far exceeded the level of self-supply.

2.28. During the period from 1983 to 1990, the output of butter sharply decreased. In 1983, butter production outstripped consumption by 50 %. Thanks mainly to the special measures to encourage butter consumption and because of the drop in production, the gap between butter output and consumption narrowed to 19 % in 1990.

2.29. In the case of skimmed-milk powder, consumption of which is still heavily subsidized, the imbalance worsened despite the considerable drop in production. In 1990, output exceeded Community consumption by 53 %, whereas up until 1988 the situation regarding production and consumption was distinctly more balanced.

2.30. In the cheese sector, the situation is less serious: as a result of a large increase in consumption, the latter is only 6 % to 8 % below production.

Changes in stocks of butter and skimmed-milk powder

2.31. In June 1991 stocks of butter and skimmed-milk powder reached a level equivalent to three and six months' consumption respectively. This level of stocks is not inordinately worrying. By contrast, the speed at which stocks can build up merely reflects the imbalance in the

market in milk and milk products and reveals the Community market's dependence on export operations that can be carried out at a particular time, as shown by the fluctuations in the stocks of butter and skimmed-milk powder during 1990. Between 1987 and 1989 these stocks decreased sharply and then levelled out at a few thousand tonnes; as of the second quarter of 1990, however, they again started to increase rapidly, reaching 450 000 t for butter and 498 000 t for skimmed-milk powder by 30 June 1991 (see Annexes XIII and XIV). This increase in stocks is due to too great a gap (18 million tonnes in 1990) between production (109 million tonnes in 1990) and consumption (91 million tonnes) and to a fall in exports, particularly in 1991 ⁽¹⁾. By contrast, stocks are decreasing only slowly, even though their disposal within the Community is encouraged by considerable subsidies.

Lack of solvent outlets for exports

2.32. Exports to third countries cannot be developed much for various reasons, in particular because they already represent nearly half of the world trade in milk products. In other parts of the world where demand could be solvent, especially in Asia, people traditionally consume fewer milk products than in western industrialized countries. Exported milk products, particularly those exported as food aid, are often used in the importing country to reconstitute milk products which are called fresh, such as whole milk, yoghurts and 'fromage frais'. In the poorest developing countries, which receive the most food aid, however, the local people do not have the buying power nor are there the public resources to allow small undertakings reconstituting milk products to balance their books.

The persistent imbalance

2.33. Since 1984, the recitals of various Council regulations ⁽²⁾ have regularly contained a description of the objectives to be achieved by the measures for controlling milk production.

(1) The fall in exports is mainly attributable to the Gulf War.
 (2) Council Regulation (EEC) No 856/84 of 31 March 1984 amending Council Regulation (EEC) No 804/68 of 27 June 1968 on the common organization of the market in milk and milk products, OJ L 90, 1.4.1984, p. 10.

2.34. Thus, in 1984, the Council stated that the market in milk products in the Community was suffering from structural surpluses as a result of an imbalance between supply and demand for milk products. It then noted that, despite the application of the co-responsibility levy introduced by Regulation (EEC) No 1079/77, quantities of milk delivered were increasing at a rate such that disposal of surpluses was imposing financial burdens and market difficulties which were jeopardizing the very future of the common agricultural policy ⁽¹⁾. When the quota system was introduced, the Council considered that a careful examination of the different possible ways of re-establishing balance in the milk sector showed that, despite the administrative difficulties which its implementation might involve, the most effective method, and the one having the least drastic effect on the incomes of producers, was the introduction of an additional levy on quantities of milk delivered beyond a guarantee threshold ⁽²⁾.

2.35. Two years later, in 1986, the Council stated ⁽³⁾ that market trends had shown that the level of guaranteed total quantities was higher than that deemed to be desirable for the purposes of striking a balance between supply and demand and that therefore the guaranteed total quantities ought to be reduced by 3 %.

2.36. Another two years later, in 1988, the Council stated again ⁽⁴⁾ that it was then clear that the results obtained from these arrangements would not suffice to achieve the objective of adaptation of supply to demand by the end of the five-year period of application of the quota system and the duration of the said arrangement would have to be extended to eight 12-month periods.

2.37. In June 1991, the Council still considered that the market in milk and milk products was in persistent surplus and that to meet the imperative need of attaining some

degree of balance between supply and demand the guaranteed total quantities needed to be reduced ⁽⁵⁾.

2.38. Thus, throughout the period of implementation of the measures for controlling milk production and in particular the quota system, the stated objective is the same, namely that of achieving some balance between supply and demand in the milk sector.

2.39. The Council's statements set out above show that the Community legislator, faced with the need to restrict the expenditure arising from the growing surpluses on the milk market, has chosen to introduce the quota system rather than reduce the support prices, even though the latter were in fact stimulating production which was often difficult to sell. By maintaining prices at levels that take account more of social needs linked to the maintaining of incomes than of the real situation on the market, the Community has, however, moved away from the logic of allocating resources according to economic performance, since producers have seized on the opportunity to produce a certain quantity of milk levy-free, which produces a guaranteed income regardless of their respective abilities.

3. THE COMMON ORGANIZATION OF THE MARKET IN MILK AND MILK PRODUCTS

3.1. The common organization of the market in milk and milk products was set up in 1968, at the same time as most of the other common market organizations, by Council Regulation (EEC) No 804/68 of 27 June 1968. This common market organization currently covers fresh milk, concentrated milk and powdered milk, as well as cream, butter and some types of cheese. Indirectly, all milk products benefit from the intervention system set up for butter and skimmed-milk powder.

The objectives

3.2. The common organization of the market aims to achieve the objectives defined in Article 39 of the Treaty. In

⁽¹⁾ Council Regulation (EEC) No 856/84 of 31 March 1984 amending Regulation (EEC) No 804/68 on the common organization of the market in milk and milk products, third recital, OJ L 90, 1.4.1984, p. 10.

⁽²⁾ As in the above footnote, fourth recital.

⁽³⁾ Council Regulation (EEC) No 1335/86 of 6 May 1986 amending Regulation (EEC) No 804/68 on the common organization of the market in milk and milk products, second recital, OJ L 119, 8.5.1986, p. 19.

⁽⁴⁾ Council Regulation (EEC) No 1109/88 of 25 April 1988 amending Regulation (EEC) No 804/68 on the common organization of the market in milk and milk products, first recital, OJ L 110, 29.4.1988, p. 27.

⁽⁵⁾ Council Regulation (EEC) No 1630/91 of 13 June 1991 amending Regulation (EEC) No 804/68 on the common organization of the market in milk and milk products, second recital, OJ L 150, 15.6.1991, p. 19.

order to fulfil these objectives, the Community regulations provide for a single trading system at the external frontiers and for intervention measures on the market to be taken in the Member States by intervention agencies. These measures need to be standardized so as not to impede the free movement of the goods in question within the Community.

3.3. By its management of the common organization of the market, the Commission therefore has to stabilize the market and ensure milk producers a fair income by maintaining the market price of milk at a target level specific to each milk year but standard for all the Community. It must also ensure reasonable prices for consumers.

The means and the mechanisms

3.4. It is by stabilizing prices, in particular of butter and skimmed-milk powder, that the Commission manages to keep the price of whole milk at the desired level. It was decided to concentrate intervention on these two products because, for the most part, any milk surpluses are processed into butter and skimmed-milk powder, as these products are easy to store.

Intervention prices

3.5. The main methods used to manage this common market organization are 'the annual fixing of a target price ⁽¹⁾ for milk, of threshold prices ⁽²⁾ for pilot products

⁽¹⁾ Council Regulation (EEC) No 804/68 of 27 June 1968, Article 3, OJ L 148, 28.6.1968, p. 13, stipulates that before 1 August of each year a target price for milk containing 3,7 % fat, delivered to dairy, shall be fixed in respect of the milk year beginning in the following year. The target price is 'that price which it is aimed to obtain for the aggregate of producers' milk sales, on the Community market and on external markets, during the milk year'.

⁽²⁾ Each year the Council, acting on a proposal from the Commission, fixes the Community threshold prices for certain products for the following milk year. These prices are fixed so that, account being taken of the protection required for the Community processing industry, the prices of imported milk products correspond to the level of the target price for milk.

of milk product groups... and of an intervention price ⁽³⁾ for butter' ⁽⁴⁾, skimmed-milk powder and some cheeses.

Intervention measures

3.6. The purpose of the intervention measures is to guarantee a common target price for milk delivered to dairies. To that end, in addition to intervention in respect of butter and fresh cream, other Community intervention measures were required to enable the best return to be obtained from milk proteins and to stabilize the prices of products which have special importance in determining producer prices for milk ⁽⁴⁾. The intervention measures take the form of the buying-up at a predetermined price by the intervention agencies of surpluses of butter and skimmed-milk powder, and of cheese, in particular Grana Padano and Parmigiano Reggiano, which are offered to them when these surpluses bring about a significant drop in the market prices. The surpluses thus bought up are stored in public warehouses. Aid is also paid for the private storage of these products in order to deal with seasonal surpluses.

Disposal measures

3.7. Since 1974, the Community has been taking measures to restore balance to the market. In order to absorb surplus production, it grants subsidies for the use of skimmed-milk powder, aid for the use of butterfats (e.g. aid for the purchase of butter by institutions and non-profit-making bodies, butter for pastry products, etc.) and subsidies for milk for schoolchildren, with a view to stimulating internal demand.

3.8. Furthermore, exporters receive refunds for their sales on the world market. Production surpluses, which tend to be self-perpetuating, often have the effect of depressing prices on the world market and, by means of the refunds which are thus augmented, increase the Community's budgetary expenditure.

⁽³⁾ Intervention prices are fixed for butter, skimmed-milk powder and some cheeses. The intervention agency is obliged to buy up the quantities which meet certain criteria as regards quality offered at this price, provided that purchases are not suspended. In that case, for butter, a system of purchasing by invitation to tender applies. Purchases of skimmed-milk powder are restricted to the period from 1 March to 31 August and to a quantity of 106 000 t. Above that, purchases may be suspended and the support of the market carried out by other measures.

⁽⁴⁾ Council Regulation (EEC) No 804/68 of 27 June 1968, second recital, OJ L 148, 28.6.1968, p. 13.

3.9. Food aid, in the form of butteroil ⁽¹⁾ (butteroil with a milk-fat content of not less than 99,8 %) and skimmed-milk powder, was, at least at the outset, also regarded as a way of disposing of surplus production, since consumption habits may change and the recipient developing countries may turn into solvent importer markets.

3.10. Despite these measures, sales to clear stocks at prices below intervention prices have in the past had to be held every so often (for example: the sale of 307 000 tonnes of butter to the former USSR in 1988).

The trading system

3.11. The creation of a single Community market for milk and milk products involves, apart from a single price system and intervention measures, the introduction of a single trading system at the external frontiers of the Community. This trading system is combined with the intervention measures and includes import levies and export refunds. The purpose of this regulated trading system is to stabilize the Community market, in particular by preventing price fluctuations on the world market from affecting the prices which prevail within the Community ⁽²⁾.

3.12. Community prices being far higher than world prices, exports are made possible only with the help of refunds paid to exporters. The cost of exports has increased, with spending on export refunds rising from 1 943,4 Mio ECU in 1984 to 1 945,8 Mio ECU in 1990, reaching a record 3 082,4 Mio ECU in 1988.

Measures for controlling milk production

3.13. As a result of experience acquired, the Community decision-makers came to realize that the market in milk and milk products could no longer be brought into balance by action relating solely to demand without also doing something about supply. They took the view, however, that a direct cut in prices sufficient to restore balance to the

market could not be made without this resulting in a drastic reduction in farmers' incomes. Thus, as a first step, they introduced the linear levy, also known as the co-responsibility levy, and then finally the quota system.

The linear levy or the co-responsibility levy

3.14. In the knowledge that the net price received by the producer is the main factor profoundly influencing supply, it was decided to introduce a co-responsibility levy in 1977 ⁽³⁾. At that time, the Council, which, at the beginning of each milk year, fixes the target price for milk for the forthcoming year, considered that a more direct link needed to be established between production and outlets for milk products by introducing for several years (no precise number has ever been specified) a uniform levy on all milk delivered to dairies and certain farm sales of milk products. Producers were thus forced to shoulder some of the financial responsibility for their surpluses.

3.15. The co-responsibility levy, which was fixed in September 1977 at a rate of 1,5 % of the target price, has been successively increased, reaching 3 % for the milk year 1984/85. Since 1 April 1989, following sales of butter to the former USSR, the introduction of the quota system and the favourable situation of the prices on the export markets, and with Community stocks being virtually non-existent, the Council has brought down the basic rate to 1,5 %. This levy does not apply to Portuguese producers nor to producers in mountain and hill areas and less-favoured areas ⁽⁴⁾.

3.16. In 1984, the Council stated that ⁽⁵⁾, over the years, the co-responsibility levy had lost its effectiveness and had failed to prevent the imbalance affecting the market in milk and milk products from worsening in the early Eighties. The effectiveness of the co-responsibility levy was definitely questioned, since, as part of the reform of the common agricultural policy, it was abolished.

⁽¹⁾ The composition and quality requirements for butteroil are described in the Commission communication regarding the characteristics of products to be supplied under the Community food-aid programme, OJ C 114, 29.4.1991, paragraph I.E.1., p. 6.

⁽²⁾ Council Regulation (EEC) No 804/68 of 27 June 1968, sixth recital, OJ L 148, 28.6.1968, p. 13.

⁽³⁾ Council Regulation (EEC) No 1079/77 of 17 May 1977 on a co-responsibility levy and on measures for expanding the markets in milk and milk products, OJ L 131, 26.5.1977, p. 6.

⁽⁴⁾ Council Regulation (EEC) No 1079/77 of 17 May 1977 on a co-responsibility levy and on measures for expanding the markets in milk and milk products, Article 1(2) and (3), OJ L 131, 26.5.1977, p. 6.

⁽⁵⁾ Council Regulation (EEC) No 856/84 of 31 March 1984 amending Regulation (EEC) No 804/68 on the common organization of the market in milk and milk products, fourth recital, OJ L 90, 1.4.1984, p. 10.

Other measures intended to restore balance to the market in milk and milk products

3.17. The introduction of the co-responsibility levy was accompanied by 'specific measures... to encourage the expansion of markets and the disposal of surpluses on the Community and world markets' (1). The proceeds of the linear levy are incorporated into the intervention system and serve to finance measures on the market, to improve the quality of milk and to subsidize the sale of milk to schoolchildren. The application of these measures was examined in the Court's Special Report No 1/86 (2).

3.18. The Council followed these measures with others also aimed at reducing supply, such as the aid to reduce the number of dairy cows, the premiums for the non-marketing of milk and premiums for the conversion of dairy herds (3).

3.19. Furthermore, the policy of intervention buying 'on demand' has also been altered, firstly by restricting intervention buying to one period of the year (4) and secondly by allowing intervention buying to be suspended if the market situation so warrants. During periods when intervention buying is thus suspended, market stability may be maintained by making use of the technique of standing invitations to tender (5) or by resuming buying-in when the market price has fallen to below a lower threshold (for example, 92 % of the intervention price) for a representative period.

The quota system

3.20. Lastly, another system for controlling milk production, which is generally known as the milk quota system,

(1) Council Regulation (EEC) No 1079/77 of 17 May 1977 on a co-responsibility levy and on measures for expanding the markets in milk and milk products, OJ L 131, 26.5.1977, p. 6.

(2) Special Report of the Court of Auditors on the contract measures for the expansion of markets for milk and milk products financed by proceeds of the co-responsibility levy, OJ C 127, 26.5.1986.

(3) Council Regulation (EEC) No 1078/77 of 17 May 1977, OJ L 131, 26.5.1977, p. 1.

(4) Council Regulation (EEC) No 773/87 of 16 March 1987 amending Regulation (EEC) No 804/68, OJ L 78, 20.3.1987, p. 1.

Council Regulation (EEC) No 777/87 of 16 March 1987 modifying the intervention arrangements for butter and skimmed-milk powder, OJ L 78, 20.3.1987, p. 10.

(5) Council Regulation (EEC) No 777/87 of 16 March 1987 modifying the intervention arrangements for butter and skimmed-milk powder, OJ L 78, 20.3.1987, p. 10.

was introduced by the Council at the time of the fixing of prices for the milk year 1984/85 and has since then been the central measure for restricting supply. This system provides for an annual individual reference quantity to be established, which, if it is exceeded, is backed up in law by a financial sanction, known as the additional levy. Initially established for a five-year period, this system was extended, in 1988 (6), until 31 March 1992. In 1992, the Council, as part of the reform of the common agricultural policy, retained the milk quota system for a further eight years.

3.21. The quota system makes a distinction between 'deliveries' to dairies and other types of industrial or commercial undertakings, which represent the main way of disposing of milk, and 'direct sales' to consumers of milk or derived farm products. For deliveries, Member States can choose (see Annex XXVI) between two formulas for applying the additional levy: Formula A, where the levy is payable by every producer who exceeds his quota, and Formula B, where the levy is payable by the purchaser (the dairy or other undertaking), which passes the burden on to the producers who have caused the overrun. Producers who have exceeded their specific 'direct sales' quota are obliged to pay the levy to a competent body. The Court considers that the Commission, bearing in mind the experience acquired over the past eight years in the various Member States, should examine which of the two formulas, A or B, is the most suitable, particularly from the point of view of sound financial management, for attaining the objectives of the quota system, i.e. bringing milk production under control. In December 1992, under the new system, the Council adopted the Commission recommendation of 1991 concerning a single formula.

3.22. For the milk years from 1984/85 to 1988/89, the guaranteed total quantity for deliveries to dairies has in principle been fixed at the level of the 1981 deliveries increased by 1 %. The guaranteed total quantity for deliveries for the Community of Ten was thus 99,5 million tonnes, except for the milk year 1984/85 where provision had been made for a transitional period with a quota of 99,9 million tonnes in order to make it easier for the sector to adapt.

3.23. Any exceeding of the individual reference quantity is 'penalized' by a Community levy, borne by the producers, called the additional levy. This levy, introduced

(6) Council Regulation (EEC) No 1109/88 of 25 April 1988 amending Regulation (EEC) No 804/68 on the common organization of the market in milk and milk products, OJ L 110, 29.4.1988, p. 27.

with effect from 1 April 1984 ⁽¹⁾, hits hard at the quantities marketed in excess of the quota. The amount of the levy should, in principle, cancel out the revenue corresponding to all milk delivered to dairies or sold directly by the producer over and above the individual reference quantity allocated previously.

3.24. The financial penalty imposed on quantities of milk delivered by producers in excess of their quota was originally fixed, per kilogram in excess, at 75 % of the target price for milk ⁽²⁾ for deliveries under Formula A and for direct sales, and at 100 % of the target price under Formula B (see paragraph 3.21). Since 1987 it has been the same for both formulas (100 %, then 115 % in 1990). The financial penalty (75 % of the target price) has remained unchanged for direct sales (see Annex VIII). Thus, for example, for the milk year 1990/91 the target price for milk was fixed at 268,1 ECU per tonne. For overruns of the specific quota for direct sales the additional levy is $268,1 \times 75 \% = 201,1$ ECU per tonne, whereas for the two delivery formulas, the financial penalty payable in the event of an overrun is $268,1 \times 115 \% = 308,3$ ECU per tonne. In its July 1991 Communication to the Council and the European Parliament on the development and future of the common agricultural policy, the Commission recommends that in the event of overrun of the individual reference quantity the penalty to be imposed on producers who have a direct sales quota be the same as that imposed on the other producers.

Budgetary revenue and expenditure in the milk sector

3.25. Until 1989 the milk sector was the most costly (about 20 % of EAGGF-Guarantee expenditure) of all the sectors of the common agricultural policy. It is only since 1990 that payments to the common organization of the markets in oils and fats and in protein plants have exceeded those relating to the market in milk products (see Annex XXI).

⁽¹⁾ Council Regulation (EEC) No 804/68 of 27 June 1968 on the common organization of the market in milk and milk products, as supplemented by Regulation (EEC) No 856/84 of 31 March 1984, therefore introduces, with effect from 1 April 1984, an 'additional levy' payable by producers who exceed the annual reference quantity that has been allocated to them.

⁽²⁾ Council Regulation (EEC) No 804/68 of 27 June 1968, Article 3, OJ L 148, 28.6.1968, p. 13, stipulates that before 1 August of each year a target price for milk shall be fixed in respect of the milk year beginning in the following calendar year. This target price is 'that price which it is aimed to obtain for the aggregate of producers' milk sales, on the Community market and on external markets, during the milk year'.

Changes in budgetary expenditure

3.26. Whereas between 1983 and 1991, total EAGGF-Guarantee expenditure doubled to stand at 31 527,8 Mio ECU in 1991, payments made in the context of the common organization of the market in milk and milk products have remained at more or less the same level since the introduction of the quota system. However, from 1983 to 1984 expenditure increased by 1 371,9 Mio ECU (+27,8 %). This rise in spending may be explained by an increase of 611,4 Mio ECU in storage costs and of 616,6 Mio ECU in export refunds (see Annex I), which reflects the problems encountered at that time in this market.

3.27. Total expenditure in the milk sector in 1991, prior to off-setting with the linear levy and the additional levy, was 6 786,3 Mio ECU, a rise of about 700 Mio ECU in comparison with the previous financial year, but at the same level as the spending of the financial years 1988 and 1989, which had been marked by particularly high export refunds (see Annex I). Current expenditure is, however, close to the nominal level recorded in 1984, i.e. when the quota system was introduced. It should nevertheless be pointed out that since the financial year 1989 quite a large item of expenditure, namely the refunds to Member States for the measures to dispose of butter in public storage (3 200 Mio ECU to be refunded over four years), has been entered in the accounts elsewhere than in Chapter 20 'Milk and Milk Products'; in 1991, this item amounted to 797,4 Mio ECU.

3.28. An analysis of the different types of expenditure for this market organization shows that expenditure on intervention gradually decreased from 2 729,7 Mio ECU in 1983 to 2 133,9 Mio ECU in 1991. Expenditure on disposal varies between 400 and 900 Mio ECU per year, to which must be added the four annual tranches of some 800 Mio ECU to reimburse the Member States, as of 1989, for the advance financing of the costs of disposing of public storage butter incurred in 1987 and 1988. The costs generated by the measures for controlling milk production, especially in the form of compensation for the definitive discontinuation or temporary suspension of milk production, amounted to 688,3 Mio ECU in 1991.

Changes in budgetary revenue

3.29. On the revenue side, the linear levy, which is the main item, decreased from 527,4 Mio ECU in 1983 to 292,0 Mio ECU in 1991. The additional levy has been

subject to considerable fluctuations, which are due to the varying degree to which quotas are exceeded and to variable off-setting on the same budget heading, examined in paragraph 3.30 of this report, against expenditure permitted by Regulation (EEC) No 857/84 for financing the buying-up of quotas for the restructuring of milk production; in 1985 in particular, the levy ended up as an item of expenditure because Germany was reimbursed for the levy which had been wrongly paid to the EAGGF in 1984. The co-responsibility levy and the additional levy combined represent only about 5,9 % of the total expenditure in the milk sector, leaving aside the specific measures to assist the reduction of production.

Budgetary booking of some revenue in the milk sector

3.30. The additional levy, like the co-responsibility levy, is not a Community own resource within the meaning of Article 201 of the Treaty. It is regarded as negative expenditure entered under Chapter 20 'Milk and Milk Products' of Title 2 of Part B of the budget. The Court must reiterate its earlier criticism of the use of the 'negative expenditure' method which involves some revenue being entered in the budget net of expenditure (see the Court's Annual Report concerning the financial year 1990, paragraphs 3.21 — 3.22) ⁽¹⁾. The practice of including negative items in the expenditure budget contravenes the budgetary principle that there should be no off-setting between income and expenditure, as laid down in Article 4(1) of the Financial Regulation in these words: 'all revenue and expenditure shall be entered in full in the budget and in the accounts without any adjustment against each other' ⁽²⁾.

4. IMPLEMENTATION OF MEASURES FOR CONTROLLING MILK PRODUCTION

4.1. Initially fixed at too high a level in relation to demand, the guaranteed reference quantities have been successively reduced by the Council since the quota system came into force (see Annex IV).

Changes in production and quotas

4.2. By way of an interim review of the situation, it is helpful to examine whether the quota system, particularly

⁽¹⁾ Annual Report concerning the financial year 1990 together with the institutions' replies, OJ C 324, 13.12.1991, p. 59.

⁽²⁾ Publication of the updated text of the Financial Regulation applicable to the general budget of the European Communities, OJ C 80, 25.3.1991, p. 4.

its 'deliveries to dairies' aspect, the system's biggest component, has succeeded in the course of successive milk years in controlling production.

4.3. After the system's first year of application (1984-1985), deliveries remained constantly in excess of the guaranteed total quantities for all the Community, even though they decreased from 99,2 million tonnes in the first milk year to 93,3 million tonnes (excluding Spain and Portugal) in the seventh (1990/91). The fall in production occurred mainly in the fourth (1987/88) and fifth years (1988/89), for which the quotas were reduced at the same time as measures relating to the definitive cessation and the temporary suspension of milk production came into force. From then until 1991, Community production was virtually stable.

4.4. With regard to relative quota overruns, it has been found that, for the fifth milk year (1988/89), the guaranteed total quantities were exceeded by far greater amounts than in the periods before or after (see graph in Annex V).

4.5. For the sixth milk year, i.e. 1989/90, deliveries totalled 98,7 million tonnes (Spain included), in comparison with 97,7 million tonnes of total quantities available. It should, nevertheless, be noted that the ceiling would have been exceeded by twice as much had the 'Nallet package' measures ⁽³⁾ not caused an overall increase of one per cent in the quantities available in the Member States at the time the milk year 1989/90 came to an end.

The non-application of the quota system by some Member States

4.6. The Court found that in the Member States where the major milk-producing regions are located, namely in the north of the Community, the measures for controlling milk production are applied relatively strictly, whereas in Spain, Greece and Italy the quota system is applied only in a fragmentary fashion (see paragraph 4.55).

Measures affecting prices

4.7. The measures for controlling milk production, of which the quota system is the cornerstone, reflect the legislator's desire to achieve a levelling-out and even a quantitative reduction in milk production, without

⁽³⁾ See footnote 1 on following page.

necessarily, however, having to make cuts in Community prices. Since the introduction of the quota system in 1984, the target prices have gone on being fixed for each milk year at a level which has remained more or less the same, i.e. 278,4 ECU per tonne for the milk years 1985/86 to 1989/90 and 268,1 ECU per tonne since the milk year 1991/92. Thus, from 1984 to 1987, the prices of milk paid to producers remained stable in most of the Member States. In the period 1988-1989, by contrast, they rose substantially in the Benelux, Germany, Denmark and Ireland. In this same period, the prices of milk paid to German, Danish and Luxembourgish producers even exceeded the target price of milk. In 1990 and 1991 the prices paid to producers in all the Member States except for Italy fell back down to below the target price (see Annex VIII). The prices paid to producers vary from one country to another and the price disparities may be quite large: in 1990 Italy had the highest price paid to producers with 34,48 ECU/100 kg, whilst the lowest price was in Ireland with 22,14 ECU/100 kg. These price differences are influenced above all by the Member States' level of self-sufficiency in milk products. In general, the prices paid to producers are lowest in Ireland, a country with a surplus of milk products and which exports them, whereas the prices paid to producers are highest in Italy, a country with a deficit of milk products and which imports them. With regard to the fluctuations over the years in the prices paid to producers, it has been found that the prices fall when Community stocks of butter and skimmed-milk powder increase and vice versa.

The relaxation of the quota system

4.8. The quota system has undergone successive modifications in order to reduce its constraints: this may be seen in the relaxation of the Community system in favour of systems geared to national needs and in the watering-down of the dissuasive effect of the additional levy.

The relaxation of the Community system in favour of systems geared to national needs

4.9. This relaxation of the quota system has two aspects: the complexity of the regulations and their disparate interpretations, and the adaptations of the quota system to national needs.

The complexity of the regulations and their disparate interpretations

4.10. The Community regulations, which were already highly complex when the Court's Special Report No 2/87

was published, have been subject to supplements and adjustments ⁽¹⁾ which have made it even more difficult to put control of milk production into practice. In fact, the

(1) Since 1986, several substantial amendments have been made to the quota system. The overall volume of guaranteed quantities, initially fixed in 1984, was reduced in 1986, and then in 1987 and again in 1991. In 1986 and in 1991, the Council, in conjunction with the quota cuts, set up a scheme for compensation for discontinuing milk production definitively and, in 1987, a scheme for compensation for the temporary withdrawal of a proportion of the quotas.

By contrast, additional quotas were granted in 1989 on two counts:

(a) firstly, 600 000 tonnes, following a judgment by the Court of Justice, to a certain category of producers, known as 'SLOM' (from the Dutch 'slachtoffers omschakeling' = victims of conversion), who had in the past given undertakings regarding the non-marketing of milk and milk products or the conversion of dairy herds (see paragraph 4.11) and who had been excluded from those granted individual quotas when the quota system was introduced;

(b) secondly, four Regulations of 11 December 1990, known as the 'Nallet package', which ended up by increasing the Member States' total quantities available by 1 % or 1 039 886 tonnes. This came as a result of granting additional quotas to certain 'priority' producers for an amount equivalent to 1 % of the guaranteed total quantities in the Community; it should be emphasized that, at the same time, the said quantities were reduced by 1 % and then increased again by 1 %; in fact, the reduction in the rate of temporary withdrawal of quotas from 5,5 % to 4,5 % which was made at the same time as the definitive quota reduction of 1 % meant that in the end the individual quotas that could actually be used remained the same;

In December 1990, the guaranteed total quantity was increased, for the period from 1 April 1991 to 31 March 1992, by 6 599 880 tonnes in order to take account of German unification. In June 1991 the guaranteed total reference quantities of all the Member States were reduced across the board by 2 % to take account of changes in the milk market; this across-the-board reduction was compensated for over a period of five years to the tune of 10 ECU per 100 kg and per year, i.e. a total of 0,5 ECU per kg. Under another decision taken at the same time, the 'SLOM' producers, following various judgments handed down by the Court of Justice, in particular in December 1990, received either the right to an individual reference quantity or an increase in the latter. At the same time, a second Community programme for the definitive discontinuation of milk production was introduced, the aim of which was to comply with the recent judgments of the Court of Justice without increasing the guaranteed total quantity. The purpose of this programme was therefore to buy back milk producers' individual reference quantities to the tune of 1 % of the guaranteed total quantity, i.e. about 1 million tonnes for the Community. This quantity of quotas was regarded as necessary in order to be able to grant the 'SLOM' producers referred to above the additional individual reference quantities to which they were entitled according to the Court of Justice's recent judgments.

The mechanisms for penalizing cases of exceeding the reference fat content of the milk delivered have also been amended several times since 1986.

quota system is regularly made more complicated by additional measures, such as the schemes for the definitive discontinuation of milk production, which are often tailored by each Member State to suit its own requirements (see Annex XXIV, paragraph 5), or the mobility of quotas in all forms of transfers. Thus, the large number of Community measures applied 'à la carte' in all their various forms by the Member States is only the tip of the iceberg as regards the complexity of these measures, which sometimes became more relaxed and sometimes more restrictive (see paragraphs 4.12 — 4.15).

4.11. The high number of appeals shows that milk producers have a great deal at stake and that the application of the regulations leaves enough room for differing interpretations to justify a request for a preliminary ruling. Without counting the judgments handed down by national courts, the Court of Justice of the European Communities has ruled on about 30 disputed cases concerning for the most part the allocation of individual reference quantities. The Court of Justice's decisions on the 'SLOM' ⁽¹⁾ cases (see paragraph 4.65) have had considerable consequences for the quota system in so far as about one million tonnes had to be reserved *ex post facto* for the 'SLOM' producers. On 29 January 1992, 102 appeals brought by natural or legal persons were still pending at the Court of Justice. Furthermore, the Court of Justice granted the 'SLOM' producers the right to receive damages and interest. In fact, by its Judgment of 19 May 1992 in Joined Cases C-104/89 and C-37/90, it ordered the Community to make good the damage suffered by the 'SLOM' producers by the fact that they were not allocated a reference quantity right from the introduction of the quota system in 1984. Some 800 applications for damages and interest have been made to the Commission ⁽²⁾.

The adjustments of the system to the Member States' national needs

4.12. Whilst the principles themselves are relatively simple, putting them into practice has gradually become more and more complex. For the initial allocation of the individual quotas, the Community regulations ⁽³⁾ fixed the reference periods and set a ceiling on the individual quotas

⁽¹⁾ SLOM = Slachtoffers omschakeling.

⁽²⁾ Immediately after the Court of Justice's judgment, the Council estimated the damages to be paid to the 'SLOM' producers at between 200 and 500 Mio ECU. In August 1992, the Commission's departments put the amount of these damages at around 100 Mio ECU.

⁽³⁾ Council Regulation (EEC) No 804/68 of 27 June 1968, OJ L 148, 28.6.1968, p. 13.

Council Regulation (EEC) No 857/84 of 31 March 1984 adopting general rules for the application of the additional levy, OJ L 90, 1.4.1984, p. 13.

per Member State in the form of a guaranteed total quantity (one for deliveries, which is directly derived from the basic Regulation, and one for direct sales ⁽⁴⁾).

4.13. The provisions have been amended several times: the first modifications were made between 1984 and 1986 in order to extend the Member States' power to adjust and modulate the quotas for the benefit of some categories of producer, whilst the second lot of amendments have been made on a number of occasions since 1984 in order to reduce or increase the Member States' guaranteed total quantities, to which must be added a reserve managed by the Community (see Annex VII).

4.14. Provision has been made in the above-mentioned Regulation (EEC) No 857/84 from the outset and subsequently in a wide variety of ways for measures allowing the Member States to set up national schemes for encouraging farmers to give up milk production and for reallocating quotas to farmers classified as priority. The Member States have made very varied use of these possibilities of buying up and reallocating quotas (see Annex XXV). They can buy up quotas by granting compensation paid in one or more instalments to producers who undertake to discontinue all or part of their milk production. The reference quantities thus released are, if need be, added to the national reserve with a view to reallocation according to criteria determined to this end.

4.15. The notion of the 'liable' Member State became reality as soon as provisions were introduced allowing Member States to off-set individual producers' overruns against their shortfalls in relation to their 'deliveries' quotas in various ways and, for the first two periods of application of the quota system, to pay into the Community budget only the levy corresponding solely to the amount by which the guaranteed national reference quantity was exceeded. Furthermore, the Member States have been granted the possibility of using the revenue from the additional levy that they have collected for financing national schemes for the cessation of milk production or for restructuring milk production when, overall, the maximum quantities of the said Member State have not been exceeded ⁽⁵⁾. These provisions increase the emphasis put on national responsibility. As a consequence, the geographical distribution of milk production tends to

⁽⁴⁾ Council Regulation (EEC) No 857/84 of 31 March 1984 adopting general rules for the application of the levy referred to in Article 5c of Regulation (EEC) No 804/68 in the milk and milk products sector, Annex, OJ L 90, 1.4.1984, p. 13.

⁽⁵⁾ Council Regulation (EEC) No 857/84 of 31 March 1984 adopting general rules for the application of the levy referred to in Article 5c of Regulation (EEC) No 804/68 in the milk and milk products sector, Article 9(4), OJ L 90, 1.4.1984, p. 13.

remain the same instead of developing in those regions where it has proved to be economically the most justified. Thus, regional specialization will be possible only at best within the Member States.

The dilution of the dissuasive effect of the additional levy

4.16. The Court has found that the dissuasive effect of the additional levy is watered down by several factors: the perpetuation of the general off-setting mechanism, the passing-on of the additional levy to individual producers, the way in which the transfers of reference quantities are made between direct sales and deliveries, the delays in collecting the levy, the inadequate adjustment in the case of overruns of the fat content, and quota mobility.

Perpetuation of the general off-setting mechanism and the passing-on of the additional levy to individual producers

4.17. The provision concerning the off-setting mechanism ⁽¹⁾, which was introduced as a provisional measure in 1985 and which authorizes the Member States to allocate the unused reference quantities of producers or purchasers to producers or purchasers in the same region and, if need be, in other regions, has been extended several times. Originally restricted to the first milk year (1984/85) because of producers' difficulties in adjusting to the new regulations on quotas, the so-called 'Article 4a' mechanism was prolonged for the second year, as of 1985, for the following three in 1987 ⁽²⁾, and in 1988 ⁽³⁾ until the expiry of the system (1992). This arrangement has thus taken on a

permanent, structural nature, 'given its flexibility,... in view of certain situations' ⁽⁴⁾. It applies to both deliveries and direct sales and may be adjusted according to certain criteria (special situation of various categories of persons liable for the levy, or of certain regions). The Article 4a mechanism, which has thus been repeatedly renewed by the Council, has a number of consequences with regard to the original objective of controlling milk production. On a general level, the wording of the text as amended in 1987 ⁽²⁾ and then in 1989 ⁽⁵⁾ allowed — and allows — the Member States to restrict the additional levy payable by the producers or purchasers to just the overrun of the guaranteed total quantity, i.e. the national quota. There has thus been a move right away from the notion of an individual quota, i.e. the idea which prevailed initially at the time of the introduction of the quotas and which aimed to make milk producers responsible for their surpluses by imposing on them, if they exceeded their quota, the penalty of the additional levy. By allowing overruns of quotas to be traded off against cases of quota shortfalls, however, the impact of the additional levy has been undermined.

4.18. In its Special Report No 2/87 on the quota/additional levy system, the Court pointed out that the joint application of the principle of national off-setting of quotas (see paragraph 4.17) and of Formula B (purchaser quota) had resulted in the dissuasive effect of the additional levy being weakened in the event of an overrun. In fact, the interplay of these mechanisms led to a 'dilution' of the levy (see Annex XXII), reflected in a reduction in the effective rate of the levy actually payable in the end by those producers who exceeded their quota.

4.19. In concrete terms, the way in which Article 4a is applied varies considerably from one Member State to another (see Annex XXVI). In most of the Member States, the producer does not know his final quota until the end of the milk year. Some Member States have set up systems for forecasting the potential amounts which will be available for distribution under the off-setting mechanism at the end of the milk year. One such country is Denmark, which has set up a forecasting system of this kind in order to minimize the risk of exceeding the individual reference quantity as supplemented by the off-setting procedure. In the Member States where off-setting is applied according to a system which favours certain priority producers, the latter feel encouraged to exceed the individual reference quantity which was allocated to them at the beginning of the milk year by the amount of off-setting they expect to benefit from at the end of the milk year.

⁽¹⁾ Council Regulation (EEC) No 590/85 of 26 February 1985 amending Regulation (EEC) No 857/84 adopting general rules for the application of the levy referred to in Article 5c of Regulation (EEC) No 804/68 in the milk and milk products sector, OJ L 68, 8.3.1985, p. 1.

⁽²⁾ Council Regulation (EEC) No 774/87 of 16 March 1987 amending Regulation (EEC) No 857/84, OJ L 78, 20.3.1987, p. 3.

⁽³⁾ Council Regulation (EEC) No 1110/88 of 25 April 1988 amending Regulation (EEC) No 857/84, OJ L 110, 29.4.1988, p. 28.

⁽⁴⁾ Council Regulation (EEC) No 1110/88 of 25 April 1988 amending Regulation (EEC) No 857/84, second recital, OJ L 110, 29.4.1988, p. 28.

⁽⁵⁾ Council Regulation (EEC) No 764/89 of 20 March 1989 amending Regulation (EEC) No 857/84, OJ L 84, 29.3.1989, p. 2.

4.20. The dilution effect was partly rectified by the change in the way of calculating the levy which was introduced in 1987 ⁽¹⁾ and became applicable as of the milk year 1986/87. For Formula B, it is a case of implementing the 'Danish' system, i.e. distributing the reference quantities that have not been used by producers within the dairies (purchasers) in proportion to the quotas of the producers who have overrun. Thus, only those producers who have recorded the biggest relative overruns in comparison to their quota pay the levy. Furthermore, a number of corrective provisions were introduced by the same amending Regulation, and again in 1988 ⁽²⁾, with the aim of imposing a 'surcharge' on the biggest overruns.

4.21. In Italy and Belgium, the additional levy was stripped of its dissuasive effect on milk producers for one of its first years in so far as it was the Member States themselves who, after much procrastinating, paid this levy out of their national budget. In addition, corrections carried out during the clearance of accounts procedure concerning the additional levy were not, generally speaking, passed on by the Member States to the producers.

Transfers of direct sales reference quantities to deliveries

4.22. In addition to their 'deliveries' quotas, the Member States have distributed amongst their producers the 'direct sales' quotas which have been allocated to them by the Community regulations. As mentioned above, the size of these quotas is small in comparison to deliveries (about 3 % of milk production); furthermore, there is insufficient information about the actual amounts of direct sales and they are not properly checked. Community regulations provide for transfers between the two categories of quota to be made in two ways:

- (a) under an amendment made in 1985 ⁽³⁾ (Regulation (EEC) No 804/68, Article 5c), at the request of the Member States the Commission can 'adjust' the national quotas for deliveries and for direct sales on the basis of objective data to take account of structural changes affecting these two categories of milk disposal by producers; several amending regulations have been adopted since 1985 and have resulted in net transfers of

quantities available from direct sales to deliveries. These successive transfers quite obviously show, at least to a certain extent, how generous the level was at which the direct sales quotas were originally fixed and their downward trend;

- (b) pursuant to an amendment (Regulation (EEC) No 857/84, Article 6a) also made in 1985 ⁽⁴⁾, individual producers who have two reference quantities (one for deliveries and one for direct sales) may, by a decision of the competent national authorities, obtain an increase in one of the reference quantities (and a corresponding decrease in the other) within a 12-month period to enable them to adapt to changes in their marketing requirements. The text provides for the corresponding movements to be entered in the national reserve which the Member States are required to constitute within each of the main categories. The way in which this procedure is interpreted varies considerably from one Member State to another, but on the whole they use it as a means of minimizing the amount by which they exceed their guaranteed total quantity for deliveries. Here again, this results in the impact of the individual quotas being reduced.

4.23. The case of Greece illustrates par excellence the uncertainty surrounding the volume of direct sales allocated at the outset as a specific quota. For the milk year 1984/85, the guaranteed total quantity for deliveries was fixed at 472 000 t and that specifically for direct sales at 116 000 t. In accordance with the provisions of the Regulation ⁽⁵⁾, the Commission transferred, in several stages, 110 000 t of the guaranteed total quantity specific to direct sales to the guaranteed total quantity for deliveries. Thus, for the milk year 1991/92, the two guaranteed total quantities, allowing for the reductions which have been decided in the mean time, are 525 985 t and 4 528 t respectively. These transfers were made by the Commission with much hesitation, especially the last transfer which it adopted ⁽⁶⁾.

4.24. A similar case to that of Greece is Spain. The guaranteed total quantity for direct sales fell from 750 000 t

⁽¹⁾ Council Regulation (EEC) No 773/87 of 16 March 1987 amending Regulation (EEC) No 804/68, OJ L 78, 20.3.1987, p. 1.

⁽²⁾ Council Regulation (EEC) No 744/88 of 21 March 1988 amending Regulation (EEC) No 804/68, OJ L 78, 23.3.1988, p. 1.

⁽³⁾ Council Regulation (EEC) No 1298/85 of 23 May 1985 amending Regulation (EEC) No 804/68, OJ L 137, 27.5.1985, p. 5.
Council Regulation (EEC) No 804/68 of 27 June 1968, Article 5c(7), 2nd subparagraph, OJ L 148, 28.6.1968, p. 13.

⁽⁴⁾ Council Regulation (EEC) No 590/85 of 26 February 1985 amending Regulation (EEC) No 857/84, OJ L 68, 8.3.1985, p. 1.

Council Regulation (EEC) No 857/84 of 31 March 1984 adopting general rules for the application of the levy referred to in Article 5c of Regulation (EEC) No 804/68 in the milk and milk products sector, Article 6a, OJ L 90, 1.4.1984, p. 13.

⁽⁵⁾ Council Regulation (EEC) No 804/68 of 27 June 1968, Article 5c(7), OJ L 148, 28.6.1968, p. 13.

⁽⁶⁾ Commission Regulation (EEC) No 3296/89 of 31 October 1989 amending Regulation (EEC) No 2033/85 adapting the guaranteed total quantities of milk and milk products referred to in Article 5c of Council Regulation (EEC) No 804/68 and in Article 6a of Council Regulation (EEC) No 857/84, OJ L 320, 1.11.1989, p. 45.

in 1986 to 527 500 t in 1989. These transfers made it possible to a large extent to off-set the reductions imposed by the Community regulations on the guaranteed total quantities for deliveries. The transfer decisions were taken in a climate of some uncertainty, given that the Spanish authorities have not allocated milk producers individual reference quantities for direct sales. The statistical data available show that, for the milk year 1989/90, direct sales exceeded their guaranteed total quantity by about 27 000 t⁽¹⁾. Spain, however, had not yet collected any additional levy at the time the audit was carried out in 1992. Milk producers who sell direct to consumers cannot after all be made responsible for any overrun at national level so long as they have not been allocated individual reference quantities for direct sales, which the Spanish authorities have still not done.

4.25. A review of the transfers adopted by the Commission (see Annex III) shows that most of the Member States have used the procedure described in paragraph 4.22(a).

4.26. Article 6a of Regulation (EEC) No 857/84 is a method which is being used more and more to limit the impact of the additional milk levy. Member States are inclined to use this method in preference to the inevitably cumbersome and restricting procedure of definitive transfers referred to above in paragraph 4.22(a); furthermore, the producers and purchasers have every interest in using the system of provisional transfers in preference to definitive transfers, which for them involves the risk of being deprived of a proportion of their total quotas for the benefit of the national reserve, which is then reallocated to priority producers. In this way, the field of application of the Article 6a procedure goes far beyond that for which it was intended. The application of Article 6a in the Member States is shown in Annex XXIII.

Delays in collecting the revenue deriving from the additional levy

4.27. Pursuant to the provisions of the Community regulations⁽²⁾, purchasers and direct sellers are required,

(1) The Spanish authorities' more recent statements show that the overrun could be bigger.

(2) Commission Regulation (EEC) No 1546/88 of 3 June 1988 laying down detailed rules for the application of the additional levy referred to in Article 5c of Regulation (EEC) No 804/68, Article 15(4) and Article 16(2), OJ L 139, 4.6.1988, p. 12.

within three months of the end of each 12-month period, to pay the competent agency of the Member State the amount of any additional levy which may be due.

4.28. With a very few exceptions, no payment was made by the purchasers within the time-limits stipulated. In some Member States, purchasers are several years in arrears with payment of part of the additional levy. Even though the purchasers are debtors to the competent agencies of the Member States, the latter do not take steps to collect the money due to them within the stipulated time-limits using the means at their disposal. In general, the purchasers refuse to pay until they have received the amounts due by the producers concerned. No Member State has imposed specific penal or administrative sanctions in cases where neither the purchaser nor the producer has settled his debts within the set time-limit. The introduction, as provided for in Commission Regulation (EEC) No 1432/88 laying down detailed rules for applying the co-responsibility levy in the cereals sector (Article 4(4))⁽³⁾, of penalties for overdue payment imposed on the producer and, if need be, on the purchaser, would undoubtedly ensure payment of the additional levy within the set time-limit and would boost the dissuasive impact of the levy.

4.29. The Commission has exerted pressure on the competent national agencies by deducting from the advances paid to the Member States the greater part of the revenue which the latter ought to have collected in additional levy. Italy and Germany have questioned whether the Commission has the right to do this and have summoned the latter before the Court of Justice of the European Communities. The Judgment handed down by the Court of Justice on 17 October 1991 (Cases C-342/89 and C-346/89) confirms that the Commission may, in the circumstances specified, reduce the advances paid to the Member States. The table in Annex XX summarizes the situation with regard to payments in arrears at 15 October 1991.

Inadequate correction in cases where the reference fat content is exceeded

4.30. The Commission determines 'the characteristics of the milk and, in particular, the fat content thereof, considered to be representative in order to establish the

(3) Commission Regulation (EEC) No 1432/88 laying down detailed rules for applying the co-responsibility levy in the cereals sector, OJ L 131, 27.5.1988, p. 37.

quantities of milk delivered or purchased' (1). In the event of the reference fat content (2) being exceeded for a given milk year, the quantity of milk delivered is increased according to a pre-determined formula. Such an increase may lead to quotas being exceeded or to an existing overrun being worsened. This may consequently result in the person concerned having to pay an amount of additional levy or may increase the amount for which he is already liable. Thus, the additional levy has not only a quantitative aspect but also a qualitative aspect in that it penalizes cases where the reference fat content is exceeded.

4.31. In spite of the numerous amendments made to this provision, it has proved difficult to implement (3). To put it simply, the Article in question has been made progressively stricter in its wording, more precise in the rules for calculating the final account but at the same time less severe in its consequences. The main points to note are as follows:

- (a) the clause which initially allowed the producer concerned to escape the levy increase if he could provide evidence that the excess (fat content) was a normal result of production conditions has disappeared;
- (b) in the event of the fat content being exceeded, the corrective mechanism is now applied if the fat content varies by 0,1 gram instead of by one gram per litre as previously; by contrast, as part of the penalty, deliveries are increased proportionally by 1,8 % per additional gram of fat instead of the previous 2,6 %, which is equivalent to reducing the penalty itself by some 30 %;
- (c) the decision, as of 1989, to take into account a negative difference with respect to the average reference content makes it possible, amongst producers delivering to the same purchaser, to off-set the differences with regard to the fat content of the year considered as representative.

(1) Council Regulation (EEC) No 857/84 of 31 March 1984, Article 11(c), OJ L 90, 1.4.1984, p. 13.

(2) Article 9 of implementing Regulation No 1371/84 of 16 May 1984, replaced by Article 12 of implementing Regulation (EEC) No 1546/88 of 3 June 1988 (which repeals the preceding Regulation), determines on the one hand the rules for establishing the reference fat content for the milk delivered, the reference period being in principle 1985/1986, and on the other the consequences of an increase in the content during a subsequent milk year.

(3) Commission Regulation (EEC) No 1033/89 of 20 April 1989 amending Regulation (EEC) No 1546/88, fifth recital, OJ L 110, 21.4.1989, p. 27.

4.32. These changes are tantamount to creating the notion of a national average fat content and, consequently, by the interaction of off-setting, they diminish the impact on individual producers of any overrun of the reference fat content. These amendments have the effect of undermining the liability of milk producers who are contributing to surplus production.

4.33. An examination of the application of the 'fats' mechanism, starting with the first milk year that may be regarded as 'normal' after the critical experiences of the first years, i.e. 1987/88, has revealed the extent of the difficulties encountered in the course of its implementation:

- (a) in France, the authorities refrained from applying the mechanism until the milk year 1989/90, putting forward as their reason the talks held with the Commission to obtain changes in the Regulation and the difficulties in determining the purchasers' reference fat content. The mechanism is admittedly particularly complex to implement, but this is no justification for the failure to declare actual overruns of the reference fat content for the period in question, which the intervention agency was aware of at least for the milk year 1988/89, and which results in the effectiveness of the additional levy being curtailed still further;
- (b) in Italy, the fats mechanism has not yet been applied. For all that, applying this mechanism would pose problems at a practical level because of the failure on the part of some purchasers to take milk quality criteria into account;
- (c) in the other Member States, except for Spain and Greece, the fat content of the milk was measured when the milk was delivered to the dairies. Thus, the systems already in operation lent themselves more to implementing the regulations on this subject, which does not, however, mean that there were no difficulties in applying them.

4.34. The upward trend in the fat content shown by the results since the introduction of the quota system leads to doubt also being cast on the dissuasive effect of the increase in the quantities of milk delivered following the overrun of the reference fat content. In several Member States, the penalty inflicted in the form of an additional levy depends wholly on the increase in the fat content over and above the reference rate. For the Community as a whole, half of the total overrun of the guaranteed total quantities can be attributed to the increase in the fat content. At the same time as milk production has been decreasing in volume, there has been an increase in the fat content, which has risen in the period from 1983 to 1990 from 3,86 % to 4,01 % of the weight of the milk (see Annex XIX). This improvement in the quality of the milk — which has in any case been sought — does, however, correspond to an

additional production of about 178 000 t of butter, i.e. it represents 10 % of total butter production or two thirds of the surplus butter produced in 1990 and sold into intervention. This increase in the fat content is equivalent, ignoring the corresponding production of skimmed-milk powder, to roughly an extra four million tonnes of milk ⁽¹⁾, in relation to a total production of 109 million tonnes in 1990.

Mobility of quotas

4.35. All the provisions relating to various transfers of quotas between individual producers have tended to undermine the effectiveness of the quota system.

4.36. The mobility of quotas is regulated as regards definitive transfers and temporary transfers (leasing) but less as regards the reallocation aspect, which is regulated in particular by means of the national restructuring schemes. By virtue of the principle whereby a reference quantity may not be transferred without the land ⁽²⁾, the purchase and sale of individual quotas without land is forbidden, but the Community regulations do not stipulate any penalties to be imposed on those who infringe this rule.

4.37. At the time of the introduction of the quota system ⁽³⁾, provisions were laid down governing transfers of quotas in the event of all or part of a holding being sold, leased or transferred by inheritance.

4.38. According to Commission Regulation (EEC) No 1546/88, 'temporary transfers... shall be recorded... (by) 31 July (at the latest) of each 12-month period of the additional levy arrangements'. For the fourth period (1987/88), this time-limit is extended to 31 December 1987 and for the seventh period (1990/91) Commission Regulation (EEC) No 2333/90 postpones the deadline until 30 September 1990.

(1) According to the equivalence to be used for calculating the levy applicable to butter deliveries, 1 kg of butter = 22,5 kg of milk — Commission Regulation (EEC) No 1546/88 of 3 June 1988 laying down detailed rules for the application of the additional levy referred to in Article 5c of Regulation (EEC) No 804/68, Article 11, OJ L 139, 4.6.1988, p. 12.

(2) Commission Regulation (EEC) No 1546/88 of 3 June 1988 laying down detailed rules for the application of the additional levy referred to in Article 5c of Regulation (EEC) No 804/68, ninth recital, OJ L 139, 4.6.1988, p. 12.

(3) Council Regulation (EEC) No 857/84, supplemented by Commission Regulation (EEC) No 1371/84 of 16 June 1984 laying down detailed rules for the application of the additional levy referred to in Article 5c of Regulation (EEC) No 804/68, OJ L 132, 18.5.1984, p. 11.

4.39. In the United Kingdom and the Netherlands, the temporary transfer scheme, also called leasing, is used incorrectly. A number of producers who have ceased milk production lease their quota each year to another producer. This practice, against which the Commission initiated infringement proceedings in April 1992, results in producers being kept in work who do not in fact produce milk themselves but just exploit the income generated by the quota system.

4.40. Pursuant to Council Regulation (EEC) No 763/89, the Council may, where necessary, set limits to the temporary transfers, in accordance with the voting procedure provided for in Article 43(2) of the Treaty ⁽⁴⁾. In application of this procedure ⁽⁵⁾, temporary transfers were not permitted for 'SLOM' producers ⁽⁶⁾. In fact, the Council considered that the 'SLOM' quotas had to be subject to certain restrictions because these quotas were not intended to give those to whom they were allocated an undue advantage but to cover the actual production of the 'SLOM' producers.

4.41. With regard to the redistribution of quotas freed as a result of the Community programme for restructuring milk production, which was restricted to 500 000 t and to four Member States (Spain, France, Ireland and Italy), Regulation (EEC) No 1183/90 lays down criteria, which may be adjusted by the Member States, for allocating additional individual reference quantities.

4.42. By virtue of the obligation to tie transfers of quotas to transfers of land, all transfers of quotas have to be monitored by the national authorities in charge of administering the quota system.

4.43. Nevertheless, in some Member States transfers of quotas are made in roundabout ways:

(a) in the Netherlands, the land to which a transfer of quotas has been linked at the time of the transaction

(4) 'The Council shall, on a proposal from the Commission and after consulting the European Parliament, acting unanimously during the first two stages and by a qualified majority thereafter, make regulations, issue directives, or take decisions, without prejudice to any recommendations it may also make'.

(5) Council Regulation (EEC) No 764/89 of 20 March 1989 amending Regulation No 857/84 adopting general rules for the application of the levy referred to in Article 5c of Regulation (EEC) No 804/68 in the milk and milk products sector, OJ L 84, 29.3.1989, p. 2.

(6) See footnote 1 on page 16.

may be ceded back or resold without the quota only one year after its acquisition. The price differential between land with a quota and land without a quota represents a good estimate of the intrinsic value of the quota. Thus, in the past, milk producers have paid, per litre of quota and depending on the region, as much as six times the price they received per litre for their deliveries of milk to dairies. If, in the transaction contract, the value of the quota is indicated separately, the price of acquiring the quotas may even be recouped fiscally by the milk producer within a period of five years;

- (b) in the United Kingdom, the procedure for transferring quotas without land is similar. In the first phase, a farmer merely has to lease or sell part of a farm with an individual reference quantity attached to it. A minimum of ten months later, the land thus sold may, if it has not been used for milk production during this period, be ceded back to the seller or lessor without a quota.

4.44. In order to prevent quotas from being transferred between producers without a corresponding transfer of land, some Member States (including Germany, Ireland and Luxembourg, but not the Netherlands) have, in the case of leasing or selling of land, introduced free transfers of quotas to the national reserve. During the first years of application of the quota system, some Member States withdrew and allocated to the national reserve a substantial part of the quota which was the subject of the transaction (in Germany and Luxembourg up to 80 %, in Belgium up to 90 %). In Ireland, up to 25 % of the quota transferred is made over free of charge to the national reserve in the event of leasing and, until the milk year 1989/90, in the event of sale.

4.45. In order to prevent milk production from being concentrated on very small agricultural areas, i.e. to prevent transfers of quotas from being made without land, several Member States have fixed an upper limit on the individual reference quantity that may be transferred per hectare (5 000 kg/ha in Germany and Luxembourg, 20 000 litres/ha in Belgium). Other Member States, in an effort to reduce the number of quota transfers, have decided not to transfer quotas for land transfers involving less than a set minimum area, for example, five hectares in Luxembourg. In some Member States, in the case of leasing, quota transfers may be made only once a year, whereas in others (e.g. Ireland), such transfers may be made several times a year, but on set dates.

4.46. The variety of administrative measures taken by the different Member States which apply the quota system

effectively shows that the national authorities have, on the one hand, tried to protect themselves against a proliferation of administrative decisions and, on the other, sought to help milk producers to minimize the impact of the quotas themselves and the additional levy payable in the event of the quota being exceeded.

4.47. Redistribution from a national reserve has the effect in most cases of giving the weakest producers in each Member State an advantage by allocating them additional individual reference quantities. Imposing minimum amounts on transfers is tantamount to putting small producers at a disadvantage, whilst imposing maximum amounts is virtually the same as curbing restructuring in favour of the producers with the highest yields.

4.48. With regard to temporary transfers, the implementing measures also differ from one Member State to another:

- (a) in the United Kingdom, any producer may lease his individual reference quantity, except for 5 000 litres which he must keep, to another producer for a period not exceeding the end of the milk year;
- (b) in the Netherlands, the individual reference quantities which may be offered for temporary transfer, solely by the producer to his purchaser for a 12-month period, are limited to an absolute minimum of 10 000 kg and an absolute maximum of 75 000 kg;
- (c) in Belgium, temporary transfers are allowed in so far as individual reference quantities allocated for deliveries are exchanged between producers delivering to the same purchaser provided that the quantities transferred do not exceed 35 000 litres for producers with an individual reference quantity of less than 300 000 litres;
- (d) in Ireland, temporary transfers are limited to a percentage of the individual reference quantity of the producer, who may offer the temporary transfer solely to his purchaser;
- (e) in Germany, temporary transfers have been permitted solely since the milk year 1990/91;
- (f) in Denmark and Luxembourg, no use is made of the possibility of temporary transfers;

(g) in the other Member States, temporary transfers cannot be made because no national implementing provisions have been laid down.

4.49. For each milk year, which begins on 1 April, temporary transfers have to be recorded by 31 July at the latest ⁽¹⁾. In some cases, temporary transfers have, by way of derogation, been definitively recorded as late as December, i.e. three months before the end of the milk year.

4.50. Temporary transfers help farmers to plan their annual milk production properly. This is the case both for the farmer who transfers his individual reference quantity and for the farmer who acquires it temporarily. Conversely, if temporary transfers are not permitted, the unused reference quantities are redistributed according to the *ex post facto* off-setting procedure (see paragraphs 4.17 ff). In this case, producers know in advance that at the end of the milk year they will receive free of charge an addition to their quota which will be allocated to them by way of *ex post facto* off-setting. Thus they have a two-fold advantage: on the one hand, part of the speculative overrun of the initial individual quota is not penalized by the additional levy stipulated by the system and, on the other, this overrun, provided that it is covered by a free quota allocated by way of *ex post facto* off-setting, is very profitable. By contrast, *a priori* temporary transfers against payment require better planning of production. In fact, if there is no *ex post facto* off-setting, any overrun is penalized financially. Furthermore, the profitability of the additional production is reduced by the leasing cost (the cost of the guaranteed income on the quota) paid for the quota which is acquired temporarily. Thus, *a priori* temporary transfers make producers who comply with the rules of the system more responsible for their production and penalize those speculating on *ex post facto* off-setting.

Control measures

Management criteria and the Commission's monitoring of the various measures

4.51. The Community regulations require the Member States to notify to the Commission a whole series of data on the national measures adopted for the application of the system in the Member States, as well as the results in figures of the implementation of the quotas and more specifically of some provisions of the regulations.

⁽¹⁾ Commission Regulation (EEC) No 1546/88 of 3 June 1988 laying down detailed rules for the application of the additional levy referred to in Article 5c of Regulation (EEC) No 804/68, OJ L 139, 4.6.1988, p. 12.

4.52. An examination of the files at the Commission has shown that the Member States do not systematically notify the Commission within the time-limits stipulated either of the national implementing regulations or of the amendments which they have made thereto. As a result, all too often the Commission becomes aware of these regulations only when it comes to clear the accounts, i.e. two years after they first came into force. This being so, the Commission is unable to monitor fully and effectively the way in which the system is being managed in the Member States.

4.53. The Commission has drawn up a form for the Member States designed to obtain information on deliveries and direct sales relating to each milk year which has just ended, as required by Article 19(3) of Regulation (EEC) No 1546/88. In many cases, these notifications arrive at the Commission well after the time-limit of within three months of the end of the milk year: for the milk year 1990/91, only nine Member States had sent the form in by the end of 1991. Some of the forms, moreover, were incomplete. In general, the Member States fail to notify the Commission of cases where Article 6a of the above-mentioned Regulation is applied, of the list of groups of purchasers and/or producers and of the quarterly figures for deliveries and direct sales (Article 19(3), first and third indents, of Regulation (EEC) No 1546/88). Lastly, there is the problem of direct sales, for which the quantities have been communicated by only five Member States. This state of affairs confirms the difficulties experienced by the Member States in exercising control over this aspect of the system, which lends itself to being easily evaded by the producers.

Control measures in the Member States

4.54. According to Commission Regulation (EEC) No 1371/84, replaced by Commission Regulation (EEC) No 1546/88, 'Member States shall adopt whatever additional measures are required:

- (a) to ensure collection of the levy, in particular inspection measures and measures ensuring that interested parties are aware of the penal or administrative sanctions to which they will be subject if they fail to comply with the provisions of this Regulation;
- (b) to deal with cases where milk production is totally or partially discontinued under Article 4(1)(a) of Regulation (EEC) No 857/84, should the provisions thereof be applied'.

4.55. In some Member States (Spain, Greece, Italy), not all the producers have yet been allocated individual reference quantities (see paragraph 4.24), and the lack of checks or the lack of strictness in the supervision and control exercised by the competent agencies of these Member States strip the quota system of all its effectiveness. The systems actually set up by the Member States for checking whether the regulations concerning the common organization of the market in milk and milk products are being complied with differ both in their conception and in their effectiveness:

- (a) in Germany, the fact that powers are dispersed makes checks rather difficult. The control authorities do not systematically crosscheck the various sources of information during the on-the-spot checks. On the basis of the information made available to it by the various bodies, the Court was unable to reconstruct the exact amounts of the milk deliveries to purchasers in Germany, because the data were gathered at different times and for different purposes.

The national auditors also do not check the materiality, i.e. they do not compare the inputs with the finished products, bearing in mind the processing coefficients, in order to ascertain whether, under normal production conditions, the finished products tally with the milk collected. Checks on farmers making direct sales are often difficult to conduct because there are inadequate bookkeeping records. The national auditors do check with those receiving compensation for the definitive discontinuation of milk production that the stipulations of the regulations are being fulfilled;

- (b) in France, deliveries to dairies are not subject to sufficiently thorough scrutiny with regard to the stock accounting or physical crosschecks, which are obviously essential for verifying the actual quantity of milk collected, particularly where the dairies are part of a complex economic structure (for example, a company with subsidiaries in one or more Member States). The system of managing and checking direct sales does not give reasonable assurance of sound financial management in terms of Community rules. Checks on the compensation for the definitive discontinuation of milk production reveal an incomplete national picture. Some 'départements' either do not make any checks or have not replied to the French Ministry of Agriculture's questionnaire about checks. At local level, in one of the three 'départements' visited by the Court, the situation is plainly inadequate;

- (c) in Denmark and the United Kingdom, the checks are generally well established and formalized, well planned and documented and cover all aspects of the quota system. The arrangements include a strict check on the quantities of milk sold and full, speedy collection of the additional levy;

- (d) in Spain, the checks carried out by the SENPA ⁽¹⁾ departments concerning those receiving compensation for the definitive discontinuation of milk production or compensation for the temporary withdrawal of a proportion of the individual reference quantities are not sufficiently effective; out of 110 on-the-spot checks carried out by the SENPA departments, only two cases of irregularities were found. Moreover, only one of the five cases checked by the Court met the conditions for granting the compensation at the time of the audit;

- (e) Ireland has set up a network of regional and local inspectors who are responsible for checking all aspects of milk production. These inspectors check the quality of the milk, the quantities of milk delivered to the purchasers, all forms of transfers, the individual reference quantities, the recipients of the compensation for the discontinuation of milk production and the activities of those selling direct; scrutiny of the checking system has shown that the few direct sellers are seldom checked and even then very belatedly;

- (f) in Belgium, the emphasis of the audit methodology ought to be on assessing the overall transparency of the management of quotas and deliveries, i.e. the auditors ought to concentrate more on evaluating the reliability of the figures which they collect. The auditors who examine the accounts of a large dairy, especially where it is part of a complex economic structure, all ought to receive specialized training; there are insufficient staff to carry out the checks as frequently as required;

- (g) in the Netherlands, the checks on the quota system are, on the whole, satisfactory. This does not, however, apply to the direct sellers to whom a specific reference quantity of less than 25 000 kg has been allocated: they are never checked;

- (h) in Luxembourg, the administrators themselves check the purchasers and direct sellers, but these checks do

⁽¹⁾ SENPA: Servicio Nacional de Productos Agrarios.

not, however, concern materiality, i.e. they do not compare the inputs with the finished products to verify whether, under normal production conditions, the finished products tally with the inputs, bearing in mind the processing coefficients;

- (i) in Italy and Greece, there are no checks on cases of individual reference quantities being exceeded because, at the time of the on-the-spot checks in 1991, the producers had not yet received any quotas.

Specific aid measures and the quota system

4.56. In order to make it easier to cut back milk production, the quota system was supplemented as of 1986 by two special measures, namely compensation for the definitive discontinuation and compensation for the temporary suspension of milk production, which are described in Annex XXIV.

4.57. With regard to the programme of aid for temporary suspension, the scheme, as it stands, may result in a producer who exceeds his quota paying the additional levy due if the Member State to which he belongs has exceeded its quota and at the same time being able to receive the compensation for temporarily discontinuing delivery. Even though the legal structure of the Community regulations allows it, it is not logical for one and the same individual producer to be both obliged to pay a financial penalty and entitled to receive compensation. The Court has, however, found this state of affairs in the Member States visited in the course of auditing individual accounts at the dairies. It also found that the cash funds supplied by the compensation helped some producers in excess of their quotas to pay the levy which was imposed on them. It is thus apparent that in this case the quota system here too loses its effectiveness since the actual financial penalty is in many instances thereby considerably reduced.

Impact of the quota system on the structure of farms

4.58. Contrary to the Council's fears that measures taken to control the increase in milk deliveries could prevent the

structural changes which are required ⁽¹⁾, the milk quota system, supplemented in most Member States by national schemes for the cessation and restructuring of milk production, has not, at the level of individual undertakings, halted progress in the milk production sector.

4.59. In fact, the yield of dairy cows has increased by around 10 %, rising from 4 285 kg of milk per cow per year in 1984 to 4 719 kg in 1990 (see Annex XVII). It should be noted that the increase in yield has been highest in those Member States which had previously shown good results, such as Denmark (6 162 kg per cow), the Netherlands (5 998 kg per cow) and France (4 885 kg per cow). These very Member States have, moreover, always been the Community's main exporters of milk products.

4.60. The Court has also found that the quality of the milk has improved given that, since the introduction of the system, the fat content of the milk has increased (see paragraph 4.34).

4.61. Furthermore, since the introduction of the quota system, structural changes in the milk production sector have speeded up: the number of dairy farms has dropped from 1 621 261 in 1983 to 1 241 627 in 1987 (EUR-10), i.e. a fall of 23,4 % in four years, whereas between 1979 and 1983 the decrease was only 14,7 %. This reduction in the number of holdings was facilitated in particular by the introduction of the Community scheme of aid for the definitive discontinuation of milk production and by the many national restructuring schemes which have accompanied the implementation of the Community scheme for controlling milk production.

4.62. It should be noted that, whereas up until 1985 this process involved a reduction in the number of dairy farms with fewer than 30 cows and an increase in the farms with more than 30 cows, between 1985 and 1987 it consisted of a decrease in all classes of farms, including those with more than 100 cows (down by 10 %). Most of the Member States with high milk production have laid down rules for the transfer of quotas to the national reserve which are unfavourable to big farms, a fact that has contributed to the drop in the number of large farms. When individual

⁽¹⁾ Council Regulation (EEC) No 856/84 of 31 March 1984 amending Regulation (EEC) No 804/68 on the common organization of the market in milk and milk products, eleventh recital, OJ L 90, 1.4.1984, p. 10.

reference quantities are transferred (sale or leasing of land), large farms are obliged to transfer to a national reserve a bigger proportion of the individual reference quantities purchased or leased than small producers (see paragraph 4.44). Furthermore, large farms are not allowed to receive additional quotas taken from the national reserve.

4.63. The discontinuation aid introduced in 1986, as applied in most Member States, was in fact a scheme for social purposes which allowed many elderly small producers, some of whom were already retired, to receive an extra pension. In Ireland, many small producers, even elderly ones, who received the compensation for the definitive discontinuation of milk production, converted their few dairy cows into breeding cattle and thus received both their discontinuation compensation and the premium for suckler cows, plus, where appropriate, the premium for male bovines.

Review of the budgetary situation

4.64. Overall, since 1984, the quota system together with the aid schemes for the definitive discontinuation and temporary suspension of milk production have involved additional expenditure of 2 784,5 Mio ECU for the Community budget and have earned an extra 920,3 Mio ECU in the form of the additional levy. Leaving aside the expenditure committed by the Member States and the costs not identified in the Community budget, the reduction in annual milk production by about eight million tonnes has cost 1 803,8 Mio ECU up until 1991, i.e. about 225 ECU per tonne, compared with the target price for the milk year 1991/92 of 268,1 ECU per tonne. The final cost of this reduction must, however, be increased by the cost of the aid measures to be paid until 1993. If, in addition, account is taken of the adjustment for the increase in the average fat content, then production has been cut by only 4,2 million tonnes (without taking into account the corresponding production of skimmed-milk powder) and the cost of the aid measures per tonne of milk not produced is twice as high. It should be remembered that the reduction in milk production has contributed, particularly by way of the decrease in the number of dairy cows, to the production surpluses found on the beef market where intervention spending has risen considerably over the past few years.

4.65. The revenue deriving from the additional levy peaked in 1989 at 466,5 Mio ECU, following a large overrun of the total quantities available for the fifth milk year (1988/89). It fell to 60,4 Mio ECU in 1991. This downward trend in the additional levy, combined with an increase of about 500 000 t in deliveries compared with the

milk year 1988/89, can for the most part be attributed to the following factors:

- (a) the increase of 502 200 t in the total Community quantity for the benefit of producers who had made an undertaking pursuant to Council Regulation (EEC) No 1078/77 of 17 May 1977 introducing up a system of premiums for the non-marketing of milk and milk products and for the conversion of dairy herds and who, having initially been excluded from the allocation of individual quotas, were granted such a right by the Court of Justice in 1988. The amendments made as a consequence by Council Regulation (EEC) No 764/89 of 20 March 1989 ⁽¹⁾ and by Council Regulation (EEC) No 1639/91 of 13 June 1991 ⁽²⁾ for the benefit of the producers better known as the 'SLOM' producers thus result in the usable quotas in the Community being increased. The Court of Justice's abolition (Judgments of 11 December 1990) of some of this Regulation's restrictive provisions has meant that the individual quotas of the interested parties have been increased still further;
- (b) the effects of the 'Nallet package' regulations, which result in an increase in the guaranteed total quantity actually available ⁽³⁾ of some 1,0 million tonnes;
- (c) the granting to Germany in 1990 of a 'rebate' of 113,7 Mio ECU in respect of expenditure incurred under a scheme to buy up reference quantities, following the clearance of the accounts for the financial year 1987 (see the Court's Annual Report concerning the financial year 1990, paragraphs 3.23 — 3.24) ⁽⁴⁾.

5. CONCLUSION

The reduction in milk production and its inadequacy

5.1. Consumption of milk and milk products in the Community has been declining since 1987. In 1990, it stood

⁽¹⁾ OJ L 84, 29.3.1989, p. 2.

⁽²⁾ OJ L 150, 15.6.1991, p. 35.

⁽³⁾ The quantity available is understood here as the total Community quantity minus the quantities temporarily withdrawn.

⁽⁴⁾ Annual Report concerning the financial year 1990 together with the institutions' replies, OJ C 324, 13.12.1991, p. 59.

at about 91 million tonnes, whereas the volume of marketed production continued to stand at around 102 million tonnes. This imbalance between production and consumption is all the more worrying in that consumption is already being supported by large subsidized sales of butter and skimmed-milk powder. Indeed, more than 20 % of production is disposed of within the Community by means of a battery of measures to support butter and above all milk powder and about 10 % is exported with the aid of export refunds. Community exports, which represent almost 50 % of the world market, are not easy to keep up, since they require the Community to continue fixing high rates of refunds. With imports being of marginal significance and exports offering little prospect of any increase in the short term of additional disposal outlets, the fact must be faced that it is very difficult to find new solvent outlets outside the Community for the Community's surplus milk production.

5.2. Nevertheless, it should be noted that, since 1984, milk production has been moving towards the desired state of equilibrium between the production and consumption of milk products. Indeed, the quota system, supplemented by heavy penalties in the case of overruns in the form of the additional levy and by measures to encourage the discontinuation of milk production, had led to an 8,2 % reduction in milk production between 1983 and 1990 (see paragraph 2.12). This reduction is, however, less effective than it seems in terms of budgetary costs in so far as the fat content of milk in the Community has increased by about 4 % (see paragraph 4.34).

5.3. Initially fixed at too high a level, the quotas have subsequently been cut a number of times. These successive reductions have been accompanied by measures which have resulted in an extra burden on the budget: Community schemes to assist the definitive discontinuation, applied in very different ways in the various Member States, or the temporary discontinuation of milk production, to say nothing of the practice in some Member States of reinvesting part of the additional levy in national programmes to buy up individual reference quantities (see Annex XXV). The reductions which have thus been made have in part been cancelled out by the increases in quotas decided by the Council following the judgments handed down by the Court of Justice in favour of the 'SLOM' producers and as part of the 'Nallet package' measures (1).

5.4. The Community discontinuation aid introduced in 1986, as applied in most Member States, was in fact a

scheme for social purposes which allowed many elderly small producers, some of whom were already retired, to receive an extra pension.

5.5. These aid measures, which have been charged to the Community budget since 1987, amount to 2 096,2 Mio ECU. Since the programme for these aid measures covers a period of seven years, the expenditure to be paid until 1993 should also be added. The amount of compensation paid for the reduction of milk production has, depending on the scheme, varied between 45 and 100 ECU per tonne of milk production eliminated (2). Since 1984, the additional levy has earned the Community budget 920,3 Mio ECU.

5.6. Despite the slight improvement in the market's imbalance, the reduction in milk production is insufficient. For these reasons, the Court considers that the reduction in guaranteed total quantities ought to be continued, even though the quantities of butter and skimmed-milk powder in public stocks are limited (see paragraphs 2.31 ff), giving the appearance of a rough balance on the market. The reduction in the guaranteed total quantities could be of less significance if the relaxation of the quota system were to be reversed and if there were to be a crack-down on those Member States which fail to apply the quota system or apply it inadequately.

Weakening of the producer's responsibility

5.7. The Community regulations intended to control milk production have developed in such a way that they have weakened the direct responsibility of individual producers in the event of the individual reference quantity being exceeded and, by contrast, increased the national responsibility of the Member States, which, at the risk of having to make most of the producers who exceed their quota pay the additional levy, are obliged to ensure that their guaranteed total quantity is kept to. The off-setting mechanism, the transfers of total quantities guaranteed for direct sales to those guaranteed for deliveries, and the average reference fat content are the most striking examples of this.

National off-setting

5.8. The off-setting mechanism, initially introduced solely for the milk year 1984/85, entitles a Member State to

(2) Compensation for the definitive discontinuation of milk production:
 — application of Regulation (EEC) No 857/84 (Article 4(1)(a)): 45 ECU/t
 — application of Regulation (EEC) No 1336/86: 60 ECU/t
 — application of Regulation (EEC) No 1637/91 temporary suspension: 75 ECU/t
 reduction of reference quantities: 100 ECU/t.

(1) See footnote 1 on page 15.

use up all its guaranteed total quantity in accordance with its own priorities. This mechanism, which has been maintained throughout the period of application of the quota system, makes it possible to withdraw penalties, at least in part, from producers who have exceeded their individual reference quantity and to dilute the penalty to be imposed on them in the form of the additional levy (see paragraph 4.17). The penalty may be watered down even more in cases where the same producer receives compensation for the temporary withdrawal of a proportion of his individual reference quantity (see paragraph 4.57). The Court considers that in the event of an overrun of an individual quota, the milk producer ought to be refused, up to an amount equivalent to the overrun, any premiums or compensation paid by way of recompense for the reduction in his production.

5.9. The Court considers that the off-setting mechanism, if it is not abolished, could be replaced by the application in all the Member States of a more liberal system of *a priori* temporary transfers of quotas, as off-setting at the end of the year encourages many producers to exceed the individual quota allocated to them at the beginning of the milk year (see paragraph 4.50).

National transfers between deliveries and direct sales

5.10. In all the Member States, direct sales are a very weak point in the quota system. From the outset there was little information on them, and on every possible occasion they have been used to cushion the impact of the additional levy (see paragraph 4.22), at both individual and national level. If the guaranteed total quantity for direct sales is not used up, the amount remaining is transferred by some Member States — all too often without any basis in terms of formal requests by the producers concerned — to the guaranteed total quantity for deliveries in order to minimize the additional levy (see Annex XXIII). Because direct sales account for a relatively small proportion of milk production (see paragraph 2.13), the Member States have in general neglected monitoring of them, all the more so since the checks needed are often difficult to carry out. Even after eight years of application of the quota system, data on direct sales are still not gathered by means of producer declarations in all the Member States. The Court considers that the Commission ought to make sure that the Member States carry out properly the checks needed to verify compliance with the individual quotas allocated for direct sales and that it should, at the latest during the clearance of accounts procedure, refuse to allow the transfers in question where the latter are made improperly.

Inadequate deterrent of the adjustment of deliveries or direct sales depending on the fat content

5.11. The penalty imposed in the event of the reference fat content being exceeded lacks dissuasive effect. The Court has found that, in many Member States, the overrun of the guaranteed total quantities is a result of the quantitative adjustments calculated on the basis of the overrun of the reference fat content. In terms of milk equivalent, the increase in the fat content is equal, according to the formulae laid down by the Commission, to a production of 178 000 tonnes of butter, i.e. two thirds of the butter surplus produced in 1990. Thus, in respect of some milk products sold for final consumption, such as butter, the quantitative reduction in milk production since 1984 has to a large extent been cancelled out by the increase in the fat content, since fat is, in particular, processed into butter, which ultimately swells Community stocks.

5.12. The Court considers that it would be expedient to increase the penalty imposed on milk producers who exceed the reference fat content in order to curb in particular the surplus butter production which results from this.

The financial advantage to traders of delaying payment of the additional levy

5.13. In almost all the Member States, the delays in collecting the additional levy have become longer and longer. Most of the Member States have failed to implement the usual appropriate recovery procedures for collecting national taxes (see paragraph 4.27). Since delays in payment are not penalized by any interest on late payments, producers liable for an additional levy have every interest in postponing payment for as long as possible. It is therefore essential for the Community to introduce interest on late payments calculated on the whole period of arrears, as exists for the co-responsibility levy in the cereals sector.

Disparate applications

5.14. The Member States take advantage of the flexibility of the Community regulations by applying the measures for controlling milk production in different ways. The national

variations in the way in which the measures are applied have two consequences: firstly, milk producers are treated differently from one Member State to another by the same Community programme or measure and, secondly, the large number of variants in the implementation singularly complicates the management, assessment, supervision and monitoring of the Community programmes and measures without ensuring a better result. On the contrary, in some cases the national variants serve more to skirt round the Community objectives than to achieve them. In certain Member States, the delay in implementing the system, the lack of control or the lack of strictness in the supervision and checks carried out by the competent agencies of these Member States strip the quota system of all effectiveness. In practice, these Member States thus allow national production to increase and, arguing that national production falls short of domestic demand, they even submit requests to the Community for their guaranteed total quantity to be increased ⁽¹⁾. It is up to the Commission to step up its monitoring of the implementing rules and to propose amendments to the regulations, if need be, in order to prevent Community objectives from being indirectly jeopardized.

5.15. Whereas the Member States with high milk production apply the quota system, albeit with some flexibility, in some other Member States (Spain, Greece, Italy), by contrast, the quota system is applied only in a fragmentary fashion. Apart from the Court of Justice's sentencing of Italy in 1987 (Case C-394/85), prior to 1992 the Commission failed to take all the necessary action to achieve the correct application of the quota system in Spain, Greece and Italy. Eight years after the introduction of the quota system, it is essential that the Commission finally takes all the measures needed to ensure that the Community quota system is applied fully in all the Member States.

Complexity of the measures

5.16. The large number of Community measures applied 'à la carte' in all their various forms by the Member States is only the tip of the iceberg as far as the complexity of the measures for controlling milk production is concerned. The numerous appeals lodged with the national courts and with the Court of Justice of the European Communities bear witness to the difficulties of application experienced in the Member States (see paragraph 4.11). The Commission ought to consolidate the regulations adopted to date, whilst

at the same time simplifying the management rules, particularly in the field of transfers of quotas.

The risks and hazards of setting quotas for production

5.17. As the Court has already found elsewhere, some of the objectives of the common agricultural policy (rational development of agricultural production, reasonable prices for consumers) have not been achieved in the common organization of the market in milk and milk products either. Since the introduction of the quota system, the common organization of the market has moved towards a fairly coordinated organization of the national markets in the Member States. Regional specialization within the Community, the main objective of which is to ensure the rational development of production and to channel it towards the most favourable regions, has been blocked by the allocation of guaranteed total quantities to each Member State. The resultant failure to use resources at Community level in the best possible manner has on the one hand been perpetuated by the rules applicable to transfers of quotas, which exclude transfers between farmers from different Member States, and on the other been aggravated by the granting of generous quotas particularly in Portugal, where the natural conditions are less favourable to milk production than in some regions further north in the Community, but also by the faulty or ineffective application of the quota system in Spain, Italy and Greece (see paragraph 4.6). The Court takes the view that consideration should be given to setting up a regulated market in transfers of quotas and to the possibility of authorizing transfers of quotas between farmers of different Member States.

5.18. The quota system, an economic system that is more restrictive than the co-responsibility levy (see paragraph 3.14), the rate of which was never high enough to have any marked influence on milk producers' behaviour, also has other disadvantages inherent in any system of quotas. Any quota system tends to be self-perpetuating because of the economic benefits which it brings the recipient producers and which shelter the latter from market pressures to improve their profitability. As a consequence, the production structures tend to remain unchanged. In order to prevent these drawbacks, schemes to restructure milk production have been set up in almost all the Member States. A further disadvantage of quota systems is the following phenomenon: the problem of surpluses, having been solved for one product, tends to migrate to another product. The production capacity available by virtue of the decrease in milk production may be used for another agricultural product. This possibility is illustrated by the problems currently being encountered in the beef sector, as the Court pointed in its Annual Report

⁽¹⁾ See footnote 1 on page 6.

on the implementation of the budget for the financial year 1991 ⁽¹⁾.

The quota system and farming structures

5.19. In some Member States, the restructuring of milk production has been heavily biased in favour of small and medium-sized producers by means of a set of national schemes for buying-up quotas and restructuring dairy farms. In other Member States, restructuring has been carried out through a quota market which is not explicitly prohibited by Community regulations, but which favours those producing the most (see paragraph 4.14).

5.20. The penalties imposed on milk producers at the time of transfers of quotas are an essential feature of the Member States' restructuring policies. Upon buying a quota linked to the purchase of agricultural land, producers have to transfer free of charge to the national reserve part of the individual reference quantity linked to the agricultural land which has been the subject of the transaction involving payment. In some Member States, these transfer penalties are so high as to impede the development of the big producers (see paragraph 4.44).

5.21. In order to avoid structural changes of a kind that might eventually have an adverse effect on the common organization of the market, the Commission ought to explore the possibility of introducing a standard system for all the Member States.

This report was adopted by the Court of Auditors in Luxembourg at its meeting of 26 May 1993.

For the Court of Auditors

André J. MIDDELHOEK

President

⁽¹⁾ OJ C 330, 15.12.1992.

ANNEX I

Table 1 — Budgetary revenue and expenditure of the common organization of the market in milk and milk products

	<i>Mio ECU</i>								
	1983	1984	1985	1986	1987	1988	1989	1990	1991
Export refunds ⁽¹⁾	1 326,8	1 943,4	2 028,2	2 154,9	2 427,2	3 082,4	2 922,3	1 945,8	2 249,0
Storage costs	1 099,0	1 710,4	1 972,8	1 497,6	1 027,1	1 095,9	1 445,4	1 878,0	1 081,2
Aid for price off-setting	2 281,4	2 475,1	2 440,1	2 356,7	2 235,4	2 052,4	1 661,3	1 637,3	1 970,5
Total disposal costs	4 707,2	6 128,9	6 441,1	6 009,2	5 689,7	6 230,7	6 029,0	5 461,1	6 168,2
Discontinuation compensation					71,0	200,0	212,2	173,5	255,4
Suspension compensation						394,8	563,6	481,1	432,9
Other expenditure	216,3	166,5	129,5	113,7	23,0				
Total expenditure	4 923,5	6 295,4	6 570,6	6 122,9	5 783,7	6 825,5	6 804,8	6 115,7	6 786,3

	<i>Mio ECU</i>								
	1983	1984	1985	1986	1987	1988	1989	1990	1991
Linear levy	527,4	699,7	639,4	551,6	447,6	487,3	423,7	313,7	292,0
Additional levy		49,5	2,1	165,5	153,7	48,3	466,5	34,7	60,4
Total levies	527,4	749,2	637,3	717,1	601,3	535,6	890,2	348,4	352,4

	<i>percentage</i>								
	1983	1984	1985	1986	1987	1988	1989	1990	1991
Levies/disposal costs	11,2	12,2	9,9	11,9	10,6	8,6	14,8	6,4	6,6
Levies/total expenditure	10,7	11,9	9,7	11,7	10,4	7,8	13,1	5,7	5,2

Source: Revenue and expenditure accounts.

⁽¹⁾ including food aid.

ANNEX II

Table 2 — Compensation for the definitive discontinuation of milk production
(Regulation (EEC) No 1336/86 — Article 2(1), 2nd subparagraph)

Mio ECU

Member State	1987		1988		1989		1990		1991	
	(1) Maximum amount payable	(2) Expenditure	(1) Maximum amount payable	(2) Expenditure	(1) Maximum amount payable	(2) Expenditure	(1) Maximum amount payable	(2) Expenditure	(1) Maximum amount payable	(2) Expenditure
Belgium	2,889	2,906	7,944	7,423	6,498	6,088	6,498	6,163	6,498	6,136
Denmark	3,906	4,287	10,743	10,621	8,789	10,285	8,789	9,674	8,789	9,514
Germany	18,842	21,871	51,817	60,469	42,395	49,042	42,395	50,058	(3) 42,395	134,161
Spain	0,466		1,283	12,701	1,049	14,076	1,049	11,207	1,049	10,808
Greece	4,320		11,880		9,720		9,720	—	9,720	0,591
France	21,206	22,427	58,318	60,559	47,714	49,092	47,714	50,352	47,714	50,016
Ireland	4,237	4,116	11,651	9,966	9,533	10,085	9,533	12,588	9,533	10,121
Italy	7,931		21,811		17,845		17,845	—	17,845	—
Luxembourg	0,213	0,234	0,285	0,639	0,179	0,520	0,179	0,536	0,179	0,534
Netherlands	9,659	3,757	26,563	4,668	21,733	45,277	21,733	8,670	21,733	7,910
United Kingdom	12,580	11,360	34,595	32,959	28,305	27,727	28,305	24,237	28,305	25,630
Total	86,250	70,958	236,889	200,005	193,762	212,192	193,762	173,485	193,762	255,421

(1) This column shows the maximum amount that may be paid to the recipients in the course of the financial year.
The Ecu/national conversion rate is the green rate.

(2) This column shows the amount of expenditure incurred during the financial year. The Ecu/national currency conversion rate is the budgetary rate.

(3) Pursuant to Annex VI to Regulation (EEC) No 3577/90, Germany is authorized to pay producers in the territory of the former German Democratic Republic compensation of a single amount not exceeding 42 ECU per 100 kg.
Source: Regulation (EEC) No 776/87, Regulation (EEC) No 1336/86, Regulation (EEC) No 3577/90 — EAGGF financial reports.

ANNEX III

Table 3 — Situation regarding definitive transfers of guaranteed total quantities for direct sales to those guaranteed for deliveries

(in 1 000 tonnes)

	1985	1986	1987	1988	1989	1990	1991	TOTAL
Belgium	25	30	50	4,34	2,851			112,191
Denmark								
Germany		175		33				208,000
Greece			70			40		110,000
Spain			50			150		200,000
France		169	140	100				409,000
Ireland								
Italy	475						350	825,000
Luxembourg								
Netherlands		50						50,000
United Kingdom		2,574						2,574
Total	500	426,574	310	137,34	2,851	190	350	1 916,765
Deliveries	99 917	99 471,6	104 431,6	98 731,6	96 105,7	97 676,6	97 514,7	

* For the purpose of comparison, the last line shows the guaranteed total quantities for deliveries in thousands of tonnes.

Source: Commission.

ANNEX IV

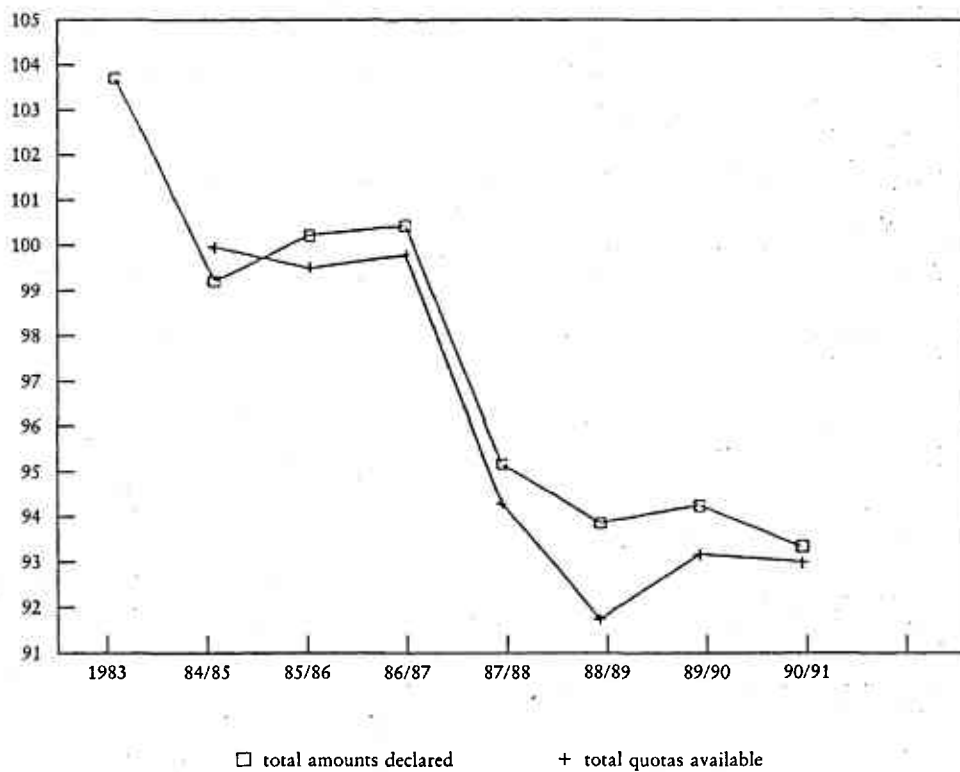
Table 4 — Situation by Member State — Milk deliveries and guaranteed total quantities

		(*1000t)							
		1983	84/85	85/86	86/87	87/88	88/89	89/90	90/91
B	Dec	3 263	3 071,3	3 223	3 256	3 153,3	3 141,4	3 155,4	3 167,4
	Qta	—	3 163	3 161	3 211	3 022,7	2 945,3	2 982,9	2 982,9
DK	Dec	5 226,8	4 912,3	4 884	4 881,8	4 603,1	4 514,2	4 551	4 546,5
	Qta	—	4 932	4 882	4 882	4 589,1	4 467	4 523,9	4 523,9
D	Dec	25 175,8	23 466	23 719	23 981	21 807,4	21 950,7	22 073,8	21 871,3
	Qta	—	23 487	23 423	23 423	22 050,6	21 465	21 834,3	21 834,3
EL	Dec	433,8	440	450	460	490	496	545,9	562
	Qta	—	472	467	537	504,8	491,4	536,7	536,7
ES	Dec	—	—	—	4 639	4 467,9	4 353,9	4 504	4 503,5
	Qta	—	—	—	4 650	4 522	4 354,8	4 551,3	4 551,3
FR	Dec	26 050	25 541,9	25 699,5	25 612	24 632,7	24 042,6	24 123,3	24 011
	Qta	—	25 585	25 494	25 634	24 196	23 555,1	23 865,1	23 865,1
IRL	Dec	5 341,1	5 584,5	5 586,5	5 533	5 280,4	5 173,7	5 286,8	5 288,7
	Qta	—	5 583	5 583	5 583	5 266,2	5 134,2	5 285,9	5 285,9
I	Dec	8 223,4	8 485,6	8 652	8 759,6	8 868,1	8 617,7	8 543,3	8 233,8
	Qta	—	8 798	8 798	8 798	8 600,6	8 373,1	8 300	8 488,2
L	Dec	281,1	291,1	294,2	290,8	279,7	273,5	275,9	280,6
	Qta	—	293	290	290	274,1	267,5	270,8	270,8
NL	Dec	12 881,1	12 195	12 259	12 274	11 398	11 211	11 203	11 209
	Qta	—	12 052	11 979	11 979	11 260,3	10 960,8	11 120,7	11 120,7
UK	Dec	16 800,5	15 305,0	15 405,6	15 505	14 629	14 254	14 461	14 481
	Qta	—	15 552	15 394,6	15 394,6	14 474,8	14 091,6	14 405,1	14 405,1
EUR 10 Total dec		103 676,6	99 293,4	100 172,9	100 553,2	95 141,7	93 674,8	94 219,4	93 651,3
EUR 11 Total dec			99 293,4	100 172,9	105 192	99 609,6	98 028,3	98 723,4	98 154,8
EUR 10 Total quota			99 917	98 471,6	99 731,6	94 239	91 751	93 125,4	93 313,6
EUR 11 Total quota			99 917	99 471,6	104 381,6	98 761,0	96 105,7	97 676,7	97 864,9

N.B. Purchasers and producers involved in direct sales are obliged (see Regulation (EEC) No 1546/88, Articles 15 and 16) at the end of each milk year to transmit to the competent agency of the Member State a statement indicating the quantities of milk or milk equivalent delivered or sold.
 Dec: amounts declared, adjusted for the fat content
 Qta: quota or guaranteed total quantity finally available for each Member State.

ANNEX V

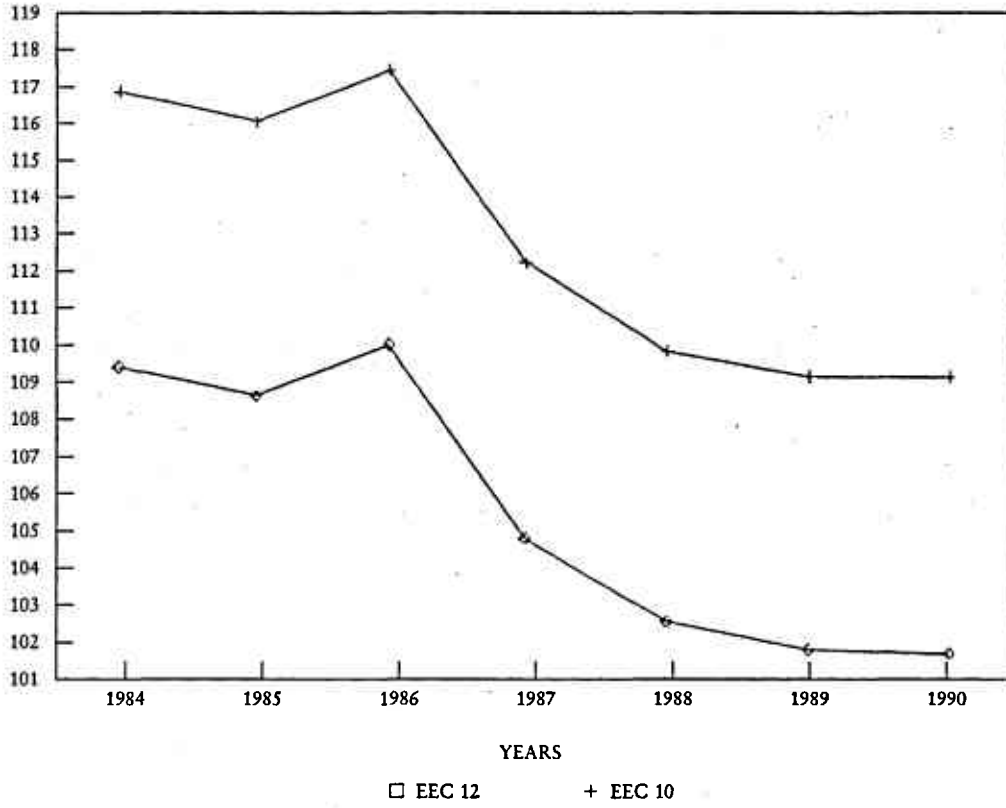
Graph 1 — Deliveries of milk and guaranteed total quantities (in millions of tonnes)



Source: Eurostat-Cronos.

ANNEX VI

Graph 2 — Community milk production (in millions of tonnes)



Source: Eurostat-Cronos.

ANNEX VII

Table 5 — Distribution of the Community reserve between the Member States
(Art. 5c(4) of Regulation (EEC) No 804/68 as amended by Regulation (EEC) No 856/84)

QUOTA	1984/85	1985/86	1986/87	1987/88	1988/89	1989/90	1990/91	1991/92
Belgium								
Denmark								
Germany								
Greece								
Spain					50 000	50 000	50 000	50 000
France								
Ireland	303 000	303 000	303 000	303 000	303 000	303 000	303 000	303 000
Italy								
Luxembourg	25 000	25 000	25 000	25 000	25 000	25 000	25 000	25 000
Netherlands								
Portugal								
United Kingdom	65 000	65 000	65 000	65 000	65 000	65 000	65 000	65 000
Total	393 000	393 000	393 000	393 000	443 000	443 000	443 000	443 000

Distribution:

Commission Regulation (EEC) No 1371/84 of 16.5.1984 laying down detailed rules for the application of the additional levy referred to in Article 5c of Regulation (EEC) No 804/68

Commission Regulation (EEC) No 1546/88 of 3.6.1988 laying down detailed rules for the application of the additional levy referred to in Article 5c of Regulation (EEC) No 804/68

Commission Regulation (EEC) No 1033/89 of 20.4.1989 amending Commission Regulation (EEC) No 1546/88 of 3.6.1988 laying down detailed rules for the application of the additional levy referred to in Article 5c of Regulation (EEC) No 804/68

Commission Regulation (EEC) No 2061/91 of 12.7.1991 amending Commission Regulation (EEC) No 1546/88 of 3.6.1988 laying down detailed rules for the application of the additional levy referred to in Article 5c of Regulation (EEC) No 804/68

ANNEX VIII

Table 6 — Changes in prices

ECU/100 kg (green rate)

Milk year	1984/85	1985/86	1986/87	1987/88	1988/89	1989/90	1990/91	1991/92
Target price for milk (3,7 % fat)	27,43	27,84	27,84	27,84	27,84	27,84	26,81	26,81

Intervention price

Butter	319,70	313,2	313,2	313,2	313,2	300,80	292,78	292,78
Skimmed-milk powder	165,88	174,04	174,04	174,04	174,04	174,04	172,43	172,43
Grana Padanocheese 30-60 days	381,75	388,93	388,93	388,93	388,93	388,93	379,67	379,67
Grana Padanocheese 6 months	472,75	480,33	480,33	480,33	480,33	480,33	470,43	470,43
Parmigiano Reggiano 6 months	521,61	529,19	529,19	529,19	529,19	529,19	519,21	519,21

Threshold price

Butter (fat = 82 %)	358,09	351,0	351,0	351,0	351,0	343,5	328,43	328,43
Skimmed-milk powder (fat < 1,5 %)	186,42	195,57	195,57	195,57	195,57	198,93	193,76	193,76

Levy

Formula A	20,57	20,88	20,88	27,84	27,84	27,84	30,83	30,83
Formula B	27,43	27,84	27,84	27,84	27,84	27,84	30,83	30,83
Direct sales	20,57	20,88	20,88	20,88	20,88	20,88	20,11	20,11

ANNEX IX

Table 7 — On-farm own consumption

(Mio t)

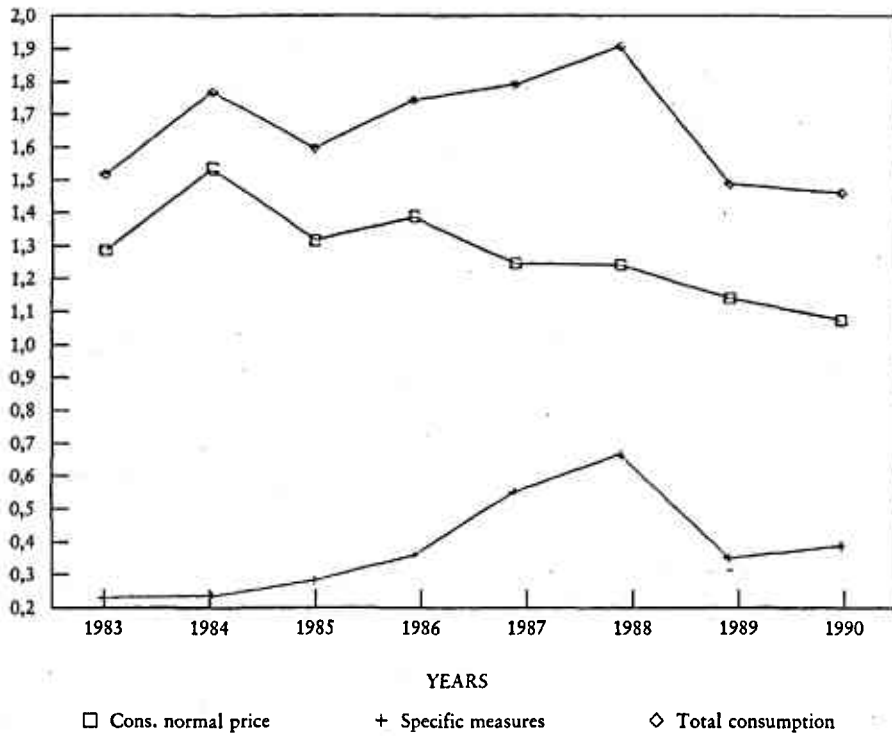
EUR 11	1985	1990
Total production	114,810	107,410
Deliveries	104,794	97,211
Ratio deliveries/total production	91,3 %	90,6 %
Direct sales *	3,962	3,000
Ratio direct sales/Total production	3,5 %	2,8 %
Own consumption/total production	5,2 %	6,6 %
Own consumption, of which animal feed	5,970 5,425	7,089 6,430

* Where no amounts were declared, the quota — also called the individual reference quantity — was used as a basis for the calculations.

N.B. Purchasers and producers involved in direct sales are obliged (see Regulation (EEC) No 1546/88, Articles 15 and 16) at the end of each milk year to transmit to the competent agency of the Member State a statement indicating the quantities of milk or milk equivalent delivered or sold.

ANNEX X

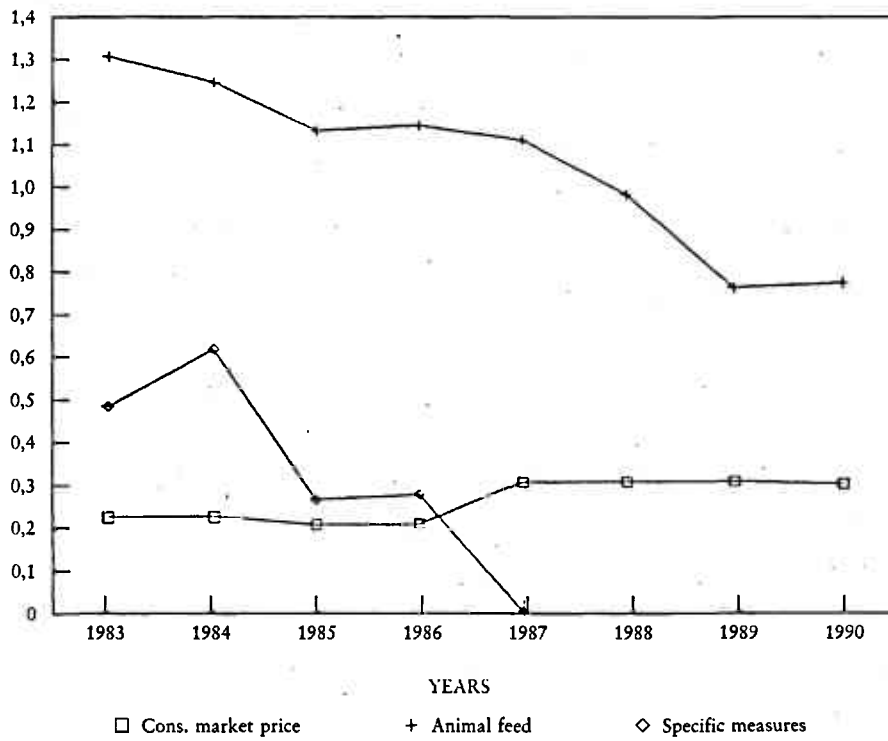
Graph 3 — Butter consumption in the Community (in millions of tonnes)



Source: Commission.

ANNEX XI

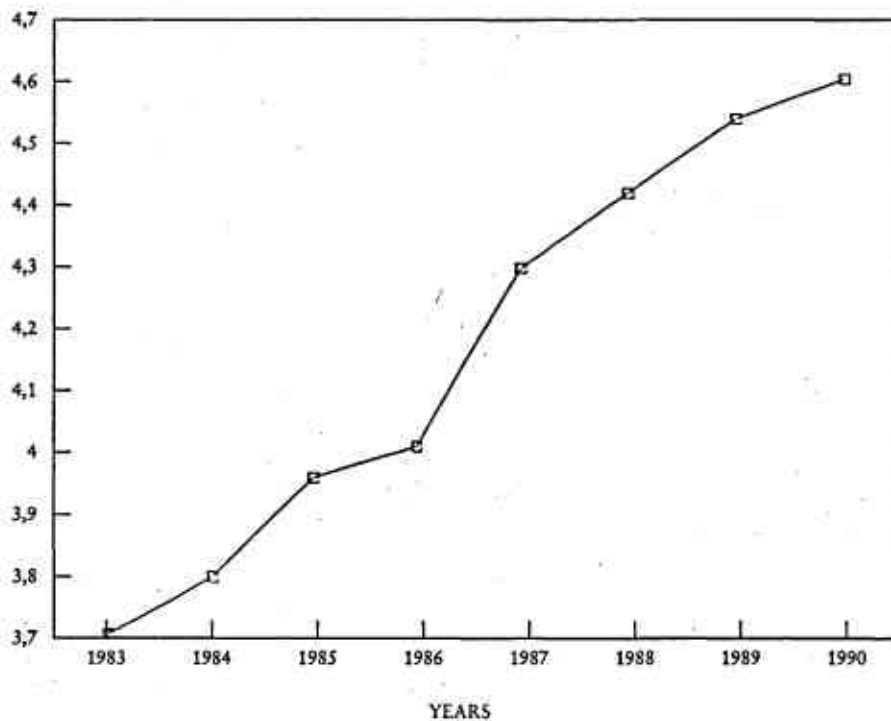
Graph 4 — Consumption of skimmed-milk powder in the Community (in millions of tonnes)



Source: Commission.

ANNEX XII

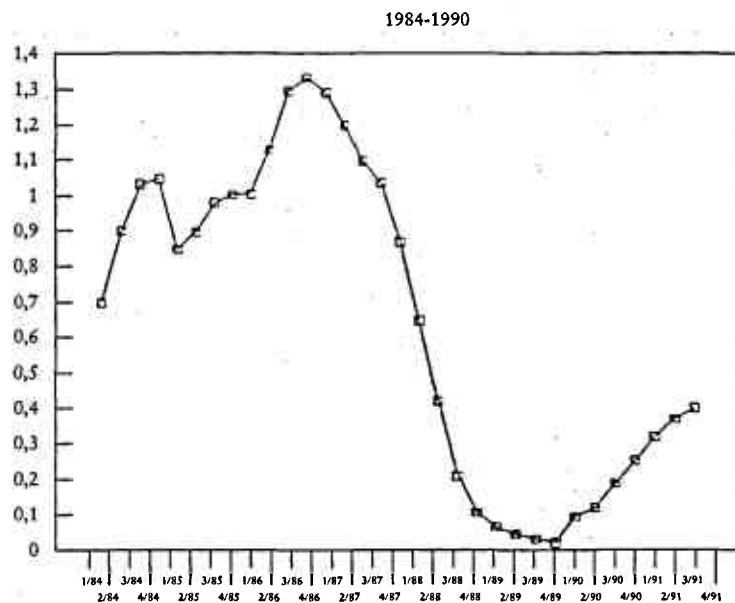
Graph 5 — Cheese consumption in the Community (in millions of tonnes)



Source: Eurostat.

ANNEX XIII

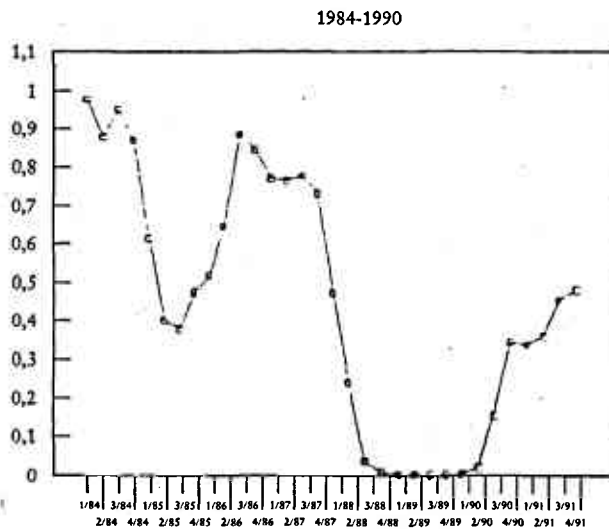
Graph 6 — Public stocks of butter in the Community (in millions of tonnes)



Source: Commission.

ANNEX XIV

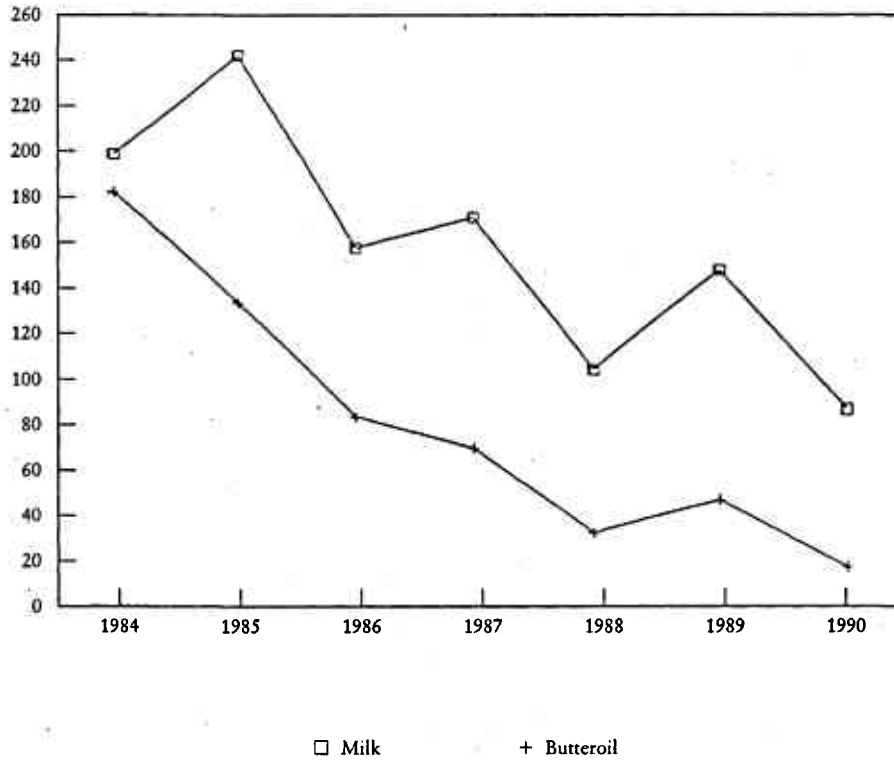
Graph 7 — Stocks of skimmed-milk powder in the Community (in millions of tonnes)



Source: Commission.

ANNEX XV

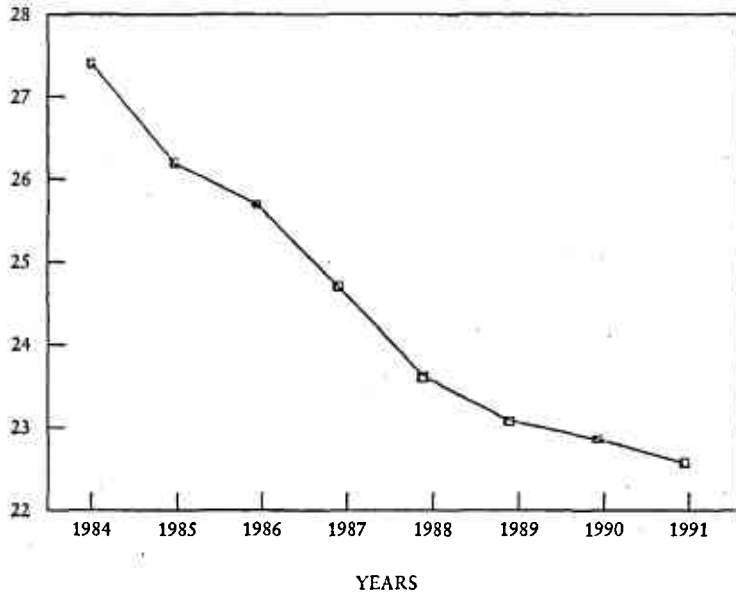
Graph 8 — Food aid (in Mio ECU)



Source: Revenue and expenditure accounts 1984-90.

ANNEXE XVI

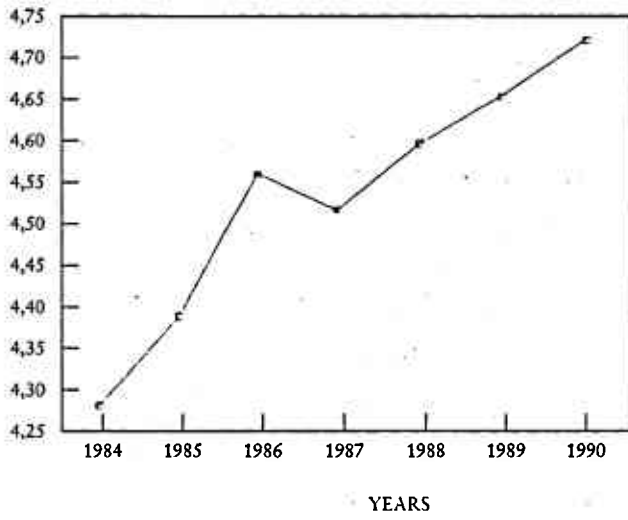
Graph 9 — Changes in dairy cattle herds (in millions)



Source: Eurostat-Cronos.

ANNEX XVII

Graph 10 — Changes in the yield of dairy cows (in tonnes per cow)



Source: Eurostat-Cronos.

ANNEX XVIII

Table 8 — Milk production as a percentage of agricultural production

Country	1984	1985	1986	1987	1988	1989	1990	1991
Belgium	16,00	16,60	17,20	17,20	17,00	16,70	15,10	13,90
Denmark	22,30	22,80	24,10	23,60	24,50	23,80	24,40	23,30
Germany	25,40	25,70	27,10	26,00	26,60	26,70	25,30	24,30
Greece	8,50	9,20	9,30	9,30	9,40	9,40	9,70	8,50
Spain	0,00	9,50	9,50	7,70	7,90	7,90	9,10	7,20
France	17,20	17,20	17,60	17,20	16,70	15,50	15,70	15,30
Ireland	32,40	35,40	35,40	34,60	33,50	35,40	32,40	31,70
Italy	11,80	11,90	11,60	11,60	11,80	11,50	11,80	10,90
Luxembourg	45,20	46,30	46,50	48,80	48,10	46,70	48,70	47,30
Netherlands	26,50	26,40	26,70	26,10	26,20	24,10	21,70	21,10
Portugal					12,80	12,10	12,00	11,80
United Kingdom	19,80	21,50	22,00	21,00	21,20	21,80	21,30	21,20
EEC	18,80	19,20	19,50	17,80	17,60	18,50	18,10	15,80

Source: The Agricultural Situation in the Community, Commission.

ANNEX XIX

Table 9 — Fat content of cows' milk

	<i>Fat content as % of weight</i>							
	1983	1984	1985	1986	1987	1988	1989	1990
Belgium	3.570	3.580	3.630	3.700	3.730	3.740	3.820	3.880
Denmark	4.280	4.240	4.320	4.350	4.390	4.310	4.340	4.430
Germany	3.870	3.890	3.910	3.980	4.010	3.970	4.040	4.100
Greece	3.550	3.557	3.613	3.577	3.562	3.507	3.500	3.540
France	3.840	3.840	3.860	3.890	3.890	3.870	3.900	3.950
Ireland	3.520	3.500	3.550	3.540	3.510	3.530	3.540	3.530
Italy	3.550	3.550	3.560	3.560	3.550	3.550	3.570	3.590
Luxembourg	3.840	3.830	3.860	3.890	3.970	3.980	4.040	4.090
Netherlands	4.120	4.130	4.170	4.270	4.310	4.290	4.320	4.380
United Kingdom	3.890	3.890	3.940	3.930	3.940	3.920	3.940	4.000
EEC 10	3.86	3.87	3.89	3.93	3.94	3.92	3.96	4.01

Source: CRONOS Monthly statistics on cows' milk deliveries.

ANNEX XX

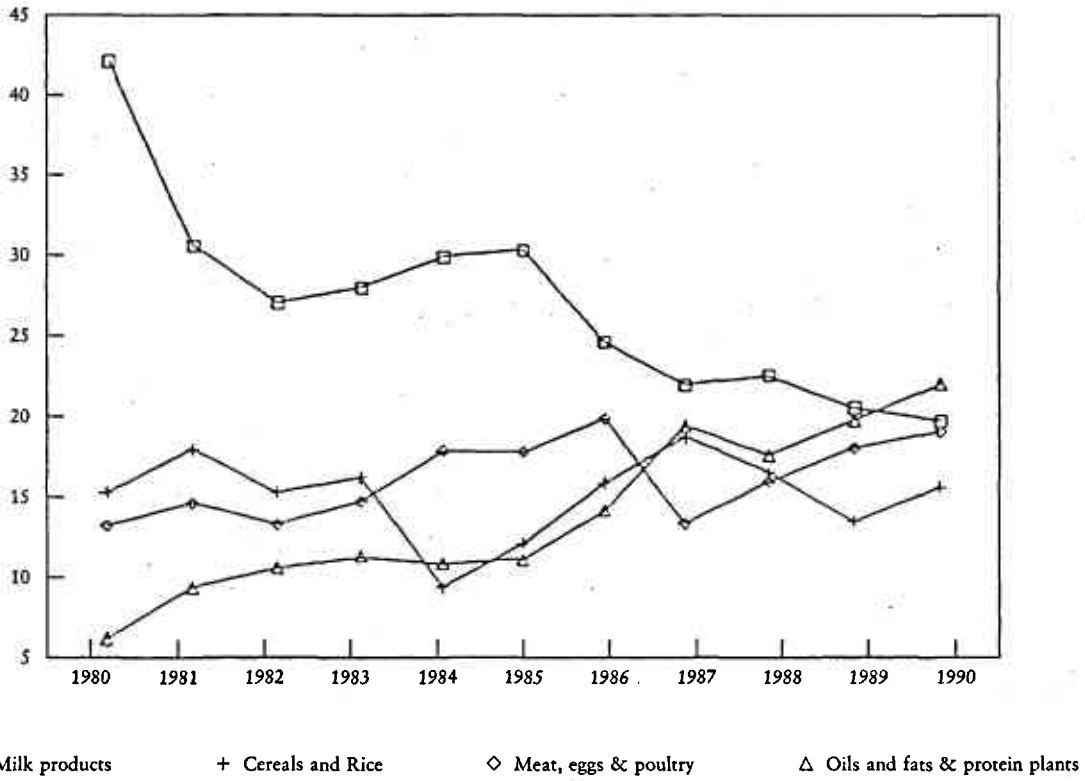
Table 10 — Situation regarding late payments as at 15 October 1991

	1989/90			1990/91		
	Amount due	Balance due at 15 October 1990		Amount due	Balance due at 15 October 1991	
	Mio ECU	Mio ECU	%	Mio ECU	Mio ECU	%
Belgium	12,00	7,86	65,51	12,68	12,44	98,11
Denmark	11,44	-0,02	-0,21	11,90	0,14	1,13
Germany	109,59	29,46	26,88	30,48	16,23	53,24
Greece	2,56	2,56	100,00	7,06	7,06	100,00
Spain						
France	39,86	8,49	21,30	5,83	5,83	100,00
Ireland				1,85	1,85	100,00
Italy	77,96	74,62	95,72			
Luxembourg	1,59	0,23	14,47	3,46	3,27	94,51
Netherlands	28,88	-2,15	-7,44	35,44	4,89	13,80
United Kingdom				13,42	0,31	2,29
EEC	283,88	121,05	42,64	122,10	52,00	42,59

Source: Commission — Member States' statements of 10 November 1991.

ANNEX XXI

Graph 11 — The CMOs — payments (as a % of EAGGF-Guarantee payments)



Source: Revenue and expenditure accounts.

ANNEX XXII

Dilution of the levy

Milk year 1991/92

Target price for milk: 0,2681 ECU/kg

Levy (Formula A or B): $115\% \times 0,2681 = 0,308315$ ECU/kg

In the event of Formula B being applied, the dairy pays the competent agency of its Member State the additional levy due on the amount by which the quota allocated to the dairy has been exceeded. It then recoups the amount paid from those producers who have exceeded their individual quota.

Suppose that the dairy buys milk from 20 milk producers, 10 of whom have exceeded their individual quota by a total of 200 000 kg. The 10 other producers have not used up all of their individual quotas. Taken together, these 10 other producers could have delivered a further 100 000 kg. This being so, the dairy exceeds its quota by 100 000 kg, since it can off-set the overruns of individual quotas against the under-utilizations of individual quotas. It therefore has to pay the following levy: $100\ 000 \times 0,308315 = 30\ 831,5$ ECU. It recovers from the 10 producers who have exceeded their quota:

$30\ 831,5 : 200\ 000 = 0,1541575$ ECU/kg.

Dilution of the rate of levy: $0,1541575 : 0,308315 = 50\%$.

In this case the producer pays only 50 % of the rate paid by the dairy.

ANNEX XXIII

Transfers of quotas between deliveries and direct sales — Application of the Article 6a procedure of Council Regulation (EEC) No 857/84 of 31 March 1984 ⁽¹⁾

The use made of the Article 6a procedure described in paragraph 4.22 has led to critical observations in two Member States:

- (a) in France, the competent authorities have obtained from the Commission, in respect of the procedure referred to in paragraph 4.22(a), a total volume of 409 000 tonnes for definitive transfers of direct sales quotas to deliveries. France did not base itself on individual requests received by ONILAIT ⁽²⁾ but on the disparity between the figure for the national reference quantities and the figure for direct sales actually made. The criteria for distinguishing between definitive transfers and provisional transfers (i.e. those linked to the economic needs to which the Article 6a procedure refers) are in fact not very clear, to say the least. Indeed, as the Commission's clearance department has found since 1987, a not inconsiderable proportion of the transfers regarded as provisional are in fact definitive transfers not admitted as such. Two aspects in particular need to be emphasized here:
- (i) first of all, net transfers to deliveries under the Article 6a procedure represent a considerable amount for the milk year 1988/89. Net transfers amounted to the equivalent of just under 30 % of the overrun, thus reduced accordingly, of the guaranteed total quantity for deliveries; a transfer of this kind is possible at this level only because of the margins of manoeuvre allowed by a 'direct sales' quota whose true degree of utilization is only partly known and, moreover, not checked by the national authorities;
- (ii) an examination of individual files corroborates this assessment. What matters for the intervention agency (ONILAIT) is the existence of, on the one hand, a dual quota and, on the other, a need at the dairy to which the mixed producer in question delivers his milk. It is the amount by which the latter exceeds his 'deliveries' quota which determines the amount of the transfer finally granted after the end of the milk year. The only ceiling imposed on the initial quota is a theoretical ceiling (97 %), since ONILAIT does not worry about the actual rate of use of the 'direct sales' quota. This is therefore a far cry from the criteria laid down in Article 6a;
- (b) in the United Kingdom, there is a structural imbalance in the way in which the quotas are distributed between deliveries and direct sales. The United Kingdom has not lodged any request for a definitive transfer of quotas from direct sales to deliveries, even though the mechanism whereby the Commission can adjust the reference quantities (mentioned in paragraph 4.22) would have been justified (at least since sales of farm cheese in the UK have been regarded as deliveries). The UK uses the Article 6a provision in order, at the end of each milk year, to make a transfer of quotas between deliveries and direct sales, known as 'interchange' in English. This mechanism deviates from the spirit if not the letter of the Community provision in that, as in France, it results in reserves being created for deliveries and it is, moreover, based on individual requests that do not specify the quantities to be transferred.

⁽¹⁾ OJ L 90, 1.4.1984, p. 13.

⁽²⁾ 'Office national interprofessionnel du lait', the French public intervention agency in this field.

ANNEX XXIV

The specific aid measures: compensation for the definitive discontinuation and compensation for the temporary suspension of milk production

1. Since 1987, and above all since 1988, spending on the common organization of the market in milk and milk products has been increased by the cost of two specific measures, namely compensation for the definitive discontinuation of milk production and compensation for the temporary suspension of milk production. The average burden of these measures in comparison with the total gross expenditure (slightly more than 10 % over the last three financial years) must be seen in relation to their aim, which is to reduce production.

A. Community cessation aid scheme introduced in 1986

2. The compensation for the definitive discontinuation of milk production introduced by Council Regulation (EEC) No 1336/86 of 6 May 1986 is granted to volunteer producers — both those who deliver and those who sell direct — in order to help achieve the objective of reducing the national quotas by 3 %. This reduction was supposed to be made overall in two stages: 2 % by 1 April 1987 and 1 % by 1 April 1988. The Regulation grants each Member State an allocation of EAGGF appropriations to cover the expenditure, which is calculated on the basis of maximum compensation of 4 ECU, raised to 6 ECU in 1987 ⁽¹⁾, per 100 kg and per year for seven years. This compensation may be supplemented by the Member States, which can adjust it according to certain objective criteria. The *Table* in Annex II shows the theoretical allocation of appropriations and the actual amount of expenditure from 1987 to 1991.

3. The main feature of the system thus laid down is that it has a three-fold approach:

- (a) it consists of an across-the-board reduction in two stages of the total quantities guaranteed to each Member State and stipulated in the basic Regulation;
- (b) it takes the form *a priori* of aid granted to individual producers, who, within a given Member State, agree to give up milk production completely; in this respect, provision is made for granting the Member States a financial allocation calculated on the basis of the volume to be reduced and the maximum rate laid down by the regulations;
- (c) nevertheless, if, for various reasons, the amount thus defined is not used in full for paying the Community compensation, the amount available may be used by the Member State in other forms for national cessation and/or restructuring programmes.

4. The basic Regulation for the compensation and its implementing Regulation (Commission Regulation (EEC) No 2321/86 of 24 July 1986) were amended by Regulations of 16 March 1987 ⁽¹⁾ and 30 November 1987 ⁽²⁾ respectively. The 1986 cessation scheme as originally conceived proved impracticable. Several major amendments to the Regulation had distorted the initial text, thus making it pointless to a certain extent to draw up a Community definition of aid to producers discontinuing production. These amendments, which accompanied the increase in the maximum rate of compensation, substantially relaxed the conditions imposed on the Member States for using the financial allocation:

- (a) the Member States are permitted to use the allocation in various forms in order to achieve the aim of overall reduction in cases where payment of compensation as defined in the basic Regulation does not allow this;
- (b) furthermore, the amended implementing Regulation makes it possible to pay the compensation in one or two instalments to all or some of the producers concerned; the latter amendment, which was introduced in a legal act of lower rank, substantially modifies the Community mechanism as initially conceived in the legal act of higher rank. Thus the Member States, which did not initially have any choice about the means they could use for achieving the objective of reducing their quotas by 2 % + 1 %, obtained a green light in 1987 to act virtually as they pleased, either by introducing cessation schemes quite different in spirit from the Community scheme, or by implementing a method of making across-the-board reductions in the quotas of all the individual producers.

⁽¹⁾ Council Regulation (EEC) No 776/87 of 16 March 1987, OJ L 78, 20.3.1987, p. 8, amending Regulation (EEC) No 1336/86, OJ L 119, 8.5.1986, p. 21.

⁽²⁾ Commission Regulation (EEC) No 3602/87 of 30 November 1987, OJ L 339, 1.12.1987, p. 59, amending Regulation (EEC) No 2321/86, OJ L 202, 25.7.1986, p.13.

5. The national measures in force are therefore very different from each other, even though the national quotas have been correctly reduced in each Member State. All that remains of the discontinuation compensation scheme is the allocation of funding to the Member States to enable them to make a definitive reduction of 3 % in their quotas in a wide variety of ways. It is thus difficult, to say the least, to assess the effectiveness of such a system at Community level.

B. Application in the Member States of the aid scheme for the discontinuation of milk production introduced in 1986

6. In Belgium and Denmark, the Community aid scheme for the definitive discontinuation of milk production has achieved its objective, even though most of those receiving the compensation have been elderly producers, some of whom have taken advantage of the scheme to bring forward their retirement.

7. In France, the Community-financed scheme set up in 1986 to achieve the 3 % objective consisted of depressive compensation, intended to assist small producers to give up production, with a maximum rate equivalent to 3 ECU that was considerably lower than the limit laid down in the regulations which was raised in 1987; at the same time, a national cessation scheme was set up, aimed at the same type of farmers but consisting in the payment of a single amount of compensation at a rate that was obviously much higher than the annual Community compensation (producers were not allowed to receive both types of compensation). In the milk year 1986/87 the target figure of 512 680 tonnes of delivery quotas to be given up was not achieved for two reasons: competition with the single national compensation payment and the farmers' hope that the maximum rate of Community compensation would be increased from 4 to 6 ECU in 1987, at the time when the compensation mechanism actually came into effect for the first tranche. The French authorities took this into account for the second programme, which aimed at a 1 % reduction by 1 April 1988, but did not reconsider the general economics of the 1986/87 programme. In fact, the French authorities, arguing that changes (referred to above) had been made to the Community regulations, forced the Commission to allow the cessation quantities still needed to attain the target 512 000 tonnes of the first cessation programme, i.e. 72 000 tonnes, to be deducted *ex post facto* from the 'rival' national scheme. This device in the end enabled France to use all the financial appropriations available to it, but in accordance with rules which were very different from those initially laid down and at the expense of unusually complex administrative arrangements. The *ex post facto* checking by the Commission and the Court of Auditors of the declared expenditure (covering eight years in all) was made all the more difficult by the fact that the standard tables drawn up by the Commission to take stock of the situation were themselves hard to understand and ill-suited to their purpose.

8. In Germany, there has been a similar situation with the Community cessation scheme introduced in 1986 coexisting with national aid schemes for the cessation and restructuring of production. In fact, five buying-up programmes have been organized since 1989. All of these, except the third, corresponded to national measures. The fifth was jointly financed by the Community under a special mechanism, which has been criticized by the Court. The first measure was organized as of 1984, as soon as it became clear that the guaranteed national quantity had been greatly exceeded by the allocations of individual quotas: a quantity of 1 001 835 tonnes was thus bought up. The second measure was organized in 1985, allowing 129 110 tonnes to be bought up. The third measure in chronological order, which corresponded to the Community scheme, failed entirely to achieve the target of 471 000 tonnes allocated to Germany. In fact, only 88 904 tonnes were bought up. The fourth measure made it possible to absorb 222 358 tonnes. The fifth measure, jointly financed with funds belonging to the EAGGF-Guarantee, achieved just under 400 000 tonnes. Thus, the Community compensation scheme suffered from the coexistence with national aid measures which proved to be more advantageous. The financial appropriations allocated to Germany for the purpose of reducing production by 3 % was indeed used in the end, but in forms different from that of the Community compensation, as in France. Lastly, the most recent programme created inequality between producers who had ceased production, in so far as the rate of compensation was fixed at 1,6 DM per kg as against 0,7 DM for the previous programmes.

9. In the United Kingdom, the overall reduction target was achieved only because of the possibilities opened up in 1987 by amendments to the regulations, namely in the form of a compulsory across-the-board reduction in the individual quota of each producer (in two stages). Originally, a Community-financed scheme and a nationally-financed scheme for compensation for the definitive discontinuation of milk production were set up, but they failed. Only a small number of producers — 269 — requested and obtained Community compensation. The reason for this failure is to be found partly in the structure of the farms, but probably more in the mobility of quotas which took place because of the market in quotas that exists in the United Kingdom.

10. In the Netherlands, it was possible to buy up only just over one fifth of the quantities planned in the scheme, as the compensation for the definitive cessation of milk production was far too low in relation to the price which the producer could receive by selling his individual reference quantity to another producer.

11. In Ireland and Luxembourg, it was possible to carry out the scheme of compensation for the definitive discontinuation of milk production completely only by also making across-the-board reductions in the individual reference quantities. In both Member States, those benefiting from the scheme were above all elderly producers who were already retired or who brought forward their retirement. The compensation supplements their pension. In Ireland in particular a large number of small producers switched to rearing calves whilst keeping some dairy cows and received compensation for the definitive discontinuation of milk production as well as the suckler cow premium.

12. In Spain, the scheme of compensation for the definitive discontinuation of milk production with a target of 162 000 tonnes managed a reduction of 155 921 tonnes. Until the end of the financial year 1990, this scheme cost the Community budget 38 Mio ECU and in the years to come will go on giving rise to spending of an almost equivalent amount. Despite this apparent success, which was achieved at heavy cost, the scheme is likely to prove not very effective in terms of the objective of reducing milk production, as, without the quota system being applied, it is virtually impossible to verify whether the conditions of the contract for the cessation of milk production are being complied with and to penalize fraud. The control reports which have been examined and the on-the-spot checks have shown how easy it is to circumvent the obligation to stop producing milk, given that there is no crack-down on failure to keep to the individual reference quantities: it is enough to say that the milk is being used for animal feed or to transfer the herd to the name of another member of the family who, even without a quota, can continue to deliver milk to a purchaser.

13. In Italy, the financial appropriations earmarked for this Member State have not been used. Even though the guaranteed national quantity was indeed reduced in two stages by means of the direct application of the new maximum figures contained in the basic Regulation, no Community cessation scheme has been implemented. The reason for this is simply that the system of individual quotas did not exist at that time in this Member State and so there could be no question of paying compensation reserved for farmers holding such a quota who would cease production.

14. In Greece, the scheme has not been applied. Council Regulation (EEC) No 1931/88 of 29 June 1988 derogates from Regulation (EEC) No 1336/86 by stipulating that 'the Hellenic Republic shall use the funds available to finance programmes to improve the quality of milk for the benefit of the producers concerned' ⁽¹⁾.

C. Aid scheme for the temporary withdrawal of quotas

15. Council Regulation (EEC) No 775/87 of 16 March 1987 provides for the temporary withdrawal of a proportion of the 'deliveries' reference quantities, in such a way that the amount of quotas actually available, calculated on the basis of the milk year 1986/87, is reduced by 4 % in 1987/88, then by 5,5 % in 1988/89 and by 4,5 % for the subsequent years (following the amendments introduced in the 'Nallet package' of December 1989). The application of this measure involves in principle the payment, until 1992, of a degressive annual amount of compensation which is financed by the Community budget and may be supplemented by the Member States. This compensation is paid to producers who hold a quota directly (Formula A) or indirectly (Formula B). Italy, Spain and Greece are allowed to derogate from the rules for applying the compensation. Greece was authorized by Council Regulation (EEC) No 1931/88 to allocate the funding which had initially been earmarked for the withdrawal compensation 'to finance programmes to improve the quality of milk for the benefit of the producers concerned'.

16. In its proposal for a reform of the common agricultural policy concerning the milk sector, the Commission recommends that the temporary suspension of 4,5 % of the guaranteed total quantities be converted into a definitive reduction of quotas without further compensation. The Commission considers in its reform proposals that the compensation which has been granted to milk producers over five years for the individual reference quantities suspended (in total 45,5 ECU per 100 kg) represents fair compensation ⁽²⁾. The decision taken by the Council will come into force as of the milk year 1993/94.

⁽¹⁾ Council Regulation (EEC) No 1931/88 of 29 June 1988 amending Regulation (EEC) No 775/87 on the temporary discontinuation of part of the reference quantities referred to in Article 5c(1) of Regulation (EEC) No 804/68 on the common organization of the market in milk and milk products, OJ L 170, 2.7.1988, p. 4.

⁽²⁾ Reform of the common agricultural policy

— Legal texts

— Milk sector

— COM(91) 409 final of 31 October 1991 (see paragraph A.1.(b), p. 1).

ANNEX XXV

National programmes for buying-up quotas and for restructuring milk production

In France, the Community programme introduced in 1986 has to compete with a national buying-up scheme whose conditions are more favourable for the producers than those of the Community programme. For each of the milk years 1987/88 and 1988/89 a national buying-up programme, financed partly by the Community budget, was open only to producers delivering to dairies.

In Germany, five national buying-up programmes were decided for the milk years 1984/85, 1985/86, 1986/87, 1989/90 and 1990/91. The aim of all these programmes was to reduce the overrun of the guaranteed national quantity that occurred when the scheme was introduced, following numerous complaints by producers.

In Belgium, only one national restructuring programme was organized, in 1985.

In Ireland, pursuant to Article 4(1)(d) of Regulation (EEC) No 857/84, a national restructuring programme was set up as of the milk year 1987/88. This scheme provides for the buying-up by a purchaser of an individual reference quantity from a producer who, in return for remuneration in the form of a single amount of compensation, undertakes to cease milk production. Individual reference quantities thus bought up may be re-sold at the same price by the purchaser to one or more of his priority producers.

Denmark, also pursuant to Article 4(1)(d) of Regulation (EEC) No 857/84, introduced a national restructuring programme as of the milk year 1990/91. The 'Mælkeudvalg', the sole purchaser in Denmark, buys up the individual reference quantities offered and sells them again at the same price to priority producers.

In the Netherlands, a national buying-up programme has been operating for all the milk years, except for the years covered by the 1986 Community programme. In general, the results have not been encouraging. The prices offered to the producer who wants to sell his quota on the market are much higher than the compensation for discontinuation proposed by the buying-up programmes (see paragraph 4.34). In view of the mediocre results of the past, it is planned to discontinue the programmes in future.

In Luxembourg, the authorities have also run a national restructuring programme for milk production for all the milk years, even concurrently with the 1986 Community programme.

In Italy, two national programmes for the slaughter of dairy cows, wholly financed by national funds, were carried out in 1986 and 1987 as a supplement to the implementation of the Community discontinuation scheme (see Annex XXIV, para. 2), which was impossible to put into practice given that the Italian milk producers had not yet been allocated individual reference quantities. The second of these programmes was carried out in derogation from Articles 1 and 2 of Regulation (EEC) No 775/87, which provided for the withdrawal of 4 % of the guaranteed total quantities for the milk year 1987/88 and 5,5 % for the following four milk years. The two national programmes for the slaughter of dairy cows made it possible to eliminate milk production estimated by the Italian authorities at more than 6 % of their guaranteed total quantity.

In the United Kingdom, the sole national buying-up programme suffered a devastating failure because the prices offered on the market considerably exceeded the buying-up price of the Community programme.

In Spain and Greece, no national buying-up or restructuring programmes have been implemented.

ANNEX XXVI

Application in the Member States of Article 4a of Council Regulation (EEC) No 857/84

In the United Kingdom (a Formula B country), the system operates in such a way, through the regional Milk Marketing Boards, that the levy passed on by the purchasers to the producers is reduced to a minimum; this is done by the available quotas being redistributed in a generally uniform manner, subject to the situation of a certain category of priority producers being taken into account.

In France (a Formula B country), at the end of each milk year ONILAIT ⁽¹⁾ organizes a huge exchange of 'deliveries' quotas between dairies once an initial off-setting has been carried out within each of them; the purpose, at both levels, of the redistribution thus achieved is to allocate the available quotas to producers according to the priority criteria laid down by Ministerial decree each year.

In Ireland (a Formula B country), the DOA ⁽²⁾ has set up a multi-phase off-setting system, known as 'fleximilk', which favours small producers. In the first phase, each purchaser off-sets the available balance of his own quota amongst his producers. Then the DOA carries out an off-setting between purchasers. Lastly, the surplus purchaser may redistribute the compensation allocated to him by the DOA amongst his producers.

Belgium (a Formula A country) has applied the off-setting of Article 4a, known as equalization, from the very first milk year, without laying down the criteria for allocating the available quantities.

In Luxembourg (a Formula B country), the SER ⁽³⁾ manages the Article 4a off-setting between the four purchasers without laying down the priorities for allocating the available quotas.

In Germany (a Formula A country), the national authorities do not apply the Article 4a mechanism: if the producers exceed their individual quota, they have to pay the additional levy, whereas the Member State passes on to the Commission only the amount corresponding to the overrun of the guaranteed national quantity. It is, however, necessary to qualify what appears to be a fairly strict application and therefore faithful to the original spirit of the Community Regulation. At the outset, Germany allocated individual quotas which considerably exceeded the guaranteed national quantity. The amounts levied by virtue of the fact that Article 4a has not been applied have subsequently been used by Germany for financing national programmes for buying up quotas.

In Italy (a Formula A country), UNALAT, the Union of milk producer associations, which represents 98 % of national production, was allocated a reference quantity for the first time in 1988. The producers belonging to UNALAT did not in turn receive an individual quota until the milk year 1990/91. As a result of this, in the absence of any declarations by the producers and purchasers, the only source of data on production up until the milk year 1989/90 was statistical surveys. This being so, there could be no question of applying Article 4a, except in very specific terms at the time of the Commission's clearance of the accounts. *De facto*, however, this situation resulted in virtually automatic national off-setting, which was not provided for by the regulations and from which individual producers benefited.

In Spain (a Formula B country), the mechanisms of Article 4a have never been formally applied: so long as deliveries of milk to purchasers are estimated by statistical surveys, the Article 4a off-setting is implicit.

In the Netherlands (a Formula A country up until the milk year 1987/88, since then a Formula B country), the Article 4a off-setting has never been applied.

In Greece (a Formula B country), Article 4a is not applicable as, according to Article 10, subparagraph 2, of Council Regulation (EEC) No 857/84 of 31 March 1984, 'all purchasers taken as a whole shall be considered as one purchaser'. This being so, off-setting is possible without using the Article 4a procedure.

In Denmark (a Formula B country), the Mælkeudvalg has been the sole purchaser since the quota system came into force. This being so, the case of Denmark is comparable to that of Greece where off-setting between producers is possible without using the Article 4a procedure.

⁽¹⁾ 'Office national interprofessionnel du lait', the French public intervention agency in this field.

⁽²⁾ DOA: the Department of Agriculture in Dublin.

⁽³⁾ SER: 'Service d'Economie Rurale', a department of the Ministry of Agriculture.

COMMISSION REPLY

2. THE MARKET IN MILK
AND MILK PRODUCTS*Changes in milk production in the
Community*

2.12. Statistics provided by Spain had understated milk production, therefore the national guaranteed quantity was in fact exceeded as from the 1988/1989 marketing year. Similarly, the statistics provided by Italy were found to have understated milk production. Enquiries aimed at establishing the actual production between the 1988/1989 and current marketing years are still underway. A report on this subject has been sent to the Council [COM(93) 109 of 9 March 1993].

2.16. The Commission will invite the Member States to enquire into the Court's inferences. It should however be borne in mind that the quantities concerned are relatively insignificant, direct sales accounting for only 3 % of milk marketed.

Changes in stocks of butter and skimmed-milk powder

2.31. The Commission draws attention to the fact that by the end of 1992, principally as a result of its management measures, intervention stocks had been reduced to 47 299 tonnes of skimmed milk powder and 172 455 tonnes of butter.

The persistent imbalance

2.39. It is responsibility of the Council, after consultation of the European Parliament, to decide how the balance between the various objectives mentioned in the Treaty should be achieved. In the context of the reform of the CAP, the Council has decided to re-orientate the agricultural policy in general towards a system which does not stimulate production of surplus products. The general arrangement of the dairy sector is in line with that policy.

3. THE COMMON ORGANIZATION OF THE
MARKET IN MILK AND MILK PRODUCTS*The objectives*

3.3. These objectives, which result from Article 39 of the Treaty and are listed in the fourth recital of Regulation No 804/68, are among the objectives of the common agricultural policy and must therefore of course be respected by all the institutions responsible for shaping the CAP.

The quota system

3.24. The 1991 Commission recommendation referred to by the Court was incorporated in the new system adopted by the Council in December 1992.

Changes in budgetary expenditure

3.27. It is inappropriate to include expenditure under article 101 in the current annual expenditure of the milk sector. This could give a misleading impression of the underlying trend in expenditure since the introduction of the 'quota' system in 1984. As the Court recognizes in point 3.28, the reimbursement of 797,4 Mio ECU in 1991 formed part of the costs occurred in 1987 and 1988 of nearly 3 200 Mio ECU when the butter disposal took place.

Furthermore, in 1992 expenditure in the milk products sector came to only ECU 4 008 million, or to ECU 4 375 million if the co-responsibility levy is not taken into account.

Finally, a comparison between annual budgetary expenditures in the early 1980's and those for 1991 should recognise that in the interim, the Community has been enlarged to include not only Spain and Portugal but also the territories of the former GDR (increase of the milk market by 64 Mio people and about 10 Mio of milk).

Budgetary booking of some revenue in the milk sector

3.30. The Commission would refer to its previous replies to the effect that this levy is an intervention mechanism and not an own resource for the Community budget. It constitutes negative expenditure to finance specific CAP measures covered by the Community budget. The collection procedure is governed by the arrangements for the management of the intervention measures for the common organization of the market for milk and milk products (see reply to paragraph 3.28 of the Court's annual report for 1985).

4. IMPLEMENTATION OF MEASURES FOR CONTROLLING MILK PRODUCTION

The non-application of the quota system by some Member States

4.6. See answer to 4.55

The complexity of the regulations and their disparate interpretations

4.10. In the context of the reform of the CAP, the Commission proposed a condensation and simplification of the Regulation on the additional levy in the milk sector [COM(91) 409]. The subsequent Council Regulation (EEC) No 3950/92, adopted in December 1992, took up a number of points for which the Court, following the Commission's lead, suggests improvements, particularly as regards application of the arrangements in accordance with a standardized formula (paragraph 3.21), the status of certain priority producers who feel encouraged by their Member State to exceed their individual reference quantity (paragraph 4.19), delays in collecting the levy (paragraphs 4.27-4.29), the elimination of which constitutes a major objective of the Commission's proposal, temporary transfers (paragraph 4.50) which the Court also sees as a major improvement to the arrangements both for individuals and overall and the regulated transfer of quotas (paragraph 5.17), without, however, covering transfers between Member States which are impracticable in the current situation.

4.11. The regulation providing compensation for 'SLOM' producers is in preparation [COM(93) 161 final of 21 April 1993].

Perpetuation of the general offsetting mechanism and the passing-on of the additional levy to individual producers

4.17 - 4.20. As regards what the Court calls the dilution of the deterrent effect of the levy, it should be pointed out that, under various correctives introduced since 1986/1987 (see paragraph 4.20), producers who have overrun must, from a certain threshold, pay all the additional levy in those Member States where the system is applied. Furthermore, while it cannot be denied that producers seek to make maximum use of the guaranteed total quantity, it is equally true that the necessary consequences have been drawn in successively reducing these quantities against payments.

Transfers of direct sales reference quantities to deliveries

4.23 - 4.24. A correction will be made under the clearance of accounts procedure if supplementary levies are not collected by Greece and Spain on all direct sales exceeding the global guaranteed quantity.

Delays in collecting the revenue deriving from the additional levy

4.28 - 4.29. In order to avoid long delays between collection and payment of the additional levy, which are incompatible with the scheme's objectives, the Council decided certain provisions in December 1992, making the purchaser liable for the levy and empowering him to collect it from producers. If these provisions do not solve the problem of delay in payments by Member States the Commission will, in the case of substantial problems, make use of its powers to reduce the monthly advances to Member States. This is in accordance with the judgment of 17 October 1991 by the Court of Justice in Cases C-342/89 and C-346/89.

Inadequate correction in cases where the fat content is exceeded

4.30 - 4.32. As regards the correction in cases where the fat content is exceeded, it is true that these provisions are difficult to implement. That is why the rules have been amended to introduce a trigger threshold (the national reference) below which the provisions do not apply. This amendment also has the advantage of providing comparable treatment for all producers in the same situation;

this was not the case previously because of differences which might arise between the situation of formula A or formula B producers at first and then, in formula B, between the purchasers themselves.

4.33. The Commission examines each year, under the clearance of accounts procedure, the application by Member States of the fat content provisions; it applies a correction when the full amount of supplementary levies has not been charged, as far as reliable data are available.

4.34. It is not the objective of the scheme introducing reference quantities for milk production to prevent an increase of the fat content of milk as long as milk production is adjusted accordingly. As the protein content of milk has remained stable a reduction in milk production due to a higher fat content would lead to a decrease of the production of skimmed milk.

As regards the Court's doubts about the deterrent effect of the correction, it should be pointed out that the current rules provide for a penalty of ECU 454.89 per 100 kg compared with an intervention price for butter of ECU 292.78 per 100 kg, giving a net penalty of ECU 162 per 100 kg (55 %). At this level, it may justifiably be assumed that any increase would run counter to the desired goal.

It is correct that around 4 mio tonnes of milk are needed to produce 178 000 tonnes of butter. However, such an increase in milk production would also involve the production of around 132 000 tonnes of skimmed milk powder.

Mobility of quotas

4.50. It is for the reasons indicated by the Court that in October 1991 the Commission submitted a proposal to the Council [COM(91) 409] obliging Member States to introduce the possibility of temporary transfers. The Council adopted on it in December 1992 after some modifications designed to ensure that structural development would not be hindered.

Control measures

Management criteria and the Commission's monitoring of the various measures

4.52 – 4.53. The Commission shares the Court's concern over missing and incomplete information supplied by the Member States. The Commission has done its utmost to improve this situation, and is currently examining the possibility of further improvements.

Control measures in the Member States

4.55. The application of the milk quota regime is monitored each year in every Member State, and many failures in application or insufficiency in controls which risk having an effect on the Community's budget have led to significant financial corrections in the accounts.

Following agreements in the Council concerning the requests of Greece, Spain and Italy for additional quotas, each has undertaken to fully apply the regime as from the 1993/1994 marketing year. The Commission is closely monitoring the implementation of these commitments, both the legal and administrative arrangements, and will report to the Council on the progress made before 31 March 1993. The effectiveness of the measures will afterwards be closely verified.

The Commission also made the following financial adjustments when taking its decisions on the clearance of accounts:

Corrections to the clearance of accounts concerning the additional milk levy

(ECU million ⁽¹⁾)

	1987	1988	1989
B	3,9	3,0	1,6
D	148,7	43,3	86,2
EL	—	—	1,3
ES	—	—	150,3 ⁽²⁾
F	—	22,2	19,7 ⁽²⁾
I	47,8	52,1	540,0
L	—	—	0,1
NL	2,7	11,8	0,8
	203,1	132,4	800,0

⁽¹⁾ Converted at the exchange rates at the end of the financial year in question.

⁽²⁾ Expenditure in respect of which Community finance has been provisionally ruled out.

Specific aid measures and the quota system

4.57. The Commission would point out that, from a legal angle, the compensation is intended to offset the reduction in the quantity which may be produced without a levy. If producers who had to pay the levy did not receive this compensation, they would be penalized twice: once when the levy is imposed on suspended quantities and a second time when the compensation is not paid. The Council has twice used this as grounds for rejecting Commission proposals to link payment of compensation to compliance with the unsuspended reference quantities.

Review of the budgetary situation

4.64. Comparison on the one hand of the additional expenditure on the programmes for the cessation and suspension of milk production, cumulated for all of the years 1984-1991 with, on the other hand, the reduction in production of 8 mio tonnes achieved for a single year compared to the base year (ie. 1991 compared to 1984), does not provide the complete picture.

Instead, the cumulative expenditure should be compared with the cumulative reduction in production:

	<i>Mio tonnes</i>		
	Milk production ⁽¹⁾	Reduction compared to	
		1983	1984
1983	118,8	—	—
1984	116,8	- 2,0	—
1985	115,9	- 2,9	- 0,9
1986	117,3	- 1,5	+ 0,5
1987	112,1	- 6,7	- 4,7
1988	109,7	- 9,1	- 7,1
1989	109,1	- 9,7	- 7,7
1990	109,0	- 9,8	- 7,8
Cumulative reduction	—	- 41,7	- 27,7

⁽¹⁾ EC 12 (not including the former GDR).

Depending upon whether the comparison is made with 1983 (the last full year before the implementation of the superlevy system) or with 1984, the cumulative reduction in production up to and including 1990 is therefore more than

40 mio tonnes or nearly 28 mio tonnes. It should, moreover, be recalled that in the period preceding the introduction of the superlevy system, Community milk production was increasing at an annual average rate of more than 2 % (average for the period 1974-1983 = + 2.2 %). If, in the absence of the quota system, and with prevailing price and intervention conditions continuing unchanged, production had continued to grow at 2 % a year, it would have exceeded 136 mio tonnes by 1990, some 27 mio tonnes higher than the actual figure for that year.

5. CONCLUSION

The reduction in milk production and its inadequacy

5.6. In the context of the CAP reforms in June 1992, the Council decided that, in principle, the global guaranteed quantities should be reduced by 1 % in 1993/1994 and by 1 % further in 1994/1995. Before a final decision is taken the Commission will submit a new report on the market situation in the dairy sector.

Furthermore, while it cannot be denied that producers seek to make maximum use of the guaranteed total quantity, it is equally true that the necessary consequences have been drawn in successively reducing these quantities against payments.

Weakening of the producer's responsibility

5.7. The concept for the Community's milk production has gradually changed over the years; more emphasis has been laid on the global guaranteed quantities rather than on individual reference quantities. However, it should not be forgotten that the global quantities have repeatedly reduced. (See also the replies to points 4.17-4.20, and 4.64).

National off-setting

5.8. The Council has rejected the Commission's proposals to link payment of the compensation to compliance with the unsuspended reference quantities (see also reply to paragraph 4.57).

5.9. As indicated in the reply to point 4.50 it was decided in December 1992 to harmonize the provisions on temporary transfers.

National transfers between deliveries and direct sales

5.10. The Commission shares the Court's opinion relating to the problems in connection with direct sales of milk. However, the Court also recognizes that this problem is limited as it accounts for a small proportion of production.

The procedures which may or may not be applied by the Member States are examined during the Commission's clearance visits and its comments are contained in the resulting reports.

Inadequate deterrent of the adjustment of deliveries or direct sales depending on the fat content

5.11 – 5.12. The Commission is of the opinion that the penalty has a sufficient deterrent effect since, as indicated at paragraph 4.34, it comes to 155 % of the intervention price.

It has never been the objective of the regulations concerning fat content to prevent an increase in the fat content of milk. The aim is to neutralize the effect of such increases via a corresponding adjustment of the guaranteed quantities.

The financial advantage to traders of delaying payment of the additional levy

5.13. The Commission refers to its reply to points 4.28 – 4.29 on improvements in payment of the additional levy. To improve the situation, the Commission has introduced interest on late payment (Regulation (EEC) No 536/93 of 9 March 1993).

Disparate applications

Complexity of the measures

5.14 – 5.16. The Commission would point out that its views concur with those of the Court on the complexity of the system. Following the 1991 Commission proposal, the Council decided in December 1992 to apply the system more simply and more uniformly (See also details given in answer to paragraph 5.21).

Finally, like the Court, the Commission regrets that some Member States have taken advantage of the flexibility of certain provisions of the Council's regulations to evade other rules (paragraph 5.14). It should be pointed out in this respect that the Commission, as it is required to do, has reacted by initiating the appropriate procedures and proposing the necessary changes to the rules both in the past [Judgment by the Court of Justice against Italy in Case 394/85 and Regulation (EEC) No 1116/89 amending Regulation (EEC) No 775/87 for example] and for the future in the proposals it sent to the Council in COM(91) 409 (particularly as regards the transfers of direct sales to deliveries and the elimination of producer groups and associations thereof).

5.15. See point 4.55.

The risks and hazards of setting quotas for production

5.17. The Court refers to two of the objectives mentioned in Article 39 of the Treaty. Article 39 has other objectives as well: to ensure a fair standard of living for the agricultural community, to stabilise markets, and to assure the availability of supplies. The Treaty also implies that environmental aspects must be given due consideration.

The relative importance of these objectives changes according to the general economical situation, employment rates, and constraints deriving from the international situation. In the context of the reform of the CAP, the Commission proposed and the Council decided on effective measures to curb surplus production whilst at the same time assuring farmers' incomes and rural development. The aspect of rational development which was originally introduced to assure supplies has thus been toned down. A highly rational production would also be to the detriment of the environment.

The quota system and farming structures

5.21. With Regulation (EEC) No 3950/92 the Council reorganized and simplified the arrangements for containing milk production. In particular, formulas A and B were replaced by a single formula amalgamating the advantages of the two. The responsibilities of the purchaser-dairy

liable for the levy and the producer who owes the levy are set out in detail and the means for collecting the levy strengthened. The producers' individual rights have been extended and are better protected. The transfer of reference quantities between producers has been set out in detail and extended to different situations. The Commission will also provide more information on control obligations in the detailed rules for the application of this scheme.

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