COMMISSION OF THE EUROPEAN COMMUNITIES

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REPORT FROM THE COMMISSION TO THE COUNCIL

ON GREEK REQUESTS IN THE COTTON SECTOR

1. INTRODUCTION

In a declaration on the operation of the cotton aid scheme adopted at the Council meeting of June 1997, the Council, at the request of the Greek delegation, asked the Commission to submit a report on aid arrangements in the cotton sector by the end of the year, with special reference to the four suggestions put forward by Greece, which involved:

- direct payment of Community aid to producers,

- regionalisation of penalties,

- basing the payment of advances on estimated production increased by a safety margin of 7.5%

- legal provision for revising production estimates in the course of the marketing year.

It should be made quite clear that this report has been drawn up solely in response to that request; it does not in any way replace the report provided for in Council Regulation (EC) No 1553/95 on the system of aid for cotton, which is to be sent to the Council and the European Parliament before the beginning of the 1999/2000 marketing year.

Consequently, this report drafted at the request of the Greek delegation cannot be regarded as an investigation of the economy of the sector in general. It consists in an in-depth examination of the four suggestions, with their advantages and disadvantages, on the assumption that all the other detailed arrangements for the aid scheme remain unchanged. This investigation is not at this stage accompanied by any proposal for changes to legislation.

The suggestions for changes have been assessed in the light of the need to maintain or, if possible, reinforce control measures and their effectiveness, in response to observations made earlier by the Court of Auditors in its annual reports.[1] The Court noted serious weaknesses in the control aspects of the CMO for cotton, and pointed out that both the Council and Parliament had urged the Commission to see that effective control measures were introduced.

2. THE PRESENT SYSTEM

The Greek delegation's suggestions relate specifically to the identity of the recipient of aid, the stabilising mechanism, and, for the last two points, the system of advance payment of grants and consequently also the system of payment of the balance. The present situation can be summarised as follows.

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1. OJ No C 309, 16.11.1993, p. 1.
OJ No C 340, 17.11.1996, p. 1.

2.1 Aid scheme and prices

Cotton does not appear in Annex II to the Treaty, but Protocol 4 to the Act of Accession of Greece explicitly recognises the specifically agricultural character of cotton production and introduces production aid. It was subsequently amended and expanded by Protocol 14 to the Act of Accession of Spain and Portugal.

One of the essential structures of the arrangements for aid to cotton is based on the well-known "deficiency payment" system. Aid equal to the difference between a guide price fixed by the Council and a world market price determined at least once a month by the Commission is granted to **ginning firms**, which are required in exchange to pay a minimum price to producers. Thus while the purpose of the aid is to provide income support for producers, its operation is based on payments to ginners. Moreover, the aid is granted for quantities of unginned cotton, although these quantities are adjusted as a function of the fibre yield of ginnning.

The guide price and the minimum price for unginned cotton of standard quality have been fixed, for a period ending with the 1999/2000 marketing year at the latest, at ECU 106·30/100 kg and ECU 100·99/100 kg respectively. These institutional prices relate to relate to cotton of fair, sound and merchantable quality, having a 10 % moisture content and 3 % impurity content and the necessary characteristics to produce, after ginning, 32 % grade 5 fibres (white middling) of 28 mm length (1-3/32").

The marketing year runs from 1 September to 31 August.

2.2 Stabiliser mechanism

In March 1995 the Commission, acting upon its undertaking at the December 1993 Council meeting "to reflect on the specific problems of the cotton sector in a spirit of fair management", sent the Council a comprehensive report on the operation of the aid system, and in particular the stabiliser mechanism.

In order to solve the problems linked to the fact that increased production in one producer Member State led to identical penalties in both, the Council introduced a system of guaranteed national quantities (GNQs) from the 1995/96 marketing year onwards, with the aim of making sure that producers in each Member State take steps to respond to overshoots themselves. To offset this, the abatement cut-off was removed, as was the possibility of carrying over part of the abatement from one marketing year to the next.

For an abatement to be applied, two conditions must be met:

I. actual Community production must exceed the guaranteed maximum quantity (GMQ) of 1 031 000 tonnes;

II. this Community production must include actual production in Spain exceeding the GNQ of 249 000 tonnes, or in Greece exceeding the GNQ of 782 000 tonnes.

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Moreover, when the abatement is applied to only one Member State, it is based, not on that Member State's overshoot of its own GNQ, but on the Community overshoot of GMQ.

The abatement involves reducing the guide price by a percentage equal to half of that by which the reference quantity is exceeded.

2.3 Advance payments and balances

One of the aims of the reform introduced from the 1995/96 marketing year was to apply penalties in a single marketing year to the producers responsible for overshooting in that year. It was therefore essential to provide for a system of payment to combine advance payments on grants in the course of the year and settlement of the balance at the end of the same year.

2.3.1 Advances

Calculation of advances

Before the beginning of the marketing year, the Commission, in accordance with the Management Committee procedure, estimates production for each Member State concerned. In view of Council Regulation (EC) No 1554/95 laying down the general rules for the system of aid for cotton, the estimated levels of production are increased by a **15%** safety margin for the calculation of a provisional abatement, through the theoretical operation of the stabilisers.

Depending on the variable levels of market prices, the amounts of the advances granted in the course of the marketing year result from the following calculation:

Guide price
- Provisional abatement
- World price

= Advance

As the present system provides for production to be estimated **once only**, provisional abatements are constant throughout the marketing year, but different as between Member States, depending on how far each has overshot its own GNQ. Consequently, for the same world price, the advance may not be the same in both Member States.

The 15% increase in estimated production provides a safety net to ensure that by the end of the year the advances granted do not exceed the aid finally due. This percentage was fixed, from the second year of application of the reform (1996/97) in the light of past figures for the previous nine marketing years, relating to the discrepancy observed between production forecasts before the beginning of the year and actual output recorded at the end (see Annex I). The figures show that a margin of 15% is neither arbitrary nor excessive.

How the system of advances operates

As soon as the unginned cotton enters the ginning plant (is taken into supervised storage) and from 16 October following the beginning of the marketing year, the Member States will, on application from the ginners, grant an advance on aid on condition security of at least 110% of the amount of the advance is lodged. When the cotton is taken into supervised storage, the ginner can indicate that the aid on which the advance is to be granted corresponds to that for the day of entry into supervised storage (subsidy of the day) or to that for a later date (post-fixing). The security is forfeit up to an amount equal to that by which the advance exceeds the aid eventually granted.

The ginning period during which quantities of unginned cotton can be taken into supervised storage and weighed ends on 31 March. However, from the present marketing year (1997/98), the Member State has the option of setting an earlier date if this does not interfere with commercial operations in the sector. In that case, the Member State adopts the new time limit at the latest 30 days before it comes into force, and informs the Commission thereof immediately.

The monthly breakdown of quantities taken into supervised storage in recent marketing years will be found in Annex II. Two points should be borne in mind: it takes longer in Greece than in Spain to dispose of the harvest, and the most active period is usually in October and November. On average, quantities taken into supervised storage up till the end of October and the end of November respectively represent, as a percentage of the total quantity for the period as a whole, 43% and 66% in Greece, and 77% and 96% in Spain.

The period during which operators can apply for advances on aid also ends on 31 March but unlike the ginning period it cannot be shortened by the Member States.

2.3.2 Balance

At the end of the marketing year, the level of the final abatement applicable to each Member State is determined on the basis of each Member State's final production, established at the latest **before the end of June.**

For each period for which a world market price for unginned cotton has been fixed, aid is calculated as follows:

Guide price
- Final reduction in guide price (final abatement)
- World price

= Aid

However, the amounts of aid thus calculated can be increased, pursuant to Article 2(4) of Council Regulation (EC) No 1553/95, if the following three conditions are met at the end of the marketing year:

– the weighted average of the world market price is greater than ECU 30.2 per 100 kg

– total budgetary expenditure is less than ECU 770 million,

– actual production in the Member State exceeds its GNQ.[2]

Definitive amounts of aid are therefore obtained as follows:

Aid
\+ Increase in aid
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= Definitive amount of aid

The balance to be paid to ginners at the end of the marketing year thus corresponds to the difference between the level of definitive aid and the amount of advances. The balance is different as between the Member States, but is in fact constant throughout the marketing year, and does not depend on the period for which a level of world prices has been fixed. It can be obtained as follows:

Definitive abatement
\- Provisional abatement
\+ Increase in aid

The balances paid in the 1996/97 marketing year following full application of the mechanism described above were as follows:

ECU 32.315 /100 kg in Greece,

ECU 0.744 /100 kg in Spain.

Consequently, the balance paid to Greek ginners was significant, corresponding to about 50% of the aid due, because actual output in Greece was considerably less than originally forecast (-24%). The balance paid to Spanish ginners, on the other hand, was quite small, because actual output in Spain was 13.6% higher than forecast, a figure very close to the 15% safety margin applied to forward estimates of production.

2.4 Actors in the cotton sector

The main actors involved in the agricultural production of cotton in the strict sense are the producer organisations and the ginning firms. A brief survey of these two categories is sufficient for present purposes, leaving aside the description of the textiles industry downstream, mainly spinners and weavers.

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2 The increase may not raise aid above the level of the two ceilings specified in the aforesaid Regulation, i.e. aid without the application of the abatement and aid resulting from an increase in the GNQs (270 000 tonnes for Spain and 850 000 tonnes for Greece).

2.4.1 *Producer groups*

During the 1980s, the Community encouraged the formation of producer groups in the cotton sector. Start-up aid and investment aid was provided, mainly for the purchase of harvesting machinery.

At present, harvesting machines are generally available, in both Greece and Spain. Producer groups still have the job of managing this stock of equipment; but they no longer seem very active in terms of concentration and adjustment of supply by producers. However, it must be recognised that these functions can be fulfilled by the industry downstream (co-operatives and others). In Spain, producer groups are not very highly organised, and indeed only involve 12% of producers.

2.4.2 *Ginning firms*

In Greece, of a total of some 90 firms, co-operatives represent about a third of the number and 40% of ginning capacity at present. There is no particular problem in the sector as a whole, in view of the level of total output.

In Spain, co-operatives also represent about a third of the total of eighteen firms. In the sector as a whole, there is some spare ginning capacity in relation to the supply of cotton, especially in recent years (1993/94 to 1995/96), when persistent drought was a major factor in limiting supply. However, if the increase in areas sown recorded in 1996/97 and 1997/98 continues, there are grounds for hoping for a better balance between supply and demand.

2.4.3 *Financial relations between ginners and producers*

Aid is granted only to ginning firms applying for it, and having lodged a contract providing for payment to the producer of a price at least equal to the minimum institutional price. Among other things, the contract must include a clause providing that, should the abatement and aid increase mechanisms be applied, the agreed price will be adjusted as a function of the effect of the two mechanisms on the aid finally granted.

When unginned cotton is taken into supervised storage, the ginner makes an initial payment to the producer, taking account, of course, of the advances received. Consequently, where prices are concerned, the ginners pass on to producers the burden of uncertainty about the aid that will finally be granted at the end of the marketing year. Once they have collected the balance at the end of the year, the ginners make the second payment to the producers, which should enable them to ensure an overall payment corresponding to the minimum price, as provided for in the rules.

This two-stage payment of producers is a precautionary measure for the ginners. If they were to make a single payment, it might turn out at the end of the year to have been too high, but it would probably be difficult to recover the overpayment. At the same time, the advances on aid that exceeded the amount of aid finally due would be recovered from the 110% security. Moreover, it should be noted that for the period from 1 September to 15 October unginned cotton taken into supervised storage cannot immediately qualify for an advance.

The system of paying Community grants to ginners in two stages, an advance followed by the balance, has not had the same effect on behaviour in the cotton sector in the two Member States.

In Greece, ginners have in fact paid producers in two stages; the producers, dissatisfied with the first payment, have held on to the harvest of unginned cotton in the hope of better prices later in the year. This has affected the disposal of the harvest, and thus the rate at which cotton is taken into supervised storage. Consequently, the period of ginning in the strict sense has also been affected.

In Spain, the situation is different in view of the surplus capacity in the ginning industry in relation to the supply from producers. Against a background of competition, the ginners made a single payment to producers, for the 1996/97 marketing year at all events, which later turned out to be much higher than the final minimum price.

3. DIRECT PAYMENT TO PRODUCERS

3.1 Greece's request and the reasons behind it

While maintaining the principle of deficiency payments, and the grant of aid on the basis of the quantity produced, Greece would like to see the aid paid direct to the producers through the agency of **producer groups**, of which there are very few at present, but which could number about 300 to 400 to cover total output.

With such new arrangements for granting Community financing, which already exist for certain CMOs such as tobacco, the principle of the minimum price for producers could be maintained, this price being paid by the groups.

Besides collecting Community aid and paying member producers the minimum price, the producer groups would choose one of the following alternatives for marketing fibre.

a) Marketing by producer groups

Under this alternative, producer groups would own the fibre and would therefore be responsible for marketing it. In this situation, the groups could own ginning plants (possibly setting up a co-operative) or lease plant from the ginners, or subcontract the ginning of the cotton on their own account.

In the last two cases, the consideration paid to the ginners by the producer groups would consist either in a flat-rate amount applied to the quantity ginned (similar to a jobbing contract) or in a financial sum to cover the hire of the ginning plant.

This alternative would considerably weaken the importance of private ginners, who would become merely intermediaries with no commercial function. As for individual producers, their situation would be unchanged. In the short term, the Greek authorities consider that this alternative could concern 40% of total production through the intermediary of co-operatives. That is the reason for suggesting the second alternative.

B) Marketing by ginners

Under this alternative, the ginners own the fibre and remain responsible for marketing it, as in the present situation. However, instead of paying the minimum price, as at present, they would undertake to pay the producer organisations an amount corresponding to the difference between the minimum price and the aid. The Greek authorities would like this to be laid down as a legal requirement in a Community regulation.

One of the effects of changing the recipient of the aid would be to weaken the position of the ginning firms against the producers when negotiating contracts and prices. The Greek authorities would like to see a two-stage process, where alternatives (a) and (b) would co-exist in the first stage, until eventually all output could be absorbed under alternative (a), whereupon alternative (b) would be withdrawn.

3.2 Analysis of the proposed changes

Marketing of the fibre by the producer groups should lead to the following advantages for producers:

- it would provide an incentive to improve the structures of producer groups;
- producers who are direct recipients of aid should feel more responsibility for the level of total output, and thus for the penalties for overshooting the GNQ;
- direct payment of the Community grant without going through the ginners could speed up payment of the minimum price to producers;
- any profits from managing the aid could be passed on by the producer groups to their members.

However, if producer groups are to market fibre, they will have to take responsibility for applying not only for supervised storage, but also, and especially, for advances and for aid, which means dealing with post-fixing, since they will be the recipients of the aid. Moreover, the groups will also be subject to the constraint of lodging security for the advances they collect.

The problems of managing applications for supervised storage are exclusively practical matters of administration or shortage of infrastructure for weighing the cotton. However, the management of advances and aid (especially post-fixing) is a sensitive matter, since it requires not only a good knowledge of the world market but also, in certain cases, correct anticipation of world prices. To lodge security, moreover, bank facilities are required. The structure of producer groups in Greece and especially in Spain does not seem suitable, as they operate at present, to enable most of them to deal with these problems and constraints in the near future.

These arrangements would mean that production of unginned cotton would be monitored by the producer groups, since it is at this stage that cotton would be taken into supervised storage: there would then be 300 to 400 checkpoints, instead of only 90 at present. However, ginned cotton would need to be checked at the ginning stage, and this check on the quantity of fibres would remain essential since the aid is granted for unginned cotton taken into supervised storage, adjusted for the fibre yield from ginning. Except for the producer groups constituted as ginning co-operatives, these twofold checks at two different stages of processing would clearly be more complicated than the present system.

If the producer groups were to market the ginned cotton (alternative (a)), they would be responsible for negotiating sales contracts for their fibre on the world market, and thus for finding potential customers.

If the combination and addition of the two mechanisms (applying for aid and negotiating fibre sales contracts on the world market) did not result in a price equal to 95% of the guide price, the producer groups would be unable to pay their members the minimum price without endangering their financial viability.

If the ginners were to retain responsibility for marketing the fibre on the world market (alternative (b)), it seems inconsistent to grant to producer groups aid that depends closely on fluctuations of world prices, which the producer groups do not have to cope with.

Moreover, this alternative would involve including a requirement in a Community regulation for the ginner to pay the producer group a certain price, corresponding to the difference between the minimum price and the aid. This would mean imposing a financial constraint on an operator that did not receive a Community grant. From a legal point of view, this requirement could be imposed provided the ginner still remained involved in the operation of the aid scheme.

The ginning process would still be a necessary condition for the granting of aid, since the quantity of unginned cotton eligible for aid would still be determined as a function of the fibre yield of ginning. Moreover, the ginner would still have the possibility of purchasing unginned Community cotton at a price close to the world market price, which would not be possible without a Community aid scheme.

From a practical point of view, however, this requirement would encounter a major problem, since the difference between the minimum price and the amount of aid varies throughout the marketing year. Consequently, the ginners would have to make continual adjustments to the price paid to the producer groups, which seems very complicated, especially when aid is post-fixed.

To determine the yield of ginning in such a system, the fibre produced by the ginners would have to be monitored. For the same reasons as those mentioned above in connection with financial constraints, there is no obstacle from the legal point of view to imposing such monitoring on an operator that does not receive a Community grant.

Under such a system, it is difficult to ensure monitoring or to impose penalties in cases of failure to comply with Community regulations. One idea might be to provide for national sanctions, or the introduction of a principle of approval of firms, which would then entail the possibility of withdrawing approval.

Against a background of monitoring and sanctions, ginners could turn to the purchase of raw unginned cotton from outside the Community.

3.3 Conclusions

In the light of the arguments, alternative (a), involving marketing of ginned cotton by the producer groups, could be advisable in some cases, but alternative (b) does not seem feasible.

Some producer groups set up as ginning co-operatives receive aid under the present arrangements in the way described as option (a) in that, as part of the co-operative sector, they market the fibre at present. In this capacity, the co-operative receives the aid, and consequently passes the minimum price on to its members.

However, it is unlikely that all the producer groups (and especially those still to be set up) will have adequate expertise to manage not only the system of applications for supervised storage, but also that of applications for advances and aid, and the actual sale of fibre on the world market. Not all producer groups will be able to join the alternative (a) scheme fully and immediately; some may reach a sufficient degree of organisation, but there is a risk that for others the financial attractions of being a direct recipient of aid may take precedence over the establishment of adequate and efficient infrastructure.

In Spain, the present low percentage of producers who are members of groups would also be a handicap for the establishment of this two-fold structure favoured by the Greek authorities.

On balance, it is suggested that the present arrangements for channelling aid through ginning undertakings as provided for in Protocol 4 should be maintained, to facilitate management and monitoring of the scheme. In this framework, Article 7 of Council Regulation (EC) No 1554/95 could be adapted. This Article provides at present that where a cotton ginning undertaking carries out ginning on behalf of an individual producer or a group of producers it must submit a statement giving details of the conditions under which the ginning is carried out and how the aid is passed on to the producers. The reference is to aid, not to the minimum price. The new Council rules could specify that, where aid is passed on to a producer group, that group must pay individual producers the minimum price to ensure compliance with the requirements for minimum prices referred to in the Protocol.

When the general operation of the cotton aid scheme is reviewed at a later stage, with the possibility of more substantial changes than those under consideration in this report, one option to consider will be that of fixed aid (per hectare or per tonne) paid direct to the producer without going through the intermediary of the groups. This option in the form in operation at present in the tobacco and olive oil sectors would eliminate the concept of minimum price, and all the problems related to the management of applications for aid, especially post-fixed aid. However, it might make producers' incomes highly variable, because of the volatility of the world price.

4. REGIONALISATION OF PENALTIES

4.1 Greece's request and the reasons behind it

Initially, Greece had asked for provision for sharing out the present guaranteed national quantity between the various producer regions.

Greece also wanted a clause similar to that granted to Germany in the framework of arrangements for oilseed crops, where the sanction applicable at national level and resulting from the stabiliser mechanism can be adjusted, at the request of the Member State concerned, to individual regions.

The purpose was to allow differentiated regional penalties as long as they were weighted to correspond to the overall national penalty. In this way, producers outside the traditional regions of production can be discouraged, while those in the traditional regions, where major investment has been made in the past, can be supported. Another purpose was to encourage the rotation of crops, and thus better environmental management of water reserves and better soil conservation.

As this first option could lead to major penalties for certain regions, the Greek authorities substantially changed their demands, and are now asking for individual production quotas to be fixed for each producer.

Under these new arrangements, production equivalent to the quota would be eligible for full aid, without any sanction, while production above the quota would receive no aid and would be remunerated on the free market.

Individual quotas would be fixed in the light of various criteria such as the area covered and the level of regional investment. They would be revised annually.

Logically, the sum of individual quotas should correspond to the guaranteed national quantity allocated to Greece at present (782 000 tonnes). The Greek authorities consider that this quantity should be increased, however.

4.2 Analysis of the proposed changes

4.2.1 Original proposal

If Greece's total GNQ were to be allocated between the regions, this would mean, as a function of the extent of overshoot, varying levels of abatement from one region to another, varying levels of aid, and consequently varying levels of minimum prices. It would therefore be essential to provide for different levels of advances on grants depending on forward estimates of production.

There would need to be a regional breakdown of the budgetary redistribution mechanism that operates when expenditure is below ECU 770 million.

These constraints would make the aid scheme complicated to manage. The reason they exist is that regional references relate to levels of output rather than to area. Moreover, a system of regional allocation as a function of levels of output might lead to transfers of production from one region to another.

4.2.2 *New proposal*

A system of individual quotas involves the same risk of transfer of production, but between producers rather than between regions. Moreover, problems similar to those besetting milk quotas or durum wheat quotas would probably arise: cumbersome management for individuals, and complex control procedures.

The aid scheme for durum wheat provided for individual entitlement related to area. Because of the major problems in applying the arrangements, the Council recently decided to repeal the system of individual entitlement by area, and to replace it with a system based on a guaranteed maximum area (GMA).

The problem of consistency arises when quotas are applied to individual producers but aid is granted to producer groups; the problem of controls also arises, in view of the clear risk of transfer of production between producers in the same group, or even between groups.

Annual reviews of individual quotas on the basis of allocation criteria that are not, at this stage, very clearly defined only add a further complication.

Individual allocation of production would mean having two categories of cotton: grant-aided cotton and non-grant-aided cotton, at the level of the producer and at the level of the ginner. It would not be easy to monitor the system, and each operator would need to keep separate accounts for the two categories of cotton. Moreover, the present system of adjusting quantities of eligible unginned cotton up or down as a function of the fibre yield of ginning would no longer be efficient in certain cases, since the upward adjustment could not be applied when it led to a quantity in excess of the quota granted.

These arrangements with two categories of cotton, one eligible for full aid with no sanction, and the other without any aid, also imply a considerable change in the scheme, since it would no longer be necessary to estimate production or to pay advances and balances.

4.3 Conclusions

The initial option involving regional allocation of the GNQ leads to complications in the management and control of the aid scheme. It would inevitably give rise to differing levels of support and remuneration from one region to another. It might also lead to the transfer of production between regions.

In the light of the arguments set out above, the option of individual quotas allocated annually can be rejected completely; it would increase the complexity of control measures, thus weakening their effectiveness, against the wishes of the Court of Auditors, the Council and Parliament.

A simpler way of avoiding the expansion of cotton-growing throughout Greece could be partially based on the present model for durum wheat. This would involve defining areas of traditional production, where the aid scheme would be fully applicable, and other areas where no support would be provided.

If such a scheme were to be adopted, it should be based on stricter controls of areas sown to cotton and of area declarations accompanying the cotton supplied to ginning undertakings. Complications would therefore be introduced whatever solution was adopted. The introduction of these provisions would mean adjusting the basic rules.

To allow some regionalisation while avoiding the undesirable transfer of production between regions, the solution would be to adapt support as a function of area. However, this alternative does not correspond to the model which the Greek authorities would like; moreover, it cannot be adopted without changing the basic principles of the present scheme.

In Spain, the concept of regionalisation of penalties clearly does not have the same implications, since Spanish cotton production is concentrated in Andalusia, which usually accounts for 95% of output.

5. ESTIMATED PRODUCTION

The Greek authorities take the view, with reason, that their third and fourth suggestions are no longer relevant in view of their new request for regionalisation of sanctions (individual quotas). This is because the abatement and consequent sanction would no longer apply, which would preclude the need to estimate production as a basis for calculating advances.

We do nevertheless consider the last two points, which are difficult to deal with separately, since they relate to the detailed rules for paying advances.

5.1 Greece's request and the reasons behind it

Greece's original suggestion was to allow more flexibility in the two parameters influencing the calculation of advances. This involved providing a legal framework for revising the estimated production in the course of the year, and reducing the percentage for the safety margin added to estimated production from 15% to 7.5%.

Greece suggested revising the production estimates at the latest during the last ten days of October, with the possibility, where necessary, of revising the figures upwards.

The main purpose is to obtain, during the course of the marketing year, an estimate as close as possible to actual final output, so as to grant aid recipients prior remuneration as close as possible to their definitive entitlement.

5.2 Analysis of the proposed changes

Revising estimates of production during the course of the year (if it revises the original figures downwards) and applying a smaller margin of safety (7.5%) contributes to reducing the difference between the provisional and the definitive abatement. Advances are thus larger in the course of the marketing year, and the balance to be paid at the end is smaller.

This means that recipients of advances can pass on the payment of the minimum price to producers more rapidly, especially if the recipients are producer groups, as suggested by the Greek authorities.

However, if the safety margin added to the first estimation, made before the beginning of the year, is only 7.5%, the budgetary risk is appreciable, since the advances granted might turn out to be higher than aid finally due.

Ginning activity is in full swing by the end of October, and revised estimates of final production would still be fairly unreliable. A safety margin of only 7.5% would entail an unacceptable budgetary risk. The 15% margin should be retained, even for the revised estimate, which would reduce the impact of the revision on the new advances.

Under these arrangements, aid recipients would receive:

- from 16 October, an advance linked to the initial estimate of production, increased by a safety margin of 15% (estimate made before the beginning of the marketing year),

- from early November, a further advance (not much higher) based on the revised estimate of production, still with a 15% safety margin and including a small retroactive component linked to the earlier advance,

- the balance at the end of the marketing year.

However, this series of payments of different amounts is a source of complications that is very likely to lead to administrative errors for the sake of what in most cases will be a very small adjustment to the advance.

5.3 Conclusions

To reduce the budgetary risk to a minimum, it might be advisable to calculate advances in two stages:

- in the first stage, the initial estimate of production made before the beginning of the marketing year could be kept, with the safety margin of 15%

– in the second stage, the estimate could be revised at the end of November, i.e. well into the period during which the bulk of the cotton is taken into supervised storage; as this estimate would be more reliable, a smaller safety margin could be applied.

By postponing the revised estimate of production until the end of November, the conditions of remuneration of operators are improved both in Greece and Spain, without risk for the budget. The complications resulting from the payment of two advances still remain, however.

To avoid the payment of several advances, with all the resulting administrative complications, it would be better to pay one advance from 16 December, instead of 16 October as at present, on the basis of the estimate of production made at the end of November increased by a safety margin of less than 15%.

These changes would require amendment of Council Regulation (EC) No 1554/95 laying down the general rules for the system of aid for cotton.

6. GENERAL CONCLUSIONS

The main purpose of this report is to enable the Council to grasp the implications of the four changes suggested by the Greek authorities, in relation to the present system, with all the other present arrangements for the cotton aid scheme remaining constant.

Other changes to the scheme might be considered with a view to involving producers more directly in the granting of Community aid. However, any such changes would be radical, implying an approach based on flat-rate aid (per hectare or per tonne); they would substantially increase the variability of incomes dependent on market prices, and imply tighter controls of the quality and quantity of output. Such options could be considered when the general operation of the scheme is reviewed; a report on the scheme as a whole is to be sent to the Council and to Parliament by 1 August 1999.

For the granting of aid to producer groups, their present structure in both Greece and Spain does not seem likely to enable most of them to cope immediately with the constraints that inevitably fall on the recipient of aid in terms of management of taking into supervised storage, advances and aid itself.

Under the alternative where ginners would be responsible for marketing the fibre downstream of receipt of aid by the producer groups, there would be a corresponding obligation to pay a certain price to the producer group. This alternative is not to be recommended, since it would raise problems of control and sanctions, but also of consistency in relation to the basic principle of the deficiency payment.

Encouragement could be given to the other alternative, where the producer groups themselves would be responsible for marketing the fibre (in Greece this is already the case for producer groups set up as ginning co-operatives). There is already a rule that cotton ginning undertakings which carry out ginning on behalf of an individual producer or a group of producers with them must pass aid on to the producers, and in that case it should be reinforced. In order to comply with the requirements concerning minimum prices laid down by the Protocol, the new Council Regulation could introduce an obligation for producer groups to pay a minimum price to their members. In those conditions, producer groups would avoid all the constraints related to the management of aid by the ginners. Moreover, producer groups carrying out ginning themselves would, as at present, continue to collect and manage the aid.

The introduction of a system of individual quotas to maintain cultivation in the traditional production areas creates a number of monitoring and management problems that cannot be solved in a manner compatible with the principles of the present aid scheme. Regionalisation of the present guaranteed national quantity implies multiple levels of aid, and thus the problem of controlling the transfer of production between regions. However, one possibility that could be considered, based on the principle at present applied for durum wheat, would be for a Council Regulation to fix areas that are not traditional production areas, where the aid scheme would not apply.

As to the rules for the payment of advances, an improvement in production estimates requires revised estimates at a time when the main period of entry into supervised storage is usually well advanced (that is, towards the end of November). In this case, a safety margin of less than 15% could be applied to the revised estimate to calculate the advance on aid without creating budgetary risk. Moreover, to avoid the coexistence of several advances, and the resulting administrative complications, postponement for two months of the actual payment of advances should be considered. These changes involve amending the general rules laid down by the Council.

The conclusions of this report can therefore be summarised as follows:

- aid should continue to be granted to the ginning undertaking, whether a private undertaking or an association, and the possibilities for paying the minimum price when ginning is carried out on behalf of producer groups should be made explicit;

- the introduction of individual production quotas would not be a good idea, but the possibility of geographical concentration of eligibility for aid should be considered;

- it might be possible to consider a single advance payment calculated on the basis of a better estimate of production, which could then be increased by a margin smaller than the present 15%.

In the light of the Council's discussions of this report, the above suggestions could lead to proposals for legislation applicable to the forthcoming marketing year 1998/99. They do not, in themselves, involve any extra expenditure for the Community budget.

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