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Towards a sustainable European wine sector

IMPACT ASSESSMENT

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EXECUTIVE SUMMARY

To address the main problems affecting the EU wine sector, e.g., a structurally unbalanced market situation, the continuous decline in consumption, the progressive loss of competitiveness of the EU wine production, the complexity of the legal framework and the insufficient consideration of environmental concerns in the CMO, four alternative reform options have been considered:

Option 1: Status quo, with possibly some limited adjustments
Option 2: Profound reform of the CMO
Option 3: Reform along CAP reform lines
Option 4: Deregulation of the wine market

The expected impacts of the policy options are summarised as follows.

Option 1, slightly adjusting the existing CMO, would not achieve the objectives of the reform. The status quo appears unsustainable in the long term, because it does neither tackle the problem of the structural imbalance of the wine market, nor enhance the competitiveness of European wine nor improve the consistency with other Community policies.

Option 2, profound reform of the CMO, would address the problems of the wine sector in both the short and long term, by concentrating budgetary resources on measures to achieve **smooth and rapid stabilisation of the market** and the **structural adjustment of the sector**. Introducing national envelopes and transferring funds to rural development would leave Member States and wine regions scope to adapt the measures available at Community level to their specific conditions and needs, thus allowing greater subsidiarity.

Option 3, the general introduction of decoupled support for wine producers, would also allow **most policy objectives to be achieved in the long term**, in particular market equilibrium in the wine sector. Moreover, it would address environmental concerns, since it allows direct application of cross-compliance to the whole vine area. However, as in the case of complete deregulation, albeit to a lesser extent**, in the short and medium term the sector would undergo quite a tough adjustment process**. Public intervention would mainly focus on supporting farm incomes rather than rapidly improving the market balance by providing help with structural adjustment. Furthermore, an even distribution of public support to the whole vine area would raise problems of political acceptability and of overcompensation of quality wine producers.

Option 4, complete deregulation of the wine sector, would **achieve a certain number of policy objectives in the long term**, in particular wine market equilibrium and increased competitiveness of wine production. However, the serious adjustment that immediate implementation of this policy would require and the lack of structural measures accompanying this process would produce **severe, negative short-term impacts** on the sector and the rural economy of the regions concerned as a whole.

1. PROCEDURAL ISSUES AND CONSULTATION OF INTERESTED PARTIES

Work on this impact assessment on the reform of the Common Market Organisation (CMO) in wine was carried out by an Inter-Service Steering Group (ISG) of the European Commission set up for the purpose in December 2005, and whose mandate is given in Annex 1. The Group was led by Directorate General for Agriculture and Rural Development (DG AGRI).

All Directorates-General (DGs) of the European Commission were invited to participate in the work of the Group, and the following DGs were actively involved in the exercise: the Secretariat-General (SG), Health and Consumer Protection (SANCO), Trade (TRADE), Environment (ENV), Budget (BUDG), Regional Policy (REGIO), Economic and Financial Affairs (ECFIN), the European Anti-Fraud Office (OLAF), Eurostat (ESTAT), and the Joint Research Centre (JRC).

The impact assessment work was carried out in the period December 2005 to April 2006, during which time the ISG held several meetings. Firstly, the current situation of the wine sector was analysed in depth and the main problems of the CMO assessed. Secondly, the group identified the objectives of the wine regime and alternative policy options to achieve those objectives. Lastly, the impacts of the policy options were carefully evaluated. During this process, the ideas formulated by different stakeholders were also taken into account.

To give stakeholders an opportunity to put forward their opinions and ideas on the present situation and future prospects of the wine sector, a seminar, “Challenges and opportunities for European wines”, was held on 16 February 2006. This seminar was attended by more than one hundred people[1] representing a wide range of interested parties, in addition to the members of the ISG. The discussion was structured in three workshops dealing with the following subjects:

1. How to strengthen European wine’s competitiveness in the EU and worldwide?
2. How to achieve a sustainable European wine policy? The contribution of European vineyards now and in the future;
3. European wines and consumers.

In a rich and fruitful debate, stakeholders largely agreed on the preliminary analysis of the current situation and the mid-term forecasts for the European wine sector by the Commission (see Annex 2). Furthermore, there was consensus on the need to keep a specific CMO for wine, but to reform it, in order to find solutions to the difficulties experienced by the sector[2].

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[1] The list of participants to the wine seminar is available on the European Commission website: http://europa.eu.int/comm/agriculture/capreform/wine/sem_participants.pdf.

[2] The conclusions of the wine seminar “Challenges and opportunities for European wines” are on the webpage: http://europa.eu.int/comm/agriculture/capreform/wine/sem_concl_en.pdf.

In addition to the seminar of 16 February 2006, the Advisory Group on Wine discussed the potential reform scenarios and many bilateral meetings were held between a wide range of stakeholders and the relevant Commission departments.

The Committee of Professional Agricultural Organisations and the General Confederation of Agricultural Co-operatives in the EU (COPA/COGECA) presented a position paper on the wine sector reform on 1 February 2006. They are in favour of a revision of the wine CMO, which should encourage strong economic organisation of the sector based on three main concepts: verticality, co-responsibility and conditionality (mainly to link EU financing and production control).

The "Comité européen des entreprises vins" (representing trade and industry in the wine sector) is in favour of a fully-fledged “wine policy” and in-depth reform of the present instruments. In particular:

– it favours the abolition of the planting ban after 2010.
– it wants to allow table wines without a geographical indication to state the grape variety and vintage year on the label.

Owing to the extreme complexity of the wine sector and to the close interrelationships between single issues, this analysis could not always address all impacts in a quantitative way. This impact assessment remains thus partly qualitative.

Table 1 – Principal features of the wine economy in the European Union

	Year	Volume/Value	Trend ↗↘
Wine production value as % of the value of EU-25 agriculture	2004	5.4%	
Production EU-25[3]	2005/2006	166 million hl	→
of which EU-15		*160 million hl*	
Production EU-15	Average of 2000/2001 to 2005/2006	163 million hl	
As % of world production		*60%*	
of which:			
France		*52 million hl*	
Italy		*50 million hl*	
Spain		*38 million hl*	
Consumption	2004/2005	131 million hl	↘
Per capita per year, of which:		28.7 l	
table wine		*13.9 l*	
quality wine		*12.9 l*	↗
non-EU wine		*1.8 l*	
Trade			
World production being involved in	2004	26%	
World trade, of which:	2004	76 million hl	
intra-EU trade		*48%*	
Imported into EU	Aver. 2003–2005	11.3 million hl	↗↗
Exported by EU	Aver. 2003–2005	12.2 million hl	→
Prices			
Average value import (value/volume)	2005	€ 207 /hl	↘
Average value export (value/volume)	2005	€ 351 /hl	
Area EU 25 [4]	2000 (2003)	3.4 million ha	→
As % of total UAA of EU		*2.2%*	
As % of world vine area[5]		*47%*	
Number of farms in EU 25	2000 (2003)	1.5 million	↘
As % of all EU-25 farms		*15%*	
Average area (all wine farms) EU-25	2003	9.2 ha	↗
Of which vine area:		*2.3 ha*	
Area under table wine for table wine specialists[6]		*1.3 ha*	
Area under quality wine for quality wine specialists[7]		*3.7 ha*	
EAGGF Budget for all vine/wine products	Budget	€ 1 228 million	↗
As % of the EAGGF guarantee (Title 5)	2005	*2.3%*	

3 Provisional data for 2005/2006.

4 Source: farm structure survey 2000 (2003 for some new Member States).

5 World vine area statistics include table grape vines.

6 Source: available data for FR, ES, IT, MT, EL, PT, and SI.

7 Source: available data for FR, ES, IT, MT, EL, PT, and SI.

2. PROBLEM DEFINITION

2.1. Economy of the sector[8]

The **European wine sector** is the largest in the world. The EU is the **world's leading wine producer** (45% of vine areas and 60% of wine production), the **biggest consumer** (60%) and the **main actor in the international trade** (both the top exporter and the top importer). France, Italy and Spain, which together account for more than 80% of the EU production, are the three most important wine-producing countries in the world.

The wine sector in the EU is composed of 1.5 million holdings (16% of all agricultural farms), utilising a vine area of 3.4 million ha (2% of the total agricultural area) and employing 1.5 million annual working units (15% of agricultural work). In 2004, wine production totalled € 17.4 billion, which represents 5.4% of agricultural output.

Wine production plays a primary role in the agricultural activity of most wine-producing Member States: it represents around 10% of the value of agricultural production in France, Italy, Austria, Portugal, Luxembourg and Slovenia, and a little less in Spain. The importance of wine production in economic activity is even greater at regional and local level: for certain regions the value of wine production exceeds 20% or even 30% of total agricultural production; the percentages can be even higher, when considering more restricted geographical areas.

In addition, for most wine-producing Member States, wine is one of their most valuable export commodities, both for the agricultural sector and for the economy in general. For those countries, therefore, wine contributes significantly to the trade balance.

For many decades now, the European wine market has suffered of **recurrent overproduction problems**, although the scale of the imbalance (or at least its perceived scale) has risen and fallen over time. During this period, there has sometimes been uncertainty about the structural nature of the market imbalance of the wine sector, mainly because production typically varies significantly from year to year, depending on weather conditions.

Since 1975/76, the problem of overproduction has been addressed by means of a policy of limiting production potential, with a ban on new plantations and an incentive for the permanent abandonment of production through a grubbing-up premium. Those instruments contributed to a substantial decrease in EU vine areas over the period (from 4.5 million ha in 1976 to 3.2 million ha before the last EU enlargement). The reduction of vine areas, combined with a substantial stability of yields per hectare, led to a decline of the total wine production[9] until the mid 90's. In the last five wine years the total production varied between 166 and 196 million hl for the EU-25.

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[8] More details on the economy of the wine sector can be found in the corresponding report published in March 2006: http://europa.eu.int/comm/agriculture/markets/wine/studies/rep_econ2006_en.pdf.

[9] Total wine production = vinified production + production of grape musts and juices.

However, the decrease in vine areas was mitigated, from 1996 onwards, by a restrictive application of the grubbing-up scheme and, following the last reform of the wine CMO in 1999, by the introduction of new planting rights. Furthermore, wine production recently felt the effects of a trend towards increasing yields in certain wine regions, notably in Spain, mainly due to the more widespread use of irrigation.

Within this general trend, the share of quality wines psr in total EU wine production has been increasing, and has currently almost equalled that of table wines.

Wine consumption in Europe has seen a significant and continuous decline in recent decades, by an average of 750 000 hl (–0.65%) per year, or 15 million hl (–11%), in the last twenty years. This tendency is the combined result of a sharp fall in consumption (–2% per year) in the traditional wine-producing Member States (in particular France and Italy), where the level of per capita consumption is higher, and a modest increase in the other countries. The falling trend in the consumption has particularly affected table wine, whereas the consumption of quality wine psr is growing. Currently, the total consumption in the EU-25 stands at approximately 130 million hl, almost equally shared between table wine and quality wine.

For other outlets for wine production (grape juices, liqueur wines, brandies, vinegar and aromatic wines), consumption has generally been stable.

Imports of wine from non-EU countries into the Community have experienced extraordinary growth during the past decade: while they played only a marginal role until ten years ago, they are now substantial, having gained considerable market shares at the expense of domestic wines. The reasons for this trend are, on the one hand, the strong development of the wine sector in many countries of the so-called "new world", in particular Australia, Chile, South Africa and the United States, and, on the other hand, the entry into force of the **Uruguay Round agreement of 1995**, which has profoundly changed trade arrangements. In particular, the abolition of a minimum price for imports (the reference price) has considerably reduced the degree of border protection. In conclusion, since 1996, the volume of wine imports into the EU-15 has been constantly growing at a yearly rate of 10%, reaching almost 12 million hl in 2004.

In the last ten years, the volume of **wine exported** from the Community to non-EU countries has been stagnant, and in 2004 it stood at about 13 million hl. On the other hand, the unit price of exports has increased compared to ten years ago; therefore, at least the value of exports grew.

Analysis of the most recent balance sheets for the wine sector in the EU-25 shows that **the sector systematically produces a surplus**. In the last six wine years (1999–2005), the average vinified production[10] per year in the EU-25 was 174.8 million hl and imports from non-EU countries 9.1 million hl. By contrast, wine consumption was 132.1 million hl; other uses[11] accounted for the equivalent of 16.1 million hl of wine and exports amounted to 11.5 million hl. Therefore, over the last six wine years, wine production has generated on average a yearly surplus of 24.0 million hl wine, or 13.8% of the production. If the volumes distilled under the scheme

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[10] The vinified production does not include grape musts and juices.

[11] other uses = brandies, liqueur wines, vinegar, aromatic wines and distillation of by-products (the last one being considered as a quality measure).

supporting the production of potable alcohol (on average 11.4 million hl) are regarded as a market outlet of the wine production, although financed by the Community, then the average annual surplus still stands at 12.7 million hl (7.2% of production). This excess volume had to be removed from the market at the expense of the Community budget under specific distillation measures, or it accumulated in private stocks, thus contributing to depressing the wine market situation, and in particular prices.
The problem of surpluses is particularly serious for table wine, but according to the most recent indications, the situation has deteriorated even for quality wines psr (in 2005 and 2006, five Member States requested crisis distillation specifically for quality wine).

The high level of surpluses has led to serious **stockpiling** and lower **market prices,** particularly since the abundant harvest of 2004.

The future **enlargement of the Union to Bulgaria and Romania** will have significant implications for the wine sector, since they are two of the most important wine-producing countries of Central and Eastern Europe, with a joint vinified production of almost 8 million hl on average.

Assuming an unchanged CMO and based on the expected trends in production, consumption and in trade dynamics, the DG AGRI **mid-term outlook for the EU-27 wine sector** to the wine year 2010/2011 is that the wine surplus will increase to 27 million hl (15.1% of production), or to 15 million hl (8.4% of production) if wine subject to distillation to support the potable alcohol sector is excluded. The differential surplus generated by the two acceding countries is estimated to be 0.5 million hl.
That outlook is for a "normal" year (that is, damping yearly fluctuations in yields) and is based on "average" assumptions.

2.2. The existing common market organisation in wine[12]

The common organisation of the wine market is one of the largest and most complex common market organisations in the common agricultural policy. This is because it covers not only the issues that many market organisations deal with, such as price, intervention and trade, but also issues specific to the wine industry (provisions concerning the production, transport and processing of wine products and wine-making practices).

Community legislation divides wines into two major categories: "**quality wine produced in specified regions**", also known as "quality wine psr" (QWpsr), and "**table wines**" (TW), this category including table wines with and without geographical indications. However, it is the responsibility of the Member States to decide on the definition of quality wine psr, which has resulted in different approaches to classifying wines among the different Member States: Germany, Luxembourg, and to a certain extent the United Kingdom and Austria have opted to classify almost all manufactured wines as quality wine psr, whereas the other Member States have a much stricter approach. This classification does not necessarily reflect the quality of the wines, particularly as some table wines, such as those with a geographical indication (*vins de*

[12] More details on the wine CMO can be found in the corresponding report published in March 2006: http://europa.eu.int/comm/agriculture/markets/wine/studies/rep_cmo2006_en.pdf.

pays, indicazione geografica tipica, vino de la tierra, Landwein, etc.) can rival top class wines in terms of price and quality, whereas some quality wines psr face disposal difficulties and are consequently sold at lower prices on the market. The majority of the market measures provided for by the common organisation of the wine market concern table wines. For instance, QWpsr does not benefit from any export refund. On the other hand, QWpsr is protected by designation of origin (at least inside the EU).

Measures taken by the market organisation can be grouped in three major categories:

- measures concerning production potential,
- market measures,
- regulatory measures.

Measures concerning production potential

The limitation of the production potential is essentially achieved using two types of measure:

- **a ban on new plantings** (apart from newly created planting rights) and time restrictions on replanting rights (eight years);
- a premium system for the **permanent abandonment of wine-growing areas**. This measure achieved a substantial reduction in the wine-growing potential of the Union. Since 1996, the impact of this measure has diminished considerably following a change in the Regulation decided by the Council, allowing Member States to exclude part or all of their territory from the system. In recent years, less than 2 000 hectares per year have been definitively grubbed up, whereas at the peak of the system, close to 56 000 hectares per year were affected. Moreover, under the 1999 reform 51 000 hectares of new planting rights were granted;
- a programme of **restructuring and conversion of vineyards**. The aim of the measure is to adapt production to market demand, to accelerate structural improvement and strengthen competitiveness, by replacing low-quality vines with better quality vineyards and/or improving vineyard management techniques.

Market measures

Under the common organisation of the wine market, **distillation** is the principal instrument of intervention. The aim of distillation is to withdraw production surpluses from the market at a guaranteed minimum price. The wine is then processed into alcohol, which is intended partly for the potable alcohol market, with the remainder intended for the fuel market. Since the 1999 reform, Community legislation has provided for four different forms of distillation, two of which are compulsory for producers and two voluntary. The purchase price of wine for distillation varies from one type of distillation to the other.

- Compulsory distillation of "**by-products** of wine-making" aims to ensure the quality of wines preventing overpressing of grape marc and wine lees (this is why the by-products of wine-making sent for distillation must have a minimum alcohol content);
- the second compulsory distillation concerns wines with a so-called **“dual purpose**", mainly Charentes wine, which, beyond a certain quantity, must be distilled;

- **potable alcohol distillation** (optional for producers) aims to support the market in wines intended for this type of traditional processing;
- **crisis distillation** (optional), may be allowed when there is a serious disturbance of the market.

A large part of the alcohol produced by distilling the by-products of wine-making and of wines with dual classification, together wit the entire alcohol of crisis distillation, enters Community public stocks and is disposed of in the EU biofuels sector or for industrial use. For a long time it was exported for use as fuel in non-EU countries. In April 2006, there were 2.5 million hl of alcohol in public storage.

Other measures provide for a **private storage** system for wine, **aid for the use of grape musts for enrichment and for the production of grape juices,** and **export refunds** for table wine and must.

Regulatory measures

These concern provisions on **wine-making** (**or oenological**) **practices**, on **quality policy** and the protection of **geographical indications, and labelling rules**.

Wine-making practices (WMP) are the set of technical practices authorized for the production of wine from grapes. They apply directly to wine producers. They are intended to ensure the conformity of the final product and to maintain the quality of the product put on the market, thus protecting consumers against frauds and health risks.

Among WMP, **enrichment** plays an important role. This practice increases the natural alcoholic strength of wine. It is carried out by adding either sucrose ("**chaptalisation**") or concentrated grape must.

Chaptalisation is a traditional technique in a large number of wine-growing regions of the north-central and eastern regions of the Community. Elsewhere, this practice is prohibited, and only grape sugar (concentrated must) may be used for enrichment.

Given that chaptalisation costs approximately one third as much as enrichment through concentrated grape must, in order to prevent producers from southern Member States from being penalised by Community rules, support for the use of concentrated must and rectified concentrated must to increase the alcoholic strength of wine was introduced.

The aid for grape must for enrichment, in addition to the direct cost for the budget, has led to an artificial expansion of enrichment (including in regions where the practice was never used before), to a reduction in the natural alcoholic strength necessary to obtain wine and consequently to an increase in yields and production throughout the Community.

Quality policy is intended to maintain a minimum quality standard for QWpsr and to encourage the production of such wines, without an uncontrollable expansion in the production. It also aims to harmonise the provisions of the Member States so as to establish conditions of fair competition in the Community. The protection of Geographical Indications (GI) is an instrument to reach the objectives the EU wine quality policy.

Wine labelling is a legacy from earlier legislation of Member States and has been developed outside the framework of horizontal Community labelling legislation. The objectives of this legislation are to protect the legitimate interests of consumers and producers, to ensure the smooth functioning of the EU Internal Market, to promote the production of quality products and to improve the transparency, openness and clarity of the regulatory discipline of the wine market.

Budgetary expenditure for the common organisation of the wine market mainly concerns table wine. Expenditure varies markedly from year to year due to changes in production conditions and represents between 2.5% and 5.5% of the total expenditure of the EAGGF Guarantee Section. 2005 expenditure amounted to € 1 269 million, distributed as follows:

- 40% represents the direct and indirect costs of the various forms of distillation, primarily distillation proper (€ 321 million) followed by the cost of alcohol in public stocks of three of the four forms of distillation (€ 185 million);
- 35% represents expected expenditure on the restructuring programme in place since 2000 (€ 446 million);
- support for enrichment by means of aid for must accounts for 16% (€ 198 million);
- the remainder is divided between private storage of wines and musts (5%, or € 70 million), export refunds (1%, or € 17 million) and the definitive grubbing-up of vineyards (a measure up to now used less and less by the Member States), which should only cost € 31 million (in 1993 the figure was in excess of € 400 million), less than 2% of expenditure on market organisation.

The budget for 2006 is € 1 494 million, a figure composed of significant expenditure on crisis distillation decided in 2005 after the abundant 2004 harvest, to which the distillations planned for the 2005 harvest must be added.

In addition, it should be pointed out that, like other sectors, wine producers benefit from agri-environmental measures and other structural measures to support rural development, although the wine sector may not in the past have used all the opportunities offered by the EU's rural development policy, opting instead to use intervention and market measures.

2.3. Strengths and weaknesses of the wine sector

Europe can be rightly considered as the birthplace of wine-making. Vine cultivation and wine-making have a millenary tradition: they have been carried out since ancient times, and have constantly been associated with the cultural values that accompanied the development of European civilisation. With such a long history, a considerable amount of technical knowledge and expertise has been developed.

European wines have a widespread reputation and are renowned for their **quality, authenticity and tradition**: geographical indications such as Champagne, Bordeaux, Rioja, Chianti, Porto, Tokaj, etc. are very well known tokens of high-quality wine all over the world.

The European Union represents by far the **major player** on the world wine market. The latest accession of the ten new Member States in 2004 further consolidated the EU's leadership, and the enlarged internal market guarantees new valuable prospects for the exports of wine-producing countries.

Vine-growing represents a **high value-added activity**, which plays a key role in economic development, employment and the development of tourism (wine routes) in rural areas, particularly at regional and local level. Its positive contribution to the trade balance of wine-producing Member States is also notable.

A significant proportion of EU wine production is highly **competitive in the world market**, and does not have any difficulty in finding commercial outlets, either on the domestic market or for export to non-EU countries, even though the wine market is already quite open to global competition and the degree of border protection is very low.

Finally, vineyards are a feature of the landscape of many rural areas, thus contributing to the preservation of an **ancient cultural heritage**. Examples of these landscapes are typically found along the Danube and the Rhine, in the Rhone Valley, on the terraces of Le Cinque Terre (Liguria), in Friuli, along the Douro and beside the Lake Balaton.

However, the European wine sector increasingly faces serious difficulties:

1. the current market imbalance between supply and demand in the Community. Recent harvests have increased stocks significantly, leading to lower prices and great pressure for expensive intervention measures such as distillations.

2. a strong and steady decline in consumption over decades, resulting from shifts in social behaviours with regard to nutrition and lifestyle.

3. a loss of competitiveness against so-called “new world” wine-producing countries. This has led, particularly since the reduction in the level of border protection following the entry into force of the Uruguay Round agreement of 1995, to a progressive erosion of the market share of EU wines, both on the domestic and on export markets.

4. the complexity of the legal framework for wine policy, which constrains EU producers and further weakens the competitive position of the European wine sector.

5. the lack of attention paid for environmental concerns in the current CMO despite the pressures exerted by wine production.

In this respect, many CMO policy tools are probably not effective in achieving their objectives:

- the effect of the **ban of new plantings** on curbing production potential has been limited by the granting of new planting rights and by the increase in yields in some producing Member States. The existence of illicit / **irregular plantings** has also contributed to the production of surpluses. The use of the grubbing-up scheme has virtually stopped;
- the **restructuring scheme** has permitted a move to higher quality wine, but could also have led to an increase in yields;
- **distillations and other market tools**, normally designed to absorb conjunctural surpluses, encourage overproduction, thereby preventing market balance. Crisis distillation has been allowed in three out of five years since the beginning of the new CMO, and again this year. Furthermore, some of these measures are not efficient, as they are suspected of having significant deadweight effects;

- some provisions of the CMO have created a **heavy administrative burden** (for example in relation to the obligations in terms of wine movements and wine depot registers) and have not always been correctly implemented (**regularisation of unauthorised planting**);
- measures are often **too strict and not flexible enough** to allow efficiency and to adapt rapidly to new production techniques, and marketing methods. For example, limiting planting rights does not allow optimal adjustment of farm structures, whereas producers in non-EU countries are not subject to such restrictions. At the same time, the rigid rules on labelling and on wine-making practices hamper innovation;
- the present **dichotomy between table wines and "quality" wines** produced in specified regions no longer provides the appropriate framework to promote the concept of Geographical Indications for wines, both within and outside the EU. In addition to several thousands of QW psr, there are also several hundreds of "table wines with GI";
- **the labelling rules**, which are specific to wine, are characterised by the heterogeneity of legal instruments and the rigidity of certain rules, which in particular make it difficult to develop so-called "varietal wines" (*vins de cépage*) or state the vintage year outside a GI, and are regularly criticized by third countries. The rules seem in general to be more producer-oriented than consumer-oriented;
- several policy tools are currently **under pressure in the framework of the WTO:** this is the case for all market measures, which are categorised under the most trade-distorting support measures (amber box), and the export refunds, for which there has already been a commitment to phasing out under the current Doha Round negotiations. Even some other provisions have been challenged by our partners: the green box classification of the restructuring and reconversion programme, the classification of table wine and quality wine, some labelling rules, the ban on vinification of imported musts and the ban on blending Community and imported wine;
- although the 2003 CAP reform introduced the principle of **cross-compliance** for direct payments to agricultural producers, the wine sector is currently excluded from this general system. However, a significant part of the vine area is already covered by cross-compliance, since any wine producer receiving direct payments for areas other than vineyards is subject to cross-compliance for his whole farm (see section 5.3).

As wine is one of the products listed in Annex I, referring to Article 32, of the Treaty establishing the European Community, it is up to the Union to lay down rules for the establishment of the common market organisation, and therefore also to address the abovementioned problems.

3. OBJECTIVES

The reform of the wine sector is expected to contribute to the Lisbon Strategy and should ensure that wine production in the enlarged European Union is **competitive and sustainable, and driven by market demand**. In particular, the reformed CMO should achieve the following key objectives:

- to ensure a better quantitative and qualitative **balance between supply and demand**, by providing for simple and effective rules allowing structural adjustment of the sector, including a reduction of production potential where necessary;

- to enhance the **competitiveness** of European wine, by allowing the development of a modern and dynamic wine industry, capable of efficiently producing wine and marketing it on the internal and the world market, thus consolidating EU leadership in the sector;
- within the general objective of competitiveness, to preserve the **authenticity** and the traditional character of the **product,** and to safeguard vineyards in sensitive areas, where vine-growing plays an important role in protecting the environment/landscapes and providing employment in rural areas;
- to **simplify the legislation**, by allowing a more effective and flexible framework of rules for production and labelling. In particular, those rules should be consumer-oriented rather than producer-oriented;
- to take into consideration wider **society concerns**, such as **health and consumer protection** and **environmental matters**;
- to take into account the accomplishments of the CAP reform initiated in 2003, in particular its market orientation, its horizontal approach and cross-compliance;
- to fully respect our international obligations;
- to achieve a **higher degree of subsidiarity**, leaving to Member States as much scope as possible for national decisions, and allowing Community action where the objectives cannot be sufficiently achieved by Member States. This should enable Member States and wine regions to adapt the measures available at Community level to their precise conditions and needs, albeit under certain common rules in order to avoid distortion of competition;
- to provide for the **smooth integration of Bulgaria and Romania** into the EU wine market organisation, enhancing the process of modernisation and restructuring of their wine industries.

4. POLICY OPTIONS

Taking into account the preliminary analysis of the strengths and the weaknesses of the EU wine sector, the problems that have emerged with the existing wine CMO, and the objectives to be achieved by the EU wine policy, four alternative reform options have been identified.

4.1. Option 1: Status quo, with possibly some limited adjustments

This reform option consists in **maintaining most of the tools of the existing CMO**, with just some specific provisions to overcome the most important problems.

The tools for the management of **production potential** would be substantially kept in place:

– **the ban on new plantings** would be **extended beyond 2010**;

– the tool of **permanent abandonment** would be also kept as it is now, with scope for wider use by MS, if the market situation should require it;

– the policy of **restructuring and reconversion** of the vineyards would continue, possibly with some adjustments to overcome the current problems (stricter control that the measure is not used for normal renewal of vineyards and/or that it does not lead to increased yields; improvement of the monitoring tools put in place to assess the effectiveness of the scheme).

The **market measures**, in particular **distillations,** would continue to play their central role in the CMO:

– as far as the **distillation of by-products** is concerned, this practice would continue to be compulsory in MS currently using it, if they so wish;

– as for the **other distillation measures**, either the instruments would be kept as such, or some adjustments would be made to contain expenditure (e.g. a slight reduction in the distillation price for the potable alcohol scheme) or to link distillations to structural measures (e.g. possible mandatory link between crisis distillation and permanent abandonment);

– **private storage** and **aid for the production of grape juice** would be kept, if necessary introducing some slight improvements;

– **aid for use of grape musts for enrichment** would be maintained at the current level, despite the pressure to increase its level, due to the reduction in the beet sugar price. No changes would be proposed concerning the use of sucrose for enrichment;

– **export refunds** would be phased out in the framework of the WTO commitments.

The **regulatory measures** (wine-making practices, quality policy and the protection of geographical indications and labelling) would remain substantially unchanged.

4.2. <u>Option 2</u>: Profound reform of the CMO

This reform option provides for **in-depth revision of all the tools of the CMO**, from the pure and simple removal of the least effective ones, to the introduction of new coherent tools acting in synergy. Nevertheless, **the CMO would still preserve its specific character**.

Market intervention measures, and in particular distillations, are suspected, despite their cost, to have been ineffective in reducing the structural surpluses of wine production in the long run. Therefore, one could envisage shifting the emphasis from that kind of tools to structural measures aiming at establishing market balance.

Since recurrent production surpluses are a feature of the wine market, **the tools for limiting the production potential would be kept in place and reinforced**:

– extension of the **ban on new plantings** for a few years beyond 2010; however, once the situation of the wine market improved and reached equilibrium, the ban would be lifted;

– strengthening of **permanent abandonment** scheme, in order to reduce global production potential, particularly that of vineyards that do not have a market outlet to match their production volume. For wine producers grubbing-up their vineyards direct income support would be provided through the granting of Single Payment Scheme entitlements;

– continuation of the **restructuring and reconversion** scheme for vineyards possibly with the improvements referred to under option 1). The need for restructuring should be carefully verified, and, if appropriate, the budgetary amounts allocated for to this measure could be reduced, with the corresponding funds being used for other measures in the national envelope (see below) or transferred to the rural development. Lastly, a link between the restructuring scheme and permanent abandonment could be established, in the sense that higher envelopes could be awarded to Member States making the biggest efforts in terms of grubbing-up policy.

All **market measures**, and in particular **distillations**, would be in general abolished:

– the **distillation of by-products** could be made voluntary for wine producers (but with no financial support from the Community), even though **the prohibition on overpressing marc and lees** (with the 10% limit of minimum alcohol content) **would be maintained** under WMP rules;

– **crisis distillation** would be abolished, or replaced by an alternative safety net mechanism[13] using a national envelope;

– dual-purpose grape distillation and potable alcohol distillation, together with private storage and must aid would be completely abolished;

– in order to guarantee fair competition between EU producers, in tandem with the abolition of the support for must, a **more restrictive approach to using sucrose** for enrichment should be adopted. The proposed restriction would consist in a complete ban on the use of sucrose;

– **export refunds** could be abolished in connection with the WTO commitments, possibly in favour of promotion, information and education measures.

The part of the current budget for market measures not earmarked for permanent abandonment would be distributed in the form of **a national envelope** or **transferred to the second pillar** as an additional envelope for wine-producing Member States and regions.

The national envelope could be used, in keeping with greater subsidiarity, for a certain number of eligible measures, subject to certain common rules in order to keep them consistent with the objectives of the reform and to avoid distortion of competition. Possible measures contained in the envelope would be, for example:

– the restructuring and reconversion scheme,
– tools providing support for safety-net mechanisms (aid for the administrative set-up costs of a sector-specific mutual fund, instruments to alleviate natural disasters, basic coverage against income crises, etc.),
– support for green harvesting.

The funds shifted to the second pillar would provide additional resources for rural development policy in the wine regions, as was the case for the reform of the tobacco sector, for example to strengthen early retirement measures for wine producers or to reinforce the agro-environmental dimension of vine-growing, for example introducing a cultural landscape payment for vine areas

[13] Communication from the Commission to the Council on risk and crisis management in agriculture, COM(2005) 74 final.

with a specific and recognised environmental/landscape value, which could otherwise be endangered, or funding environmentally-friendly production methods, such as organic and integrated crop management (ICM).

For **wine-making practices**, apart from the problem of enrichment, which was already analysed in connection with the market measures, the following amendments would be proposed:

- simplifying the process of approval of wine-making practices through the transfer of competence from the Council to the Commission,
- recognising OIV (International Organisation of Vine and Wine) practices, with filtering at Commission level for their incorporation into Commission regulation,
- authorising wine-making practices for export to countries accepting them;
- ending the ban on vinification of imported musts and on blending Community wines with non-EU wines

A **geographical indication (GI)** system, specific to the wine, would be kept; however, this system would be improved making it more consistent with the general system of Protected Geographical Indications and Protected Designation of Origin (PGI/PDO) and aligning it to the provisions of the WTO-TRIPS agreement. This could entail a revision of the EU classification system for wines.

Finally, **labelling rules** should be simplified by creating a single legal framework for all the different categories of wine, thereby making labelling policy more flexible and adapted to the needs of consumers. Closer links to horizontal rules on compulsory particulars could also be envisaged.

A possible variant of option 2, 'Profound reform of the CMO' could be a more resolute approach, lifting the ban of new plantings immediately, together with market measures. As a consequence, the grubbing-up programme would be abolished, and the whole budget would be transferred either to the national envelope or as an additional envelope to rural development measures in wine-producing Member States and regions. Compared to the basic option, this variant would tend to require harsher adjustment efforts for the wine sector, since it contains some pronounced aspects of deregulation. However, with respect to the option 4 mentioned below, the impacts of this variant would be much more mitigated, due to the availability of considerable budgetary resources through the national envelope and the reinforced rural development policy for restructuring the sector.

4.3. Option 3: Reform along CAP reform lines

This reform option provides for the **integration of the wine sector in the mainstream CAP,** as reformed since 2003. **The entire budget for the wine sector would be converted into Single Payment Scheme (SPS) reference amounts** to be distributed on a hectare basis. **Vines would be made eligible for the activation of SPS entitlements and would be subject to the general system of cross-compliance, modulation and financial discipline**.

The **ban on new plantings** would be extended for a few years beyond 2010 as under option 2, however, once the situation of the wine market improved and reached equilibrium, the ban would be lifted. The **policy of permanent grubbing-up of vineyards** would be largely abandoned and the **envelope for the restructuring** scheme would be **transferred to the budget for the SPS**.

All **market measures** would be in abolished and the budgets for them redistributed under the SPS.

In tandem with the abolition of the aid to must, **the use of sucrose** for enrichment would be prohibited, as in option 2.

For **regulatory measures** (wine-making practices, quality policy and protection of geographical indications and labelling), the same approach would be followed as in option 2.

4.4. Option 4: Deregulation of the wine market

The option of deregulation would entail the immediate **abolition of all policy instruments** for the management of production potential and the market measures.

In other words, the tools for managing the **production potential** (the ban on new plantings and permanent abandonment) and the policy of **restructuring and reconversion within the CMO,** together with **all market** measures, would be immediately abolished, thus leading to complete deregulation of the sector.

The budget would be either suppressed or transferred to the second pillar for Rural Development policy in general.

Wine-making practices would no longer be dealt with at EU level, OIV rules being the only regulatory framework. **The use of sucrose** for enrichment would be nevertheless kept as it is in the present CMO.

For **geographical indications** and **labelling rules**, the current system would be completely integrated in horizontal schemes (respectively the PDO/PGI system and the horizontal directive on the labelling of foodstuffs).

Table 2: Summary table of the policy options

WINE REFORM	Potential			Market measures								Regulatory mesures		
Options	**Ban of new plantings**	**Permanent abandonment (grubbing-up)**	**Restruct. of vineyards**	**By-products distillation**	**Dual purposes distillation**	**Potable alcohol distillation**	**Crisis distillation**	**Private storage**	**Aid to grape juice**	**Aid to musts (enrichment)**	**Export refunds**	**Wine-making practices**	**Quality policy, GI protection**	**Labelling**
<u>Option 1</u>: Status quo with limited adjustments	Prolongation	Maintained	Maintained, improved monitoring	Maintained	Maintained	Maintained, possibly with reduction of price	Maintained, possibly with links with grubbing-up	Maintained	Maintained	Maintained (despite pression from sugar price)	Phasing out according WTO commitments	no substantial change	no substantial change	no substanti change
<u>Option 2</u>: Profound reform of CMO	Extension for a few years	Important strengthening	Maintained, link with grubbing-up. Possible reduction of envelope with shift to national envelope or 2nd pillar	Abolition - budget replaced by national envelopes or shifted to 2nd pillar for wine regions + maintaining prohibition on overpressing						+ ban on the use of sucrose	Abolition and replacement through promotion and information measures	Competence to the Commission, link to OIV practices, special practices for export, end of ban for imported musts	Simplification, alignment on WTO-TRIPS and on PGI/PDO system, revision of wine classification system	Competence Commissior unique tools all wines, mc flexibility
<u>Option 3</u>: Reform along CAP reform lines	Extension for a few years	Abolition	Conversion of budget into SPS reference amounts	+ maintaining prohibition on overpressing						+ ban on the use of sucrose		Competence to the Commission, link to OIV practices, special practices for export, end of ban for imported musts	Simplification, alignment on WTO-TRIPS and on PDO/PGI system, revision of wine classification system	Competence Commissior unique tools all wines, mc flexibility
<u>Option 4</u>: Deregulation of the wine market	Abolition	Abolition	Abolition with possible shift to 2nd pillar	Abolition with possible shift to 2nd pillar						+ status quo on the use of sucrose		OIV rules as only regulatory framework	Full integration in the PDO/PGI system	Full integratio in horizonta directive oi labelling oi foodstuff

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5. ANALYSIS OF IMPACTS

5.1. Economic impact

5.1.1. Market balance

The DG AGRI mid-term outlook for the EU-27 wine sector to 2010/2011 (*see Annex 2*), is that, assuming an unchanged CMO, the wine surplus in an "average" year could be 27 million hl (15.1% of production), or to 15 million hl (8.4% of production), if wine subject to distillation to support the potable alcohol sector is excluded.

<u>Option 1</u>: Status quo, with possibly some limited adjustments

Simply fine-tuning the policy tools under the existing CMO is **not expected to lead to major positive impacts on the equilibrium of the wine market** compared to the mid-term outlook.

A reduction in the minimum distillation price granted to producers under the potable alcohol scheme will not produce any improvement in the balance of the wine market, unless the price cut is substantial. As the current distillation price of €2.488/%vol/hl is systematically higher than the table wine price in the regions most interested by this distillation measure, even a 20% lower price would probably remain attractive for the majority of the producers applying for the scheme, so that they would not be forced to adjust the volume of their wine production. The only proposed adjustment that would potentially contribute to alleviating the market imbalance could be the introduction of a compulsory link between crisis distillation and the grubbing-up programme, but the impact of such a link would basically depend on how strict the requirements were, and would in any case be limited by budgetary constraints.

<u>Option 2</u>: Profound reform of the CMO

Among the policy changes proposed under this option, the following have a direct effect on the market balance of the wine sector:

– abolition of market measures (in particular distillations);
– new provisions on wine enrichment (suppression of must aid and ban on the use of sucrose);
– strengthening of the policy of permanent abandonment;
– measures introduced under the national envelope or rural development policy.

<u>Market measures</u>
To achieve a balance in the wine market it is necessary to remove all policy incentives that have led to the current situation of structural overproduction. The key measure is the abolition of the market support, which will guarantee, **in the long term, a balanced market situation**.

However, the cut in production needed to reach equilibrium will occur only following significant structural adjustment in the wine sector. This process could force less competitive wine holdings, currently relying on public support, to abandon the activity, and/or induce producers to reduce their yields in order to prevent overproduction problems.

Moreover, the abolition of some market tools supporting the use of wine production, such as potable alcohol distillation, could, **in the short term**, even cause **a greater imbalance in the wine market**. In particular, ending support for the distillation into potable alcohol would make EU wine alcohol less competitive in the alcoholic beverages market (compared with both alcohol produced from other raw materials and wine alcohol that could potentially be produced in non-EU countries); we can therefore expect some pressure for an overall reduction in the production of wine-based spirits and/or for a substitution in the long term of EU wine alcohol with imports. As a result, less EU table wine to supply this outlet would be withdrawn, thereby creating an additional surplus on the wine market.

The distillation of wine by-products is a different matter. Abolishing Community aid for this practice, while maintaining the ban on overpressing grapes, should not have any impact on overall wine production. Appropriate controls could reduce the risk of fraudulent overpressing practices, which would contribute to a greater imbalance in the market in the short term.

Wine enrichment

The impact of the combined abolition of the aid to must and of the ban on the use of sucrose on the wine market balance is extremely complex and difficult to estimate.

Ending the aid for must would certainly stop the recent trend towards artificial expansion of enrichment in countries or regions, mainly in Southern Europe, where this practice was not traditional. The immediate consequence would be that a large part of the volume of must currently used for enrichment (on average about 5 million hl), would come onto the market of table wine. On the other hand, the less intensive use of enrichment practices would result in an increase in the natural alcoholic strength of wines and, as a consequence, a reduction of yields, for both table wines and quality wines psr.

At the same time, **the ban on the use of sucrose** in Central and Northern European countries would entail massive replacement of beet sugar by concentrated grape must. This could contribute to a significant improvement of the market balance. According to a 1991 report[14], **the abolition of the aid for must and the simultaneous ban on chaptalisation would reduce total wine production in the Community by 6.8 million hl**. Although one might argue that positive impacts in terms of the reduction of wine production could be potentially weakened by removing the ban on vinification of must imported from non-EU countries, in reality the entry-price system for must should continue to ensure the protection for the domestic market.

Permanent abandonment

Strengthening the grubbing-up programme under this policy option, provided that the aid is set at an attractive level for producers, has an **immediate positive effect on the balance of the wine market**, because it directly reduces production potential, and therefore wine production. However, the decrease in production is probably less than proportional to the area abandoned, since it is primarily vineyards with low yields that are expected to be grubbed-up.

National envelope and shifts to Rural Development

As far as the national envelope and the shifts to RD are concerned, the impact on market balance will mainly depend on the mix of measures chosen by Member States; however, some of the

[14] The enrichment of wine in the European Community, Wageningen University, EUR report 13239, 1991.

measures suggested in the option could play an important role in reducing the wine surplus by enhancing the restructuring of the sector (e.g. early retirement of wine-growers and investment aid) and some other promote at least a better market orientation of production.

Apart from the abovementioned set of tools, other policy measures could indirectly contribute to improving wine market balance: introducing flexibility in wine-making practices and in labelling rules, and setting up promotion projects in non-EU countries, should help expand demand for EU wine by improving its competitiveness (*see section 5.1.3*).

In conclusion, the combined impact of the above policy changes will certainly lead **in the long term** to **a structural improvement in market equilibrium**. The introduction of tools aimed at reducing production potential, namely the policy of permanent abandonment, and other measures encouraging the restructuring, would play a major role in the transition towards the market equilibrium. These policy instruments would **accompany the process of structural adjustment** of the sector, brought about by the abolition of market measures, alleviating to some extent its adverse short-term effects. **At the end of the process, when market balance is achieved, the ban on new plantings could be lifted**.

<u>Option 3</u>: Reform along CAP reform lines

Under this option, the only change in policy tools capable of achieving a better market balance, albeit only in the long term, is the abolition of market measures (including the aid for must and related provisions linked to wine enrichment), the impact of which was analysed under option 2.

Therefore, in the absence of measures supporting a cut in production potential (or an expansion of demand) and structural adjustment of the sector in the short term, **the transition to market equilibrium, prompted by the abolition of the market measures, would be slower**. This would produce more intense suffering for the sector, which has relied for many decades on traditional market intervention instruments and would now have complete responsibility for adjusting to the changed market situation. The positive impact generated by greater flexibility in wine-making practices and in labelling rules in terms of improving the competitiveness of wine production would not be sufficient to alleviate the sector's short-term problems. However, as it is the case for option 2, **a situation of market balance would eventually be achieved**, therefore the ban on new plantings would then no longer be meaningful.

<u>Option 4</u>: Deregulation of the wine market

Assuming deregulation of the wine market, the two main policies having a direct impact on market balance are the termination of the market measures (including aid for must) and the abolition of the ban on new plantings.

As mentioned under options 2 and 3, abolishing market measures is an efficient way **to achieve equilibrium between supply and demand in the long term**, but would trigger abrupt structural adjustment in the wine sector.

Removal of the ban on new plantings would be initially involve a risk in terms of greater market imbalance, since there would be no limit to the expansion for the most efficient producers, thus possibly leading in the mid-term - as soon as the new vineyards would enter into production - to an increase in wine production. Of course, in a long term, the wine market would again reach equilibrium between demand and supply, but, until then, the abolition of the ban on new plantings would amplify the restructuring needs of the wine sector and therefore the difficulties of the market.

5.1.2. Prices and agricultural incomes

<u>Option 1</u>: Status quo, with possibly some limited adjustments

<u>*Long-term impact*</u>

The fragility shown by the wine market in the recent years proves that the sector is too dependent on Community support and that **the system is unsustainable**. The growing surpluses forecast in the mid-term outlook for the wine sector to 2010/11 (see Annex 2) will generate increasing pressure on intervention measures and on the corresponding budget. It will be increasingly difficult to clear the growing wine stocks rapidly and effectively using market tools. Recurrent crises would entail a **progressive decline in prices, and consequently in farm incomes**.

In this situation, **"cosmetic" reform of the CMO would be inadequate**.

Even in the scenario of an "improved" status quo, the proposed linkage between recourse to crisis distillation and the grubbing-up policy, due to the limited size of the budget envelope, could only result in minor improvement in the market balance and therefore also in prices and agricultural incomes. On the other hand, the slight reduction proposed in the minimum price to producers for potable alcohol distillation would not make the measure more effective, but simply reduce the cost of support for distillation that would take place anyway.

<u>*Short-term impact on prices*</u>

Of course, the short-term impacts on prices and incomes would very much depend on the conjuncture. In order to make the different policy options comparable, we assume "average" conditions for each of them.

In order to simulate the short-term impact of the status quo scenario on wine prices, and hence agricultural incomes, we link price development to the forecast development of wine stocks. In this respect, the following assumptions are made:

– on the basis of the mid-term forecasts presented in the Annex 2, the structural surplus generated by the wine market in a "normal" year would be **15 million hl** (excluding the volume of wine distilled under the potable alcohol distillation scheme). In a status quo scenario, this surplus could be partly removed by dual-purpose grape **(2 million hl)** and crisis distillation, but the remaining volume would accumulate in the form of additional wine stocks;
– although **crisis distillation** is not always been applied, and its use varies significantly from one year to another, between 2000 and 2005 an average of **4 million hl wine** per year was distilled. Distilling greater volumes in future would not be feasible from a budgetary point of view.

Hence, **the surplus generated by the wine** market would lead on average to an annual increase in stocks of **9 million hl** (15 – 2 – 4 million hl).

Subject to those assumptions, it is possible to give a rough idea of the scale of the impact on table wine prices through simple regression analysis, in which the average annual prices of table wine in the EU are related to the level of wine stocks over the period 2000–2005 (*more details on regression analysis can be found in Annex 3*).

The annual price data for the EU are calculated as the weighted average[15] of the annual table wine price in France, Italy and Spain, where those annual prices are calculated respectively as the average of the weekly quoted price.

On the basis of the statistical relationship between table wine prices and total wine stocks, and assuming that the level of stocks in "year 0" of the reform is equal to the average for the period 2000–2005, **the decrease in average wine prices** resulting from an increase of stocks of 9 million hl is estimated to be about **6%**[16].

After a further increase of wine stocks of 9 million hl the following year, the price decrease, compared to the initial value at the beginning of the "year 0", would be around **–12**%. **Prices would be therefore quite low**.

In the context of a general fall in prices, table wines would be probably most affected, since they are the main beneficiaries of distillation measures, but it seems unlikely that the quality wines sector could be spared from the downward trend in prices.

<u>*Short-term impacts on agricultural incomes*</u> *(detailed results can be found in Annex 4)*

The forecast price drop would also have a direct impact on agricultural incomes. We will mainly focus on table wine producers, who are the main beneficiaries of the market measures and therefore most affected by an unfavourable market situation.

To assess the scale of the impact on incomes, a microeconomic analysis has been carried out, based on information from the Farm Accountancy Data Network (FADN). To this end, seven "model farms" were built to represent the most typical table wine producers in five of the largest wine-producing EU regions (Poitou-Charentes, and Languedoc-Roussillon in France, Puglia and Sicilia in Italy and Castilla-La Mancha in Spain).

For each of these "model farms", based on 2003 FADN data, all relevant information was analysed, both concerning structural features (total utilised agricultural area, vine area, other crops, family labour and paid labour in the farm) and economic results (output, subsidies, costs, farm net value added and family farm income). The **income indicator** used for the analysis,

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15 The weighting factor used is the total wine production in the different Member States.

16 Different types of regression model have been tested (linear, exponential) and the results are very similar.

which is the most common for agricultural activity, is the **Farm Net Value Added per Annual Work Unit (FNVA[17]/AWU)**.

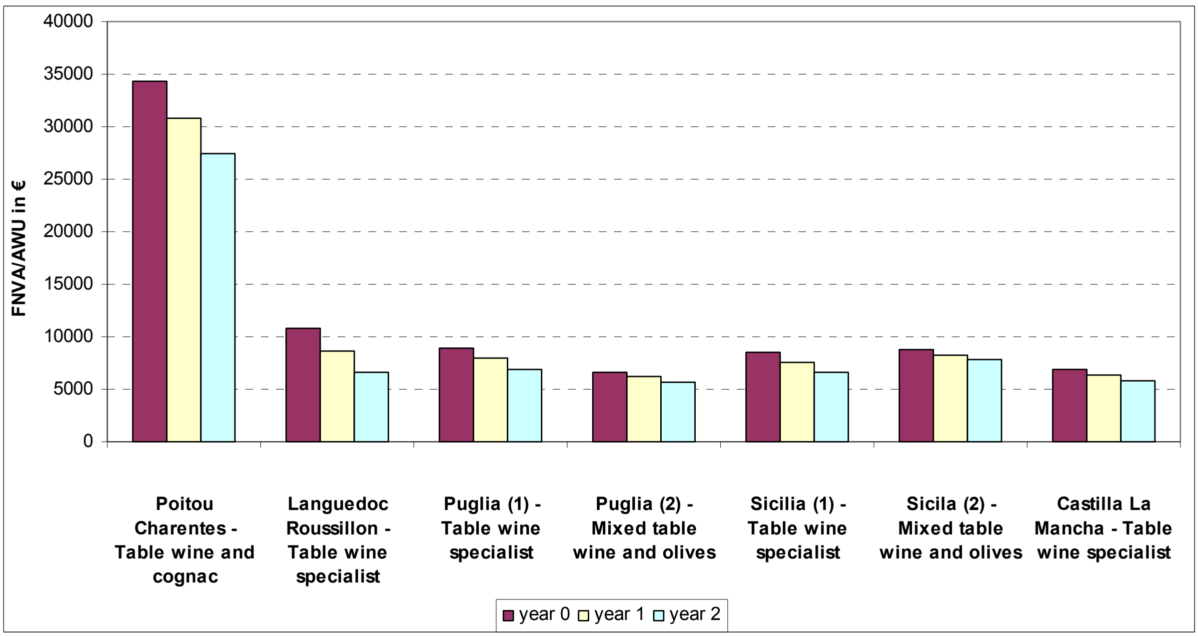
Assuming unchanged farm features, and notably a constant cost structure (static approach), the economic results of the model farms were projected to "year 0" of the reform. In doing this, it was acknowledged that wine prices in 2003 were particularly favourable; therefore they were replaced by the average price recorded in the period 2000–2005. For that reason, the farms considered in the "year 0" are less profitable than in the base year 2003.

Once the economic results of the wine farms for the "year 0" were obtained, the FNVA/AWU for the two following years was simulated; this was calculated by applying, to the wine output in the "year 0", the forecast price drop.

The results of this simulation exercise indicate that the **price decrease would have a very significant impact on agricultural incomes**, which would, after the first year, fall by between **5% for non-specialised table wine producers in Sicily and 19% for table wine specialists in Languedoc-Roussillon. After two years, agricultural incomes in those two regions would decline respectively by 11% and 39%.**

However, it is important to note that, due to the static approach (unchanged farm feature and constant cost structure), the method tends to overestimate the fall in income, because it does not consider any economic adjustments by the farms.

Graph 1: Evolution of FNVA/AWU of seven typical wine farms in five EU regions before and after the implementation of reform option 1



17 **Farm net value added** = Total farm output + Balance current subsidies and taxes – Intermediate consumption – Depreciation.

Source: DG AGRI – FADN

The explanation for the generally sharper fall in income in Languedoc Roussillon is that, as those farms are highly specialised, they are completely dependent on the wine market situation. Moreover, despite being currently more profitable than their Italian and Spanish counterparts, French producers have higher production costs and a higher ratio of costs to revenue, due to the nature of their business, which is more capital-intensive; if those costs are not covered by a certain level of income the production, they risk becoming a heavy burden.

By contrast, farmers in Southern Italy and in Castilla-La Mancha manage, despite the relatively heavy income losses, to maintain a certain profitability, due to their low-input production system.

Option 2: Profound reform of the CMO

Long-term impacts

As was previously mentioned, the abolition of market measures would lead in the long term the wine sector to market balance. This long-term equilibrium can be expected to be mainly achieved by production falling into line with demand, rather than through a downwards adjustment of wine market prices. Apart from yearly production fluctuations due to climatic factors, the level of wine stocks would then be stable over time.

For those reasons, **prices and agricultural incomes would reach satisfactory levels** and could be comparable to those in the best years under the existing CMO, when the surplus recorded (excluding wine distilled under the potable alcohol distillation scheme) was close to zero. In this situation of market balance, the conditions for abolishing the ban on new plantings would finally be met.

Conjunctural problems linked to occasional surpluses generated by exceptionally abundant harvests, could be tackled through measures supporting safety net mechanisms under the national envelope.

Short-term impacts on prices

It was mentioned above that abolishing potable alcohol distillation could worsen the wine market balance in the short term. Moreover, and more important, the ending of all market measures would mean that **production surpluses** could not be physically removed from the market through specific distillation measures, but **would invariably accumulate as additional stocks**, which would have the effect of depressing prices and consequently agricultural incomes.

On the other hand, strengthening the grubbing-up programme to reduce production potential, and providing new incentives for restructuring the sector under the national envelope or rural development policy, would accelerate the adjustment of production and the reduction of production surpluses, thereby diminishing the short-term accumulation of wine stocks.

Although it is virtually impossible to quantify exactly the combined effect of the proposed set of measures on short-term trends in wine stocks, some assumptions are made to link such trends to the possible development of wine prices and hence of agricultural incomes.

– on the basis of the mid-term forecasts presented in Annex 2, the immediate abolition of the distillation measures would mean that the **structural surplus** generated by the wine market in a “normal” year would increase wine stocks by **15 million hl**;

– due to the disposal of less wine for distillation to potable alcohol, an **additional surplus volume** would be generated. As the market in wine-based spirits is well established, but on the other hand the loss of competitiveness against alcoholic beverages based on other raw materials and/or potential future substitution by imports of cheaper wine alcohol from non-EU countries could seriously reduce the uses of EU wine for the production of distillates, it could be supposed that this additional surplus could amount to **4 million hl**, which would be also accumulated in the form of new stocks;

– following the abolition of aid for must and the simultaneous **ban on chaptalisation**, we assume that the replacement of beet sugar by concentrated grape musts would produce a reduction of **6.8 million hl** in total wine production (*see section 5.1.1*);

– the reinforcement of the **policy of permanent abandonment and the restructuring incentives** provided under the national envelopes would encourage less competitive producers to leave the wine sector. We could assume that grubbing-up alone would allow the abandonment of 80 000 ha of vineyards per year, which could reduce wine surplus by approximately **3 million hl**. The other structural measures under second pillar reduce it by further **1 million hl**.

Omitting, for simplicity’s sake, the smaller possible impacts of other proposed measures, we could estimate that, under this policy option, **the surplus generated by the wine** market in the first year after reform would lead on average to an increase of stocks of **8.2 million hl** (15 + 4 – 6.8 – 4 million). In the second year of the reform, wine stocks would continue to increase, but “only” by **4.2 million hl** (8.2 – 4 million).

On the basis of the same regression analysis made for option 1, relating table wine prices to total wine stocks, **the decrease in the average table wine prices produced by the trend in stocks is estimated at 5% in the first year and 8% after two years.** Prices would be at a low level, but **still better than in the status quo scenario**, and with **prospects of short-term recovery**, given the favourable trend in stocks.

Again, **table wines would probably be most affected by the price drop**, but **quality wines would probably be affected by the general downward trend as well**.

<u>Short-term impact on agricultural incomes</u> *(detailed results can be found in Annex 4)*

The same method based on model farms as under option 1 was followed for option 2.

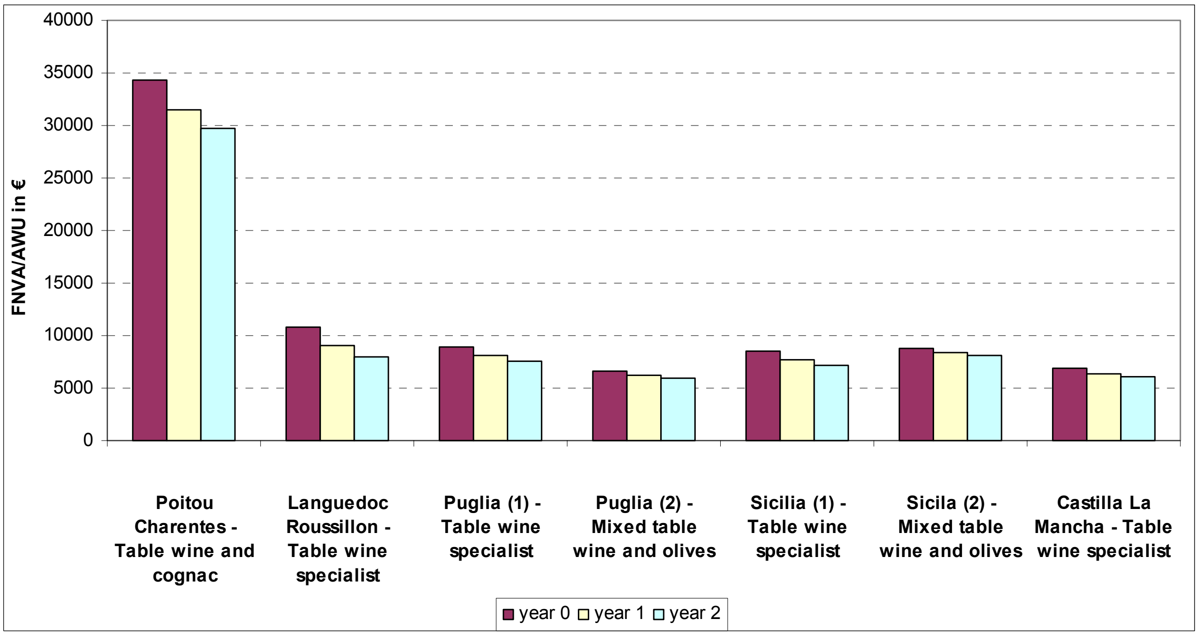
Following the same static approach, which assumes unchanged farm features, and notably a constant cost structure, the results of this simulation exercise indicate that the price decrease would have quite a **significant impact on agricultural incomes**, which would, after the first year, fall by between **5% for non-specialised table wine producers in Sicily and 16% for table wine specialists in Languedoc-Roussillon**. **After two years, agricultural incomes in those two regions would decline respectively by 7% and 26%.**

The explanation for the different magnitudes of income reduction in the various types of farm and regions is basically the same as under option 1.

Again, because of its static approach (unchanged farm feature and constant cost structure), the method tends to overestimate the fall in income.

Furthermore, another factor determining an overestimation of the income decrease, and specific to this option, is the difficulty to fully include in the model-farm approach the indirect positive impact on income determined by some measures in the national envelopes and in the strengthened rural development policy.

Graph 2: Evolution of FNVA/AWU of seven typical wine farms in five EU regions before and after the implementation of reform option 2



Source: DG AGRI – FADN

One final comment on the impact on income of the proposed **ban on the use of sucrose** for enrichment: the effect will be to increase production costs in the wine regions currently making use of this oenological practice. According to the study mentioned above[18], the replacement of sucrose by unsubsidised concentrated must could **increase the production costs** of that part of German wine production relying on chaptalisation, **by 15–25%**. This cost increase could lead to a significant income loss. However, it is not straightforward to quantify that income loss exactly, due to the impossibility of simulating cost variations for specific farm production using the FADN, and because of the small size of the German FADN sample of wine holdings.

[18] The enrichment of wine in the European Community, Wageningen University, 1990.

<u>Option 3</u>: Reform along CAP reform lines

<u>Long-term impact</u>

The same considerations set out for option 2 would be broadly applicable to option 3: the **achievement of the market balance** would **in the long term** guarantee that prices and agricultural incomes reached satisfactory levels. In this case as well, once market balance was attained, the ban on new plantings would be pointless. However, the time frame needed to achieve market balance would be longer, due to the complete absence of specific structural measures accompanying the abolition of market tools. On the other hand, the longer adjustment period would be compensated for by a higher level of income in the end, due to the payment of decoupled aid.

Finally, it should be mentioned that no instrument in the CMO would be available to deal with conjunctural overproduction problems, which, due to climatic conditions, occasionally affect the wine sector.

<u>Short-term impacts on prices</u>

As for option 2, ending distillations measures would mean that **production surpluses** would invariably **accumulate as additional stocks**, with serious consequences for market prices.

Moreover, in the absence of measures supporting a reduction of production potential (or an expansion of demand) and structural adjustment of the sector, wine stocks in the short term would accumulate more rapidly than under option 2.

Again, some assumptions have to be made in order to link the trends in wine stocks to the possible development of wine prices and hence of agricultural incomes.

– according to the mid-term forecasts referred to above, the immediate abolition of distillation measures would, in a "normal" year, increase wine stocks of **15 million hl**;
– additional wine stocks, in the order of **4 million hl**, would accumulate due to less table wine being distilled to produce alcoholic beverages following the abolition of the corresponding distillation scheme;
– wine stocks would drop by **6.8 million hl** following the introduction of the ban on chaptalisation.

In conclusion, we could estimate that, under this policy option, **the surplus generated by the wine** market would lead on average to an annual increase of stocks of **12.2 million hl**.

On the basis of the same regression analysis made for options 1 and 2, relating table wine prices to total wine stocks, **the decrease in average table wine prices resulting from the trend in stocks is estimated at 8% in the first year and 16% after two years, which would lead to the lowest price levels ever.**

Again, **table wines would be probably most seriously affected,** but **quality wines would probably be affected by the general downward trend in prices as well.**

<u>Short-term impact on agricultural incomes</u> (detailed results can be found in Annex 4)

The same approach based on model farms as under option 1 and 2 was followed for option 3. The only peculiarity of this specific case is that the simulated income must take into account the value of the new decoupled hectare payment received by the wine holding.

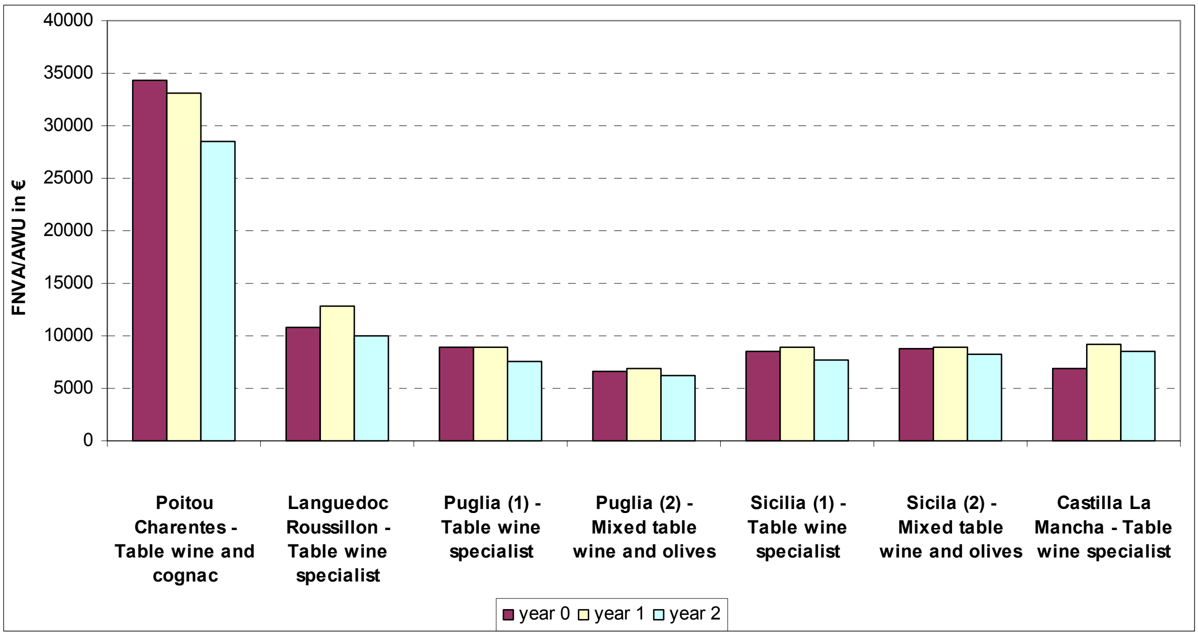
Assuming that total expenditure on the CMO is transferred to the Single Payment Scheme, the **decoupled payment would amount to approximately €380 per ha** (€1 300 million for 3.4 million ha). This direct payment would be subject to modulation.

The results of this simulation exercise indicate that the introduction of a hectare payment would initially at least compensate for (and in some cases would even exceed) the price drop, so that **the impact on agricultural incomes would vary, after the first year of the reform, between –3% in Poitou-Charentes and +34% in Castilla-La Mancha.** However, the further price drops in subsequent years would lead to a progressive decline income. After two years, agricultural incomes would already be declining everywhere (between –5% for non-specialised table wine producers in Sicily and –17% in Poitou-Charentes), except in Spain.

The reason for the income increase in Castilla-La Mancha is that, given the low yields and the low price of table wine in that region, the level of decoupled payment turns out to be quite substantial for that type of farm.

However, the **steep fall in prices** from one year to another could mean a decline of agricultural income in subsequent years, so that **the main difficulties could occur in the medium term**, before market balance is achieved.

Graph 3: Evolution of FNVA/AWU of seven typical wine farms in five EU regions before and after the implementation of reform option 3



Source: DG AGRI – FADN

Again, the ban on the use of sucrose would have the same adverse impact on production costs and incomes of Central and Northern European wine regions as noted for option 2.

Finally, distributing the whole wine budget as a flat-rate decoupled payment per hectare of vine area would mean that quality wine producers, even in the upper range, would benefit from direct payments as well. This could make it **difficult to accept the system** and lead to **overcompensation of certain quality wine farms**, which might in fact be affected very little by the worsening of the market situation. On the other hand, any alternative system discriminating between quality wine and table wine producers could introduce disparities between single producers, would be technically very difficult to implement and could lose the advantages of a simple and universal approach, e.g., as far as scope for applying cross-compliance rules is concerned (see section 5.3).

Option 4: Deregulation of the wine market

Long-term impact

As mentioned under the previous two options, long-term achievement of market balance is the guarantee that the **prices and agricultural incomes will stabilise at a satisfactory level**. However, the immediate removal of the ban on new planting rights, combined with the lack of structural measures in the CMO accompanying the abolition of market measures, would complicate the move towards market equilibrium, which would **take longer** compared with other options.

Furthermore, as in option 3, there would be no instrument to alleviate conjunctural problems linked to the extreme variability of wine production.

Short-term impact on prices

As for the other options, after the abolition of distillations, **production surpluses** would **invariably accumulate as additional stocks**, with serious consequences for market prices and consequently agricultural incomes.

Compared to option 3, wine stocks would accumulate even more steadily, due to the proposal to maintain the status quo as far as the use of sucrose for enrichment is concerned (which would prevent production from decreasing). On the other hand, the immediate removal of the ban on new planting rights would not have an impact on production in the short term, but only in the medium term, due to the time it takes for any new vineyards to enter into production.

In short, we could estimate that, under this policy option, **the surplus generated by the wine** market would lead on average to an annual increase in stocks of **19 million hl** (wine surplus including the 4 million hl resulting from the abolition of potable alcohol distillation).

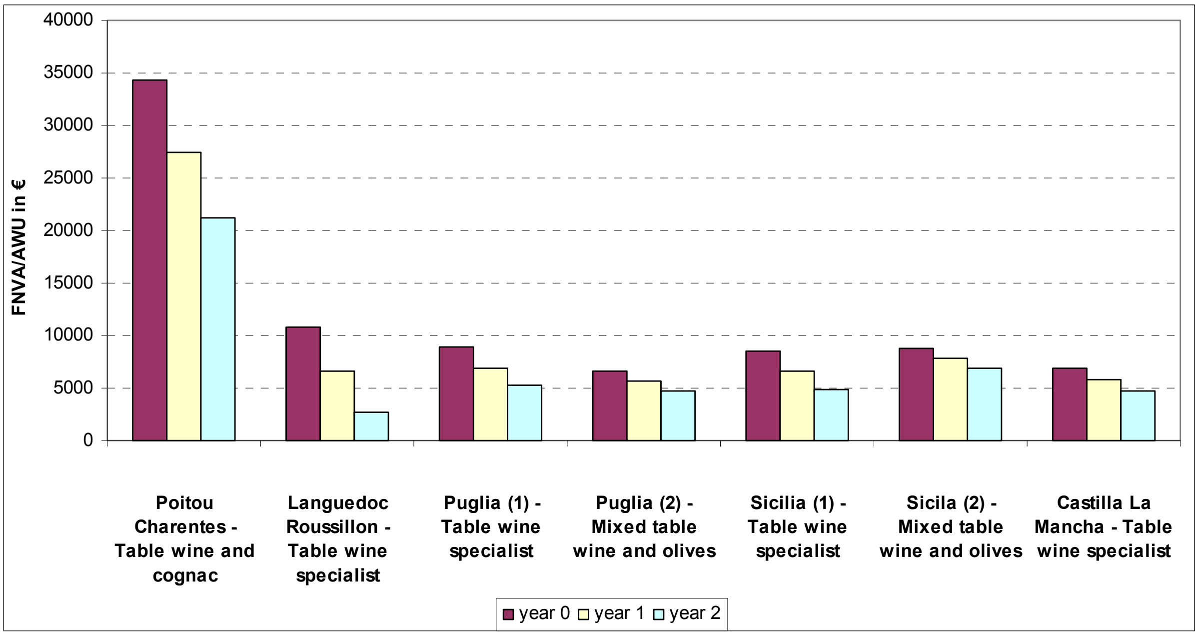
On the basis of the same regression analysis **the decrease in average wine prices resulting from the trend in stocks is estimated at 12% in the first year and 23% after two years, which would represent the highest price drop of all the options.**

Short-term impact on agricultural incomes (detailed results can be found in Annex 4)

Based on the usual model farm approach described under the previous options, agricultural income was simulated.

The results of this simulation exercise show that the consistent price decrease under the deregulation scenario would have a very significant impact on agricultural incomes, which would, after the first year, fall by **between 11% for non-specialised table wine producers in Sicily and 39% for table wine specialists in Languedoc-Roussillon**. **After two years, agricultural incomes in those two regions would decline respectively by 21% and 74%.**

Graph 4: Evolution of FNVA/AWU of seven typical wine farms in five EU regions before and after the implementation of reform option 4



Source: DG AGRI – FADN

5.1.3. Competitiveness

Competitiveness is a many-sided concept and difficult quantify and measure. Broadly speaking, the competitiveness of an industry can be defined in terms of the profitability of its production. In an undifferentiated-products industry, profitability is mainly linked to lower production costs compared to competitors, but, in differentiated products industries like the wine sector, another fundamental factor of profitability is the attractiveness of the product compared with the same industry in other countries, with which one might trade.

Thus, a wine industry is competitive if it has the capacity for profitable and viable production and can compete on the world scene by producing and marketing wines that meet consumers' expectations and preferences.

Although a large part of the EU wine production can be certainly considered **highly competitive in the global market**, the increasing erosion of the market share of EU wines as against so-called new world wines, both on the domestic and on the export markets, shows a worrying loss of competitiveness of our industry, particularly in the low and medium quality segment.

The EU wine industry has **several handicaps** compared to its competitors:

– **smaller production and processing structures**, and lower yields, entailing higher production costs and lower volumes to respond to demand from large scale retailers;
– too large range of products and **less clear price positioning and marketing strategies**, making it difficult for consumers to understand, identify, remember and find again products they need or like;
– **greater regulatory constraints** in the CMO, like planting rights, the ban on new plantings, cumbersome procedures to allow the development of innovations in oenological practices or marketing strategies, and on the other hand, market support mechanisms preventing adjustment of production.

<u>Option 1</u>: Status quo, with possibly some limited adaptations

Although some instruments of the existing market organisation have played a positive role in boosting the competitiveness of the EU wine sector, for example the restructuring programme, which has allowed a **quality improvement** and an alignment of production with demand, the CMO has largely contributed to the loss of competitiveness of the EU wine sector; therefore a substantial extension of **the existing regime would not lead to any improvement**, but could only worsen the situation.

<u>Option 2</u>: Profound reform of the CMO

The measures proposed under this option would significantly contribute to an improvement of the competitiveness of the EU wine sector in different ways:

1. Ending market measures would encourage **structural adjustment** in the wine sector, leading less competitive holdings, whose production is currently largely intended for distillation, to abandon the activity. The overall competitiveness of the sector would thereby increase.
2. The reinforced grubbing-up programme and the incentives for early retirement of wine producers would facilitate structural adjustment of the wine sector and help to **increase the average size of wine holdings** in the EU, although the gap with the huge companies in new world countries could certainly not be closed.
3. Confirming the restructuring programme and strengthening rural development measures would permit **continued modernisation** of the vineyards, thus contributing to a **greater cost-effectiveness and better market orientation** of EU wine production.
4. More flexibility in the procedure for approving new wine-making practices would increase **scope for innovative techniques**. The possibility of authorising specific wine-making practices only for export would allow EU producers to operate on the world market in conditions of equal opportunities with non-EU competitors.

5. Simplifying the GI system and the labelling provisions would **increase transparency for the consumer**. Moreover, a greater flexibility in the regulatory framework would provide **new marketing opportunities** for EU wines: for example, permitting the indication of the wine variety and vintage year for table wine without GI would allow the expansion of the "vins de cépage" segment, which was one of the key factors for the recent overwhelming success of new world's wines.

6. A more ambitious promotion and information policy could underpin new wine marketing strategies and innovations in wine-making practices.

As far as the proposed ban on the use of sucrose for enrichment is concerned, it was already mentioned that this provision could lead to an increase of production costs in wine regions currently making use of this practice. Replacing sucrose with unsubsidised concentrated must could **increase the production costs** of that part of German wine production relying on chaptalisation by **15–25%.** This would have an adverse effect on the competitiveness of the producers concerned.

<u>Option 3</u>: Reform along CAP reform lines

The most significant positive impact, described under option 2, also apply to option 3. In particular, ending market measures would provide for better market orientation of wine production and the improvements introduced in the regulatory framework for wine-making practices, geographical indication system, and labelling rules would facilitate innovation.

However, concentrating the entire budgetary envelope on the SPS would mean wine producers could no longer benefit from the restructuring programme or any structural measure promoting a higher competitiveness.

Finally, we have to point out the adverse impact of the ban on sucrose for enrichment on competitiveness of Central and Northern European wine producers currently making use of this wine-making practice.

<u>Option 4</u>: Deregulation of the wine market

Besides ending market measures, common to options 2, 3 and 4, **the main advantage provided by the deregulation scenario is the immediate abolition of the ban on new plantings**.

The possibility of expanding the vine area without restrictions gives the most efficient producers freedom to **optimise the size of their holdings and to operate at the most convenient production scale**, although the rules regulating the access to GIs and protected denominations would de facto partly restrict the area eligible for protected designations.

Maintaining the status quo as regards allowing producers to enrich wine with sucrose would avoid the loss of competitiveness of Central and Northern European wine producers described in options 2 and 3.

Finally, as far as the so-called regulatory measures are concerned, incorporating the whole legal framework into horizontal legislation could produce improvements in competitiveness to the same extent as the more sector-specific approach in options 2 and 3. In any event, the practical impact would depend on the implementation of the general systems and on the way in which the particularities of the wine sector are taken into account, so as to promote the quality of the product and protect of the image of European wine inside the EU and in the world.

5.2. Economic and social impact on rural areas

Vine-growing and wine production play an important economic and social role in the level of activity and employment in rural areas of many Member States in the EU. As was mentioned in section 2.1, wine production represents, in the most important producing countries, about 10% of the value of their agricultural production.

In 2003, there were more than **1.5 million holdings with vineyards** for wine production[19] in the EU-25[20], representing more than **15% of all EU farms**.

Wine farms as a whole absorb over **1.5 million Annual Work Units**, which corresponds to about **15% of the total AWU employed in EU agriculture**. Compared with other crops, vineyards are **more labour-intensive**, even though this higher labour-intensity is compensated by a smaller average farm size. The family labour force strongly prevails, but employment of regular non-family labour is considerable in some regions, particularly in France. Compared with other types of farms, wine holdings typically have a higher proportion of older farmers.

Vine-growing is vitally important in certain EU regions, where it represents an even greater share of regional agricultural output, use of the agricultural area and/or agricultural employment. There, the value of wine production accounts for 20% to 30% of final agricultural production, with a maximum of over 45% in Languedoc-Roussillon (France). At a more local level, the percentages are often even higher.

In those wine regions, alongside the permanent jobs in the vineyard, there is seasonal employment in the harvest and jobs linked to wine-making. Wine is either made directly on the holding, in a cooperative's cellars or by a private enterprise, but always near to the production area, for reasons both technical and legal. Wine production is an activity where processing takes place on the spot, so the added value remains in the production region. That value can also be increased to the benefit of the producers if they sell directly from the holding.

Finally, the **economic and social function of wine production** extends well beyond the production and marketing of wine and should therefore be measured taking into account **indirect economic activity in the production regions**: its knock-on effect in terms of employment, for example linked to wine distilleries, or tourism, contributes to the rural development of the regions it is present in. In addition, grape and wine production fulfils non-commercial functions – its structuring effects having an impact on the countryside, villages and rural communities.

Broadly speaking, the impact assessment on agricultural incomes (see section 5.1.2) already provides useful indications about the possible economic and social impact of the four reform options on rural areas of regions, in which vine-growing plays a major role in their agricultural activity.

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[19] Source: Eurostat's Farm Structure Survey.

[20] Although 2003 was pre-enlargement, data are for EU-25.

<u>Option 1</u>: Status quo, with possibly some limited adjustments

The continuation of the existing wine regime, even with limited adjustments, has been proved to be unsustainable in the long term. The progressive deterioration of the market situation in the wine sector would increasingly lead to economic and social **difficulties in rural areas** of the most concerned regions.

<u>Option 2</u>: Profound reform of the CMO

In general, the smooth stabilisation of the market balance, and hence the achievement of economic sustainability of wine production, would have a favourable impact, not only on the wine sector itself, but on the agricultural and economic activity of rural areas as a whole. In particular, the funds allocated to the national envelope would **facilitate structural adjustment** of the sector and mitigate the adverse economic and social effects of downscaling wine production.

In addition, the grubbing-up premium and reinforced early retirement measures under rural development would give adequate support for non-competitive or older vine-growers, thus providing them an opportunity to leave the activity. On the other hand, coupling the grubbing-up of vineyards with granting SPS entitlements could ensure viable alternatives for farmers intending to reconvert production.

Other rural development measures could address additional specific problems linked to restructuring.

<u>Option 3</u>: Reform along CAP reform lines

The complete lack of specific structural measures accompanying the abolition of market tools and helping the structural adjustment of the wine sector would entail **significant risks for the cohesion of wine producing regions**. This could particularly affect the fragile rural economies of the new and the acceding Member States.

While wine producers would be partly compensated for the price drop and loss of income through a decoupled payment, some of the jobs directly and indirectly linked to the wine production could be lost.

<u>Option 4</u>: Deregulation of the wine market

Immediate deregulation of the wine sector would have the **most radical impact on the economy of wine-producing regions**. Besides the significant fall in income for wine producers (see section 5.1.2) and the adverse effects linked to the absence of structural measures accompanying the adjustment process in the wine sector (as for option 3), abolishing the ban on new plantings could lead to a substantial **shift of production between wine-producing regions or even between Member States**, thus resulting in an additional risk for the economy of less competitive and hence more fragile wine-producing entities.

Again, the new and the acceding Member States will particularly suffer from the complete lack of necessary support, preventing them from taking the opportunity to apply the necessary structural measures they need (grubbing-up and/or restructuring) to adjust their wine production, in quality and quantity, to demand. Given the importance of the agricultural dimension, and in particular of the wine sector, in Romania and Bulgaria, it is very likely that this would impact on their rural economies as a whole.

5.3. Impact on the environment

Vine-growing has both positive and negative effects on the environment.

The most important environmental pressures exerted by wine production are:

– <u>impact on the soil</u>: erosion (if vine rows are arranged in the direction of the slope and soil is uncovered between the rows), compaction, loss of organic matter and contamination through plant protection products;

– <u>intense use of plant protection products</u>, in particular fungicides, which have an adverse impact on water, soil and biodiversity;

– <u>disposal of waste and by-products of vine-growing (e.g. pesticide packaging) and wine-making (marcs and lees).</u>

Other environmental concerns raised by wine production, although to a lesser extent and limited to certain regions, are an increasing use of irrigation, the effects of excessive specialisation and risks resulting from disordered grubbing-up of vineyards.

A major wine regime measure with considerable environmental consequences is **distillation of the by-products of wine-making**. On the one hand, it allows a sound management of these by-products, thereby avoiding environmental risks (acidification of the soil, infiltration of alcohol in underground waters, air pollution by ethanol and ozone production, etc.); on the other hand the practice of not returning the elements contained in these by-products to the soil and of using mineral rather than organic fertilisers contributes to a progressive loss of soil organic matter. Moreover, the environmental costs of distillation operations (energy use, transport of by-products to distilleries, etc) are not negligible.

Despite all the environmental implications of vine-growing, the **wine CMO contains few explicit references to environmental concerns**. More specifically, **the extent to which the environment is integrated in the wine regime is very limited** compared to other market organisations that have undergone the 2003 CAP reform.

In particular, as vine land is not eligible for direct payments, it is **not covered by cross-compliance rules**. This means that there is currently no environmental baseline for vine-growers, except that provided by environmental directives. In reality, some wine producers and part of the corresponding vine area are nevertheless already covered by the system of cross-compliance, since any wine producer receiving direct payments (for areas other than vineyards) is subject to cross-compliance for his whole farm. According to FADN data, **74% of professional wine producers in the EU and 57% of the corresponding total vine area are subject to cross-compliance obligations**, but with considerable variation at Member State level, the largest coverage being in Greece and the lowest in France and Germany.

The reform of the CMO should better integrate environmental concerns in the wine regime. This could be achieved along two lines:

1. **establishing an environmental baseline of what it is reasonable to expect a farmer to fulfil without additional support**. This baseline would include statutory management requirements under Annexe III and all standards in Annex IV of Regulation 1782/03 on cross-compliance, whose scope should be adapted and extended to cover specific problems concerning vine-growing;

2. **support for environmentally-friendly production methods**, which go beyond the environmental baseline, like organic production, Integrated Pest Management (IPM) and, if possible, Integrated Crop Management (ICM).

<u>Option 1</u>: Status quo, with possibly some limited adjustments

The status quo would result in the continuation of a number of pressures on the environment, putting the wine regime significantly behind almost all other CMOs in terms of environmental integration. The wine sector jeopardise its own image for producing a wholesome and desirable product.

<u>Option 2</u>: Profound reform of the CMO

As under this option many wine farms would not receive direct payments, which could be cut in the event of non-respect of cross-compliance rules, there is **no easy way to enforce the environmental baseline in the whole vine area**.

However, the proposed option offers enough **flexibility to adopt alternative measures**. A realistic solution to tackle the problem could be the following:

– make support provided by each single measure granted under the wine CMO, including all measures eligible for the national envelope and under the second pillar, conditional on cross-compliance;

– where the first method is not applicable, leave Member States to apply their usual statutory penalties for non-compliance with Community legislation.

Financial incentives for environmentally-friendly production would be provided as agro-environmental measures, reinforced through the new funds transferred to the second pillar as an additional envelope earmarked for wine-producing regions.

Other new elements introduced by option 2 could be assessed as follows:

– Strengthening **permanent abandonment** would have a globally positive impact on the environment, since it generally reduces monoculture and the associated environmental pressure. However, it could also lead to environmental risks if the land is abandoned (risks of soil erosion) or replaced by more intensive production. In any event, the grubbed-up area could be given an SPS entitlement, thus falling immediately under the scope of cross-compliance. The proposed cultural landscape payment under the rural development programme could also help to prevent the adverse impact of a far-reaching grubbing-up programme for vines in areas with a specific and recognised environmental/landscape value, which could otherwise be endangered.

Regarding the use of vine land after grubbing-up, historical records show that the situation is quite different from one MS to another[21]: in Portugal, vines were mainly replaced by maize and then sugar beet; in France by arable land and fallow land; in Spain by cereals, olive trees (particularly in Castilla-La Mancha), vines to produce table grape and orchard; in Germany, by fallow land and in some cases by forest land; in Italy, in the Po Valley by arable land, in the hilly regions of Trentino and Romagna by orchards and in Southern Italy by olive trees; in Greece, finally, by olive trees.
It some cases, e.g. in Castilla-La Mancha in Spain, grubbed-up vineyards were abandoned, either immediately after grubbing-up or later, since, due to the arid conditions; the cereals that were often cultivated after the vines were not as profitable as expected. In general, vineyards were also rarely replaced by forest;

– the removal of all **distillation measures** may have a positive impact on the environment, assuming residues/wastes from wine-making are dealt with in a proper manner. In Member States currently withdrawing by-products under supervision, no environmental concerns have been raised. Consequently, the proposed measure would imply no changes to the present system, which already applies environmentally-friendly methods. In Member States currently applying the compulsory distillation of by-products, wine producers (or cooperatives) that, under the proposed system, are not in a position to utilise their marcs and lees on the farm, e.g. as organic fertiliser after an appropriate composting or anaerobic process, should approach the problem as a waste management issue. From that angle, delivering the by-products to a distillery, even for free, could be economically reasonable. Nevertheless, particularly in regions where there are few distilleries, and the average distance between the wine holdings and the closest distillery is considerable, the risk of inappropriate disposal of by-products can not be neglected. Appropriate disposal and/or recovery options, in keeping with EU legislation, would therefore need to be developed at national or regional level. Controls should be reinforced, and penalties for abuse imposed in accordance with the requirements of the environmental baseline;

– making the **authorisation of new WMPs** easier could enable faster approval of more environmentally friendly practices and processes and prohibit or restrict harmful ones. Environmental aspects should be decisive when considering whether to authorise the use of wine-making practices;

– the greater flexibility on **labelling rules** could be used to enhance the value of environmentally-friendly practices such as organic production.

Option 3: Reform along CAP reform lines

The main asset of this option is that **the environmental baseline would be automatically covered by cross-compliance**, adapted and extended as outlined above.

However, using the entire budget to create SPS reference amounts would prevent funds being shifted to rural development to enhance environmentally-friendly production techniques, although the possibility of using part of the SPS envelope for measures for specific types of

[21] What land use for sustainable agriculture?', European Commission, DG AGRI.

farming and quality production, as under Article 69 of Regulation (EC) No 1782/2003, would be still open.

Concerning distillations, wine-making practices and labelling rules, the same remarks as under option 2 would apply.

Option 4: Deregulation of the wine market

Under this option, **an environmental baseline would be very difficult to implement**, since no support of any kind would be granted to vine-growers underof the wine CMO. The situation would be comparable to the status quo, in which only wine farmers receiving direct payments for areas other than vineyards are subject to cross-compliance. The only possibility would be to leave Member States to apply their usual statutory penalties for non-compliance with Community legislation.

In addition, there would be no wine region-specific transfer of funds to the second pillar that could enhance environmentally friendly production techniques.

More specifically, **lifting the ban on new plantings could entail some risks to the protection of the environment:**

– increasing environmental pressure due to **possible expansion of the vine area in the short term**. However, permanent expansion of the European vine area does not seem to be economically realistic, given that achieving market balance and absorbing market surpluses should lead instead, in the long term, to a reduction of vine area;

– **possibility of production shifts towards areas where vine-growing has a competitive advantage**. For example, vineyards could "move" from mountainous and hilly regions, where vine-growing is more costly but could play an important role for the environment (combating soil erosion, lesser diseases problems due to drier climate conditions and consequently lesser consumption of fungicides, etc.), to the plains.

Concerning distillations, the same remarks as under options 2 and 3 would apply.

5.4. Impact on trade and WTO conformity

The impact of the four policy options on trade dynamics is essentially linked to their impact on the competitiveness of the EU wine sector, which are analysed in section 5.1.3. In addition, developments in international negotiations, both at multilateral (WTO) and bilateral level (trade agreements), represent another important exogenous factor.

Given the importance of the Community's export interests in the wine sector, it is essential to ensure full access to our export markets worldwide and to achieve better international protection for our geographical indications. A coherent domestic wine regime, fully consistent with our international obligations, is essential for a sound and credible position in international discussions, which would justify and strengthen a firm EU position on GIs and wine-making practices.

For the wine sector, the main issues at stake in the WTO are:

– internal support:
in 2005, 63% of annual wine CMO expenditure was classified as Amber Box, which is the most trade-distorting type of support. Basically all market measures fall into this category, namely distillations (including the taking-over of alcohol), must aid and private storage. While the EU is currently still below its Amber Box ceiling, the pressure on this type of support is very great;

– export refunds:
WTO negotiations have reached an agreement in principle on phasing out all export subsidies. Refunds currently granted under the CMO will have to be cancelled;

– quality policy/GIs:
the existing quality regulatory framework is criticised by our international partners and does not allow optimal international protection of our geographical indications under the WTO-TRIPS Agreement;

– labelling provisions:
our labelling rules are subject to severe criticism from non-EU countries, which consider them discriminatory.

Option 1: Status quo, with possibly some limited adjustments

In spite of the minor adjustments proposed, including the phasing out of export refunds already agreed in the current Doha Round negotiations, in the status quo scenario almost all WTO problems of the existing wine regime would remain unsolved; therefore **many provisions of the CMO would potentially be under attack in the future**.

Options 2–3–4

All three options would be **completely WTO-friendly**, given that:

– all market tools, currently classified as Amber Box support, plus export refunds, would be cancelled;

– almost all new measures proposed under the different options, such as the reinforced programme of permanent abandonment and the second-pillar structural measures in option 2, as well as the SPS in option 3, are classified as Green Box, which is the less trade-distorting type of support. The only uncertainty concerns the national envelope under option 2, whose Green Box status should be verified on the basis of the complete list, the exact definition and the actual use of eligible measures. Among the most important measures foreseen in the national envelope, the support to restructuring and reconversion of vineyards is currently considered as Green Box, whereas the classification of new measures, as risk and crisis management tools or green harvest should be established in the context of the WTO;

– the quality policy, the GI system and the labelling framework would be amended to make them WTO friendly;

– other rules at risk vis-à-vis WTO-TBT provisions, such as the ban on vinification of imported must and on blending Community wines with non-EU wines, would be abolished.

5.5. Impact on wine quality, health and consumer protection

5.5.1. Wine quality

Although wine quality is primarily the responsibility of wine producers, the regulatory framework should ensure quality and conformity with product definitions. WMPs have met those objectives, and European wines as a whole have a reputation for high quality. Apart from wine-making practices, other CMO measures can play an important role in gearing production improving quality. One example is the programme for restructuring vineyards introduced in the 1999 reform, which has supported the reconversion of vineyards with a view to adapting wine production to consumers demand for quality.

Option 1: Status quo, with possibly some limited adjustments

In this scenario, there would be **no new impact** on wine quality compared to the existing situation, therefore the option can be considered to have neutral effects.

Options 2–3–4

In these three options, the main contribution improving wine quality is the abolition of market measures, which currently provide support mainly to lower-quality wines, thus encouraging continued production. The improved market orientation of the CMO proposed in these options should tend to **favour the segment of higher quality wines**, which are increasingly appreciated by consumers.

The abolition of Community aid for **distillation of the wine by-products,** maintaining the prohibition on grape overpressing as wine-making practice, should not have any impact on overall wine quality. Appropriate controls could prevent any fraudulent overpressing practices which could otherwise jeopardise quality.

Finally, the greater flexibility introduced with respect to wine-making practices should only enhance the scope for innovative techniques without giving rise to any risk of lower wine quality.

5.5.2. Health and consumer protection policy

Although a moderate alcohol consumption may be beneficial to health (reduction of coronary heart diseases and type II diabetes risks), any abuse is obviously harmful, both in terms of damage to health (liver cirrhosis and alcohol-related cancer), and because of the adverse impact on road safety. Moreover, the social costs of alcohol harm are also very high. In recent years concerns have grown about the increasing trend in alcohol consumption among young people, particularly of spirit-based mixed drinks.

Recent studies appear to show a short-term relation between price and alcohol consumption, given that increased taxes on alco-pops have led to a drop in consumption. This link seems to be even more evident for young consumers, who tend to opt for low-cost alcoholic beverages, especially when their only intention is to drink to intoxication.

In the existing wine CMO, some market measures have an adverse impact on public health. **Potable alcohol distillation** is a controversial measure, because it heavily subsidises the transformation of wine into a beverage of a higher alcohol content. Moreover, by allowing cheaper production of wine spirits, it encourages demand, which conflicts with concerns about the risks of damage to health. Secondly, the **aid for must** has led to an artificial expansion in the use of enrichment, which is intended to increase the alcohol strength of wine and allows higher yields, and hence lower wine quality and production costs. On the other hand, the restructuring scheme might have a beneficial impact on public health, because it aligns production with the demand for higher price quality wines, often consumed with meals and in moderation.

Finally, the existing **quality regulatory framework and the labelling rules** seem to be geared rather to the producer consensus than to consumer protection. **They lack clarity and transparency**, and tend to **confuse consumers**, preventing them from appreciating the qualitative differences between products.

Option 1: Status quo, with possibly some limited adjustments

Under this option, subsidies to market measures, particularly potable alcohol distillation and aid for must would be maintained or not sufficiently cut, thus leading to **inconsistency with public health policy**. The existing problems of quality policy and the labelling rules would remain unchanged.

Options 2–3–4

The abolition of subsidised potable alcohol distillation and of aid for must, and, more generally, the idea of reducing surpluses through gearing production to market, are likely to have a **beneficial impact on public health**. Option 2 would allow the most rapid absorption of the wine surplus and avoid a sharp fall in the wine price in the short term (see section 5.1.2).

Moreover, the proposed simplification of quality policy, geographical indication system and labelling rules could **rightly address concern for consumer information and health protection**. Education and information campaigns proposed under option 2 could provide additional instruments to enhance **consumer awareness** vis-à-vis wine labelling.

5.6. Impact on management efficiency

Reform of the wine sector is expected to bring about improvements in management efficiency, taking into account the shortcomings of the current CMO in this regard. This can achieved by simplifying regulation, which would help to limit management and statistical monitoring costs, ease implementation and controls, and hence reduce the risk of fraud and misuse of public funds. Simpler and clearer rules are easier for operators to understand and obey, and also for national authorities to control.

In addition, increased efficiency can be achieved by increasing subsidiarity giving to Member States more freedom to decide the type of measures they need to best suit their specific situation.

Overall, option 1 would bring no improvements while the three others would have various advantages, depending on the option considered.

Simplification

Simplification is a major goal of all European legislation, particularly so in a sector where the regulations have become highly complex, in many ways hampering its efficiency.

Option 1, the status quo, even with some improvements, would not allow this goal to be achieved, as all the complex measures currently applied would be maintained. In particular for the two acceding Member States, in spite of the efforts undertaken in the enlargement process to implement the *acquis*, the current system would certainly prove very difficult to apply.

Option 2 (profound CMO reform), and particularly option 3 (new CAP-type reform), would allow far-reaching simplification in the following ways:

- under option 2, ending some complex measures (planting rights, distillations, private storage of wine and public storage of alcohol, etc.), in some case after a transitional period, improving the measures maintained (grubbing-up, restructuring) and carefully screening the types of measures to be introduced to ensure they meet simplification requirements, would guarantee a sound new legal framework which would be easier for the Member States to monitor;
- under option 3, incorporation in the single farm payment system and the corresponding abolition of crop specific measures would, in time, clearly simplify implementation.

Option 4 (deregulation) would, by definition, allow the most radical legal simplification.

Administrative and statistic monitoring

One of the first consequences of simplifying of the wine legislation would be to improve the administration and monitoring of the sector, notably as regards data collection and statistical treatment.

The current system of statistical monitoring, including the vineyard register, is rather cumbersome; consequently its implementation has been problematic and not always cost effective at Community level or at Member States level. It must be fundamentally reshaped.

While option 1 (improved status quo) would not allow this goal to be achieved, options 2 (profound CMO reform) and 3 (CAP-type reform) would. Option 4 (deregulation of the wine market) would allow radical simplification of the data needed and consequently monitoring.

The main improvements would have to include:

- a simplified EU system of information on wine and vineyards;
- a clear definition of the new statistical requirements in relation to other information and reporting requirements, to be decided upon in the framework of the EU statistical programme;
- improvement of vineyard registers and inventories as the main source of information to meet the new statistical requirements as well as other information and reporting requirements.

Controllability

Another consequence of a more straight-forward set of measures would be, through clearer rules, to allow a greater controllability and prevent frauds and misuse of public funds.

Option 1, the status quo, even improved, would not allow this goal to be achieved, as all the complex measures currently applied which have evident shortcomings would be maintained.

Option 2 (profound CMO reform) and particularly option 3 (CAP-type reform), would allow far-reaching improvements in the two following different ways:

- under option 2, withdrawing some complex measures (planting rights, distillations, private storage of wine and public storage of alcohol), in some case after a transitional period, improving the measures maintained (grubbing-up, restructuring) and carefully screening the types of measures to be introduced would prevent many problems (such as illegal plantings) and substantially limit the cost of controls (in particular with the end of the use of sucrose combined with the abolition of must aid). However, the implementation of new measures under the national envelop would probably require new provisions to control correct public spending and avoid frauds;
- under option 3, incorporation in the single payment system and the corresponding end of crop-specific measures would, in time, allow clear rationalisation of controls.

Option 4 (deregulation) would, by definition, mean the most radical simplification of controls and limiting the risk of frauds.

Subsidiarity

Option 1 (improved status quo) would not allow any improvement in subsidiarity, which is currently limited to the ban on grubbing-up and add some topping up of premia.

Options 2 (profound CMO reform) and to a lesser extent option 3 (CAP-type reform) would increase Member States' freedom to chose measures and ways to implement them, notably, in the case of option 2, in the framework of the rural development programmes.

Option 4 (deregulation) would also increase subsidiarity but in the sense that very few measures would be retained at European level in the CMO and that funds would be made available for rural development measures to be decided by the Member State under its rural development plan.

Budget

Option 1 (improved status quo) would, with the severe deterioration of the market balance (see part 5.1), put the current budget devoted to the wine sector under pressure. Finally, a higher expenditure in the wine sector could also result in a general negative impact for agricultural producers in general, which would be penalised, in the context of the mechanism of financial discipline, through cuts in the direct payments.

Options 2 (profound CMO reform) and option 3 (CAP-type reform) would be based on the principle of budget neutrality and achieve a better value for money use of community funds.

Option 4 would, in the short term, reduce the budget needs for the sector. This would be the consequence of a rapid withdrawal of all the measures currently financed without the introduction of new measures. However, the severe socio-economic consequences of this option could have substantial indirect budget costs, notably in the long term.

6. COMPARING THE OPTIONS

Table 3 summarises the various impacts of the different policy options.

Option 1, slightly adjusting of the existing CMO, would not achieve the objectives of the reform. The status quo appears unsustainable in the long term, because it does neither tackle the problem of the structural imbalance of the wine market, nor enhance the competitiveness of European wine, nor improve consistency with other Community policies.

Option 2, profound reform of the CMO, would address the problems of the wine sector in both the short and long term, by concentrating budgetary resources on measures to achieve **smooth and rapid stabilisation of the market** and the **structural adjustment of the sector**. Introducing national envelopes and transferring funds to rural development would leave Member States and wine regions scope to adapt the measures available at Community level to their specific conditions and needs, thus allowing greater subsidiarity.

Option 3, the general introduction of decoupled support for wine producers, would also allow **most policy objectives to be achieved in the long term**, in particular market equilibrium in the wine sector. Moreover, it would address environmental concerns, since it allows direct application of cross-compliance to the whole vine area. However, as in the case of complete deregulation, albeit to a lesser extent**, in the short and medium term the sector would undergo quite a tough adjustment process**. Public intervention would mainly focus on supporting farm incomes rather than rapidly improving the market balance by providing help with structural adjustment. Furthermore, an even distribution of public support to the whole vine area would raise problems of political acceptability and of overcompensation of quality wine producers.

Option 4, complete deregulation of the wine sector, would **achieve a certain number of policy objectives in the long term**, in particular wine market equilibrium and increased competitiveness of wine production. However, the serious adjustment that immediate implementation of this policy would require and the lack of structural measures accompanying this process would produce **severe, negative short-term impacts** on the sector and the rural economy of the regions concerned as a whole.

Table 3: Summary table comparing the impacts of the options

SUMMARY IMPACTS	Option 1: Improved status quo	Option 2: Profound reform of the CMO	Option 3: Reform along CAP reform lines	Option 4: Deregulation
Market balance	Increasing surplus	Smoothest achievement of balance	Increasing surplus in the short and mid term Market equilibrium in the long term	Increasing surplus in the short and mid term Market equilibrium in the long term
Prices	Sharp decrease due to unsustainability of the system	Decrease in the short term Recovery after achievement of balance	Sharp decrease in the short and mid term Recovery after achievement of balance	Very sharp decrease in the short and mid term Recovery after achievement of balance
Agricultural incomes	Progressive decrease due to unsustainability of the system	Decrease in the short term Recovery after achievement of balance	Decrease in the mid term Recovery after achievement of balance No safety net mechanism	Very sharp decrease in the short and mid term Recovery after achievement of balance No safety net mechanism
Competitiveness	No improvement	Rapid improvement through economic sustainability and improved regulatory measures allowing flexibility and innovation	Improvement in the long run through economic sustainability and improved regulatory measures allowing flexibility and innovation	Strong improvement in the long run through economic sustainability, freedom to farm and improved regulatory measures allowing flexibility and innovation
Economic and social impacts on rural areas	Progressive deterioration due to unsustainability of the system	Improvement due to smooth achievement of economic sustainability	Risks due to heavy restructuring needs	Important risks due to heavy restructuring needs and possible production shifts between regions
Environment	No improvement	No easy solution to apply cross-compliance on all vine area Shifts to RD can be used to encourage more environmentally-friendly measures	Direct applicability of general cross compliance	Very difficult to apply cross-compliance No available funds to encourage more environmentally-friendly measures
Trade WTO compatible	Different measures potentially under attack	Most problems solved	Most problems solved	Most problems solved
Wine quality	Neutral	Increase through better market orientation	Increase through better market orientation	Increase through better market orientation
Health / consumer	No improvement	Stop to unacceptable support to distillation into potable alcohol Labelling rules more transparent and consumer oriented	Stop to unacceptable support to distillation into potable alcohol Labelling rules more transparent and consumer oriented	Stop to unacceptable support to distillation into potable alcohol Labelling rules more transparent and consumer oriented
Budget	Increasing pressure	Neutral	Neutral	Possibility of savings
Subsidiarity	No improvement	Much more flexibility with national envelope and increased RD funds	Flexibility in the implementation of the SPS	Possibly more flexibility via shift to RD
Simplification, applicability controllability	No improvement	Moderate simplification	Strong simplification, but specific operational difficulties in implementing SPS in wine sector	Most problem solved

7. MONITORING AND EVALUATION

Monitoring and assessing the economic, social and environmental effects of EU public policies has become a standard element of the political process.

Most EU legislative acts include monitoring of their implementation by Member States, and of their impact and effectiveness at EU level in order to propose further action or redirection of the measures, if necessary.

Many of the actions needed to apply the common policy on wine to be developed by Member States and relevant stakeholders. Considerable experience in monitoring exists in the Commission departments and in the Member States. Hence, there is scope for cooperation, sharing of information, and improvement of core indicators and enhancement of analytical tools used to monitor and assess policies. Existing statistical systems covering wine production potential, market trends, micro- and macro-economics, the evolution of regional patterns, and the environment provide a complex framework and need to be simplified, adapted and reshaped to provide sufficient information in this context.

The reformed wine policy would need to be monitored and evaluated in relation to a whole range of potential impacts identified in this report. This needs an assessment of progress towards meeting the objectives listed in part 3 and of all types of impacts identified in part 5.

The basis for reporting on progress should be a common framework for monitoring and assessment, to be proposed in the legal act.

The new wine CMO will be included in the multi-annual evaluation programme for CAP policies.

ANNEXES

ANNEX 1:
MANDATE OF THE INTER-SERVICE STEERING GROUP

1. Commission decision

When adopting its working program for 2006[22], the Commission has envisaged a Communication on the reform of the common market organisation in wine[23].

In accordance with the plan for better legislation and with the guidelines for the execution of Impact Assessments[24], a proposal for the reform of the wine CMO must be accompanied by an Impact Assessment directed by an Inter-Service Group (ISG)[25].

2. Framework

The European wine sector is the most important worldwide: The EU is the **first wine producer** in the world (45% of vine areas and 60% of wine production), the **first consumer** (60%) and the **main actor in the international trade** (at the same time the first exporter and the first importer).

Wine production plays a primary role in the agricultural activity of most wine-producing Member States: it represents around 10% of the value of the agricultural production in France, Italy, Austria, Portugal, Luxembourg and Slovenia, and a little less in Spain. The importance of wine production within the economic activity is even greater at regional and local level: for certain regions, the value of wine production exceeds 20% or even 30% of the total agricultural production, and those percentages can be even higher, when considering more restricted geographical areas.

The wine CMO, which was established in 1962, is one of the largest and most complex in the common agricultural policy. This is because it covers not only the issues that many market organisations deal with, such as price, intervention and trade, but also issues specific to the wine industry (provisions concerning the production, transport and processing of wine products and wine-making practices. The CMO has been reformed many times, the last time in 1999.

The wine CMO is one of the last sectors, which did not undergo the CAP reform process of 2003–2005. Its instruments do not seem adequate any longer in the context of the new global market situation, in particular to orient wine production and marketing to the needs of the demand. Currently, the wine sector experiences a critical situation in the most important European markets: on the one hand harvests are often abundant, on the other hand wine consumption is progressively declining and the trade balance deteriorating (strong increase in the imports from third countries and stagnation of exports). This results in an alarming accumulation of wine stocks and in the decline of market prices.

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22 COM(2005) 531 final of 25 October 2005.

23 Regulation (EC) No 1493/1999 of 17 May 1999 (OJ L 179 of 14.7.1999, p. 1).

24 COM(2002) 276 of 05.06.2002 and SEC (2005) 791 of 15 June 2005.

25 *"An Inter-Service Steering Group is compulsory for all items of a cross-cutting nature… to provide specialised inputs and to bring a wider perspective to the process ... making it also easier to reach agreement during the Inter-Service Consultation. […]".*

The reform of the CMO aims therefore at setting provisions to achieve a better balance between supply and demand and to improve the competitiveness of wine produced in the Community, but also to ensure that EU wine production is sustainable and to preserve the authenticity and the traditional character of the product.

On the other hand, health concerns linked to excessive alcohol consumption within certain sectors of society, and in particular young people, can be increasing observed. In this context, DG SANCO has started an impact assessment on alcohol policy. If the timetable of the two exercises makes it possible, it would be appropriate to take into account the results of the abovementioned impact assessment in that concerning the wine reform.

3. Stages in the work of the wine steering group

The stages in the work of the wine steering group should follow the pattern set out in the communication and guidelines on impact assessment, taking also into account the experience acquired with the previous impact assessments in the context of the reform of common market organisations in sugar and tobacco.

3.1 Analysis of problems

"The first question in the process of impact assessment concerns the identification and analysis of the problem or problems in one or more domains. These are described in economic, social and environmental terms."

To identify and analyse the main problems of the wine sector, the following documents will help provide basic information to the Group:

– the independent evaluation of the CMO[26] completed in November 2004 in the framework of the evaluation programme of the common agricultural policy;

– the independent evaluation on the environmental impact of the CMOs of permanent crops, which is being finalised;

– the Commission report to the European Parliament and the Council on the management of planting rights[27];

– an internal economic report on the situation of the wine market, which is being finalised;

– an internal report on the Common Market Organisation in wine, which is being finalised;

The identification of the main problems to deal with in the impact assessment will be completed during the phase of consultation (point 4).

3.2 Identifying the objectives

"On the basis of the analysis of the problems, the objectives of the action will be expressed in terms of the results expected by a given date."

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26 INNOVA report, http://europa.eu.int/comm/agriculture/eval/reports/wine/index_en.htm.

27 COM(2004) 161 final of 12.3.2004.

In the framework of the wide political strategies of the European Union (Lisbon strategy and strategy for the sustainable development) and of the orientations of the reformed CAP, the Group will try to identify the specific objectives of the wine sector (market equilibrium, improvement of competitiveness, combination of tradition and innovation, etc.), always taking into account the constraints linked to the international commitments and the financial perspectives of the Union.

3.3 Identifying the options

"Alternative means or instruments for achieving the objectives should always be considered from the initial stages of formulating proposals. The principles of subsidiarity and proportionality must also be taken into account and considered all through the impact analysis process. The analysis must always include the "no policy change" scenario as a point of reference for comparison with other options."

The Group will have to choose a set of options, which could potentially reach the objectives of the reform, and which are sufficiently differentiated to express the different views about the future of the sector, thus encouraging the impact assessment of a wide range of possibilities. These options have to take into account the general approach adopted in 2003 for the CAP reform, the specificities of the wine sector and the international agreements of the Union with third countries.

With a view to presenting more integrated proposals at Commission level, the group could consider the assistance that other Commission policies and instruments might bring to achieving these objectives or to alleviating the costs of the reform for the different parties concerned.

3.4 Analysing the impacts

"For the policy option retained, and where possible for selected alternatives all relevant positive and negative impacts should be examined and reported on in the impact analysis, with a specific emphasis on their environmental, economic and social dimensions. This process has two stages: first the relevant impacts are identified ("screening"), then they are assessed in qualitative, quantitative and/or monetary terms ("scoping")."

The directorates-general participating in the ISG will be invited to examine the impact of the different reform options for the wine CMO on their area of competence. Besides the three dimensions mentioned in the orientations on impact assessments (environmental, economic and social), other domains have to be considered, e.g. regional policy, public health.

3.5 Comparing the options

"After having analysed the corresponding impacts, the next step consists in comparing the impacts in order to allow the evaluation of strengths and weaknesses of each policy option. This can allow drawing the conclusion that one option is superior to the others. However, it is important to stress that the final decision on whether, and how, to proceed is political."

3.6 Monitoring and *ex-post* evaluation

"The impact assessment should identify any possible difficulties in implementing the options assessed and describe how these will be taken into account, for example in the choice of

implementation periods or the gradual phasing-in of a measure. The subsequent ongoing or ex-pos*t evaluations will follow the rules of the Communication on Evaluation, i.e. an overall* ex-post *or interim evaluation at a periodicity not exceeding six years, depending on the nature of each activity"*

4. Consultation

"The purpose of the extended impact assessment is to… consult with interested parties and competent experts… to supplement and validate data collection ... and to allow a debate on the wider issues."

First of all, the Group will benefit from the results of the evaluation of the CMO. Furthermore, the process of identifying the problems and the impact assessment of the options will be deepened in the context of a large *stakeholders* consultation, which will take place during the month of February 2006, with the participation of dozens of experts representing all stakeholders interested to the reform of the wine sector (producers, retailers, consumers, public health operators, local administrators of producing regions, etc.).

5. Timetable

15 December 2005	Constitution of the Steering Group: working plan and approval of the mandate. Presentation of the wine market
January 2006	Description of the wine CMO
	Critical analysis of the CMO measures
16 February 2006	Participation of the Steering Group to the "*stakeholders"* consultation
February – March 2006	Analysing the problems, defining the objectives, identifying the impacts, outlining draft options
	Defining the specific contribution
March – April 2006	Preparation and discussion of the specific contributions
April 2006	Discussion and approval of the impact assessment report
May – June 2006	Inter-service consultation and adoption of the Communication by the Commission.

ANNEX 2:
MID-TERM FORECASTS FOR THE EU-27 WINE SECTOR TO 2010–11

The table below represents the summary market balance of the EU-27 wine sector to the year 2010–11, as forecast by DG AGRI, on the assumption of an unchanged policy framework and based on a "normal year" in terms of wine production.

On the basis of different assumptions regarding the evolution in vine areas, wine yields, consumption trend and trade balance, three alternative scenarios are built: "average" (or "most likely"), "low surplus" (or "most optimistic"), and "high surplus" (or "most pessimistic").

For each of the three scenarios, the market balance, defined as the difference between the total availability and the total use of wine production, is estimated. Two alternative market balance indicators are calculated, which differ in the way they consider the volumes of wine distilled in the context of the potable alcohol distillation. In the SURPLUS 1, those volumes are considered as a production surplus rather than a real market outlet, whereas in SURPLUS 2, they are regarded as a market outlet of wine production and therefore deducted from the production surplus.

Table 4: Supply balance for the EU-27 wine sector at the horizon 2010–11

	olympic AVERAGE 1999-2003	WINE YEAR 2003/04	WINE YEAR 2004/05	FORECASTS 2010/2011		
				Average Scenario	Low surplus Scenario	High surplus Scenario
PRODUCTION	180.4	166.8	191.5	178.8	173.2	183.3
SURPLUS 1 (a)	21.9	14.3	34.8	27.0	18.8	38.0
in % of the production	12.2%	8.6%	18.2%	15.1%	10.9%	20.7%
SURPLUS 2 (b)	10.5	4.0	23.8	15.0	7.8	25.0
in % of the production	5.8%	2.4%	12.5%	8.4%	4.5%	13.6%

(a) including wine withdrawn for distillation into potable alcohol
(b) excludes wine withdrawn for distillation into potable alcohol

ANNEX 3:
IMPACT ON PRICES

Regression analysis between average annual prices of table wine and wine stocks

Option 1: Status quo

Regression analysis between EU average annual prices of table wine and total wine stocks
Stocks in 1 000 hl and prices in €/°vol/hl

Historic data

Vintage year	Total wine stocks on 31.07	Average price
2000	142 221	3.23
2001	161 900	2.78
2002	156 725	2.84
2003	151 704	3.32
2004	155 636	3.36
2005	174 914	2.72
Avearge 2000-05	**157 183**	**3.04**

Simulation
stocks increasing by 9 Mio. hl per year

Vintage year	Stocks on 31.07	Simulated price (linear model)	% variation compared to year 0	Simulated price (exp model)	% variation compared to year 0
year 0	157 183	3.04	-	3.03	-
year 1	166 183	2.86	**-6%**	2.86	**-6%**
year 2	175 183	2.69	**-12%**	2.69	**-11%**

Option 2: Profound reform of the CMO

Regression analysis between EU average annual prices of table wine and total wine stocks
Stocks in 1 000 hl and prices in €/°vol/hl

Historic data

Vintage year	Total wine stocks on 31.07	Average price
2000	142 221	3.23
2001	161 900	2.78
2002	156 725	2.84
2003	151 704	3.32
2004	155 636	3.36
2005	174 914	2.72
Avearge 2000-05	**157 183**	**3.04**

Simulation
stocks increasing by 8.2 Mio. hl in the year 1 and by additional 4.2 Mio. Hl in the year 2

Vintage year	Stocks on 31.07	Simulated price (linear model)	% variation compared to year 0	Simulated price (exp model)	% variation compared to year 0
year 0	157 183	3.04	-	3.03	-
year 1	165 383	2.88	**-5%**	2.87	**-5%**
year 2	169 583	2.80	**-8%**	2.79	**-8%**

Option 3: Reform along CAP reform lines

Regression analysis between EU average annual prices of table wine and total wine stocks
Stocks in 1 000 hl and prices in €/°vol/hl

Historic data

Vintage year	Total wine stocks on 31.07	Average price
2000	142 221	3.23
2001	161 900	2.78
2002	156 725	2.84
2003	151 704	3.32
2004	155 636	3.36
2005	174 914	2.72
Avearge 2000-05	**157 183**	**3.04**

Simulation
stocks increasing by 12.2 Mio. hl per year

Vintage year	Stocks on 31.07	Simulated price (linear model)	% variation compared to year 0	Simulated price (exp model)	% variation compared to year 0
year 0	157 183	3.04	-	3.03	-
year 1	169 383	2.80	**-8%**	2.80	**-8%**
year 2	181 583	2.56	**-16%**	2.58	**-15%**

Option 4: Complete deregulation

Regression analysis between EU average annual prices of table wine and total wine stocks
Stocks in 1 000 hl and prices in €/°vol/hl

Historic data

Vintage year	Total wine stocks on 31.07	Average price
2000	142 221	3.23
2001	161 900	2.78
2002	156 725	2.84
2003	151 704	3.32
2004	155 636	3.36
2005	174 914	2.72
Avearge 2000-05	**157 183**	**3.04**

Simulation
stocks increasing by 19 Mio. hl per year

Vintage year	Stocks on 31.07	Simulated price (linear model)	% variation compared to year 0	Simulated price (exp model)	% variation compared to year 0
year 0	157 183	3.04	-	3.03	-
year 1	176 183	2.67	**-12%**	2.67	**-12%**
year 2	195 183	2.30	**-24%**	2.36	**-22%**

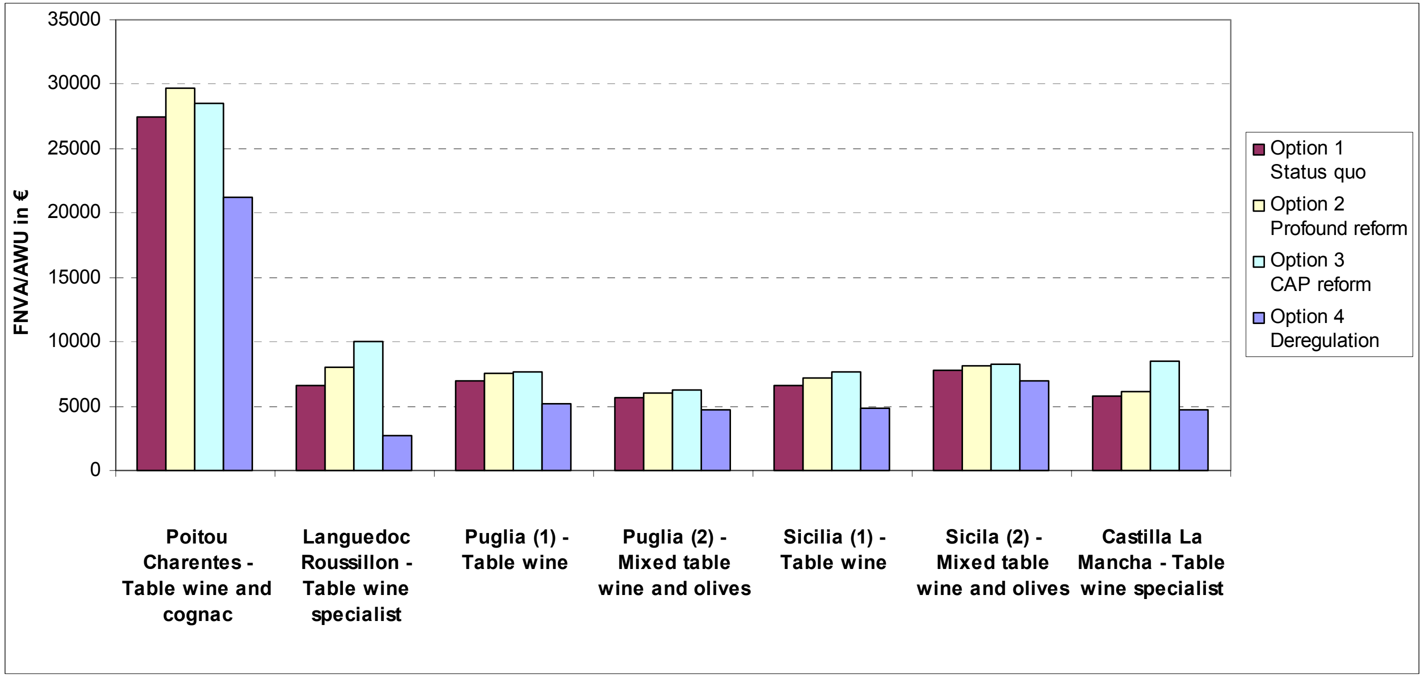
ANNEX 4:
IMPACTS ON AGRICULTURAL INCOMES

Summary results of a model-farm approach on table wine farms in some EU regions
Variation of agricultural income (FNVA/AWU) in %

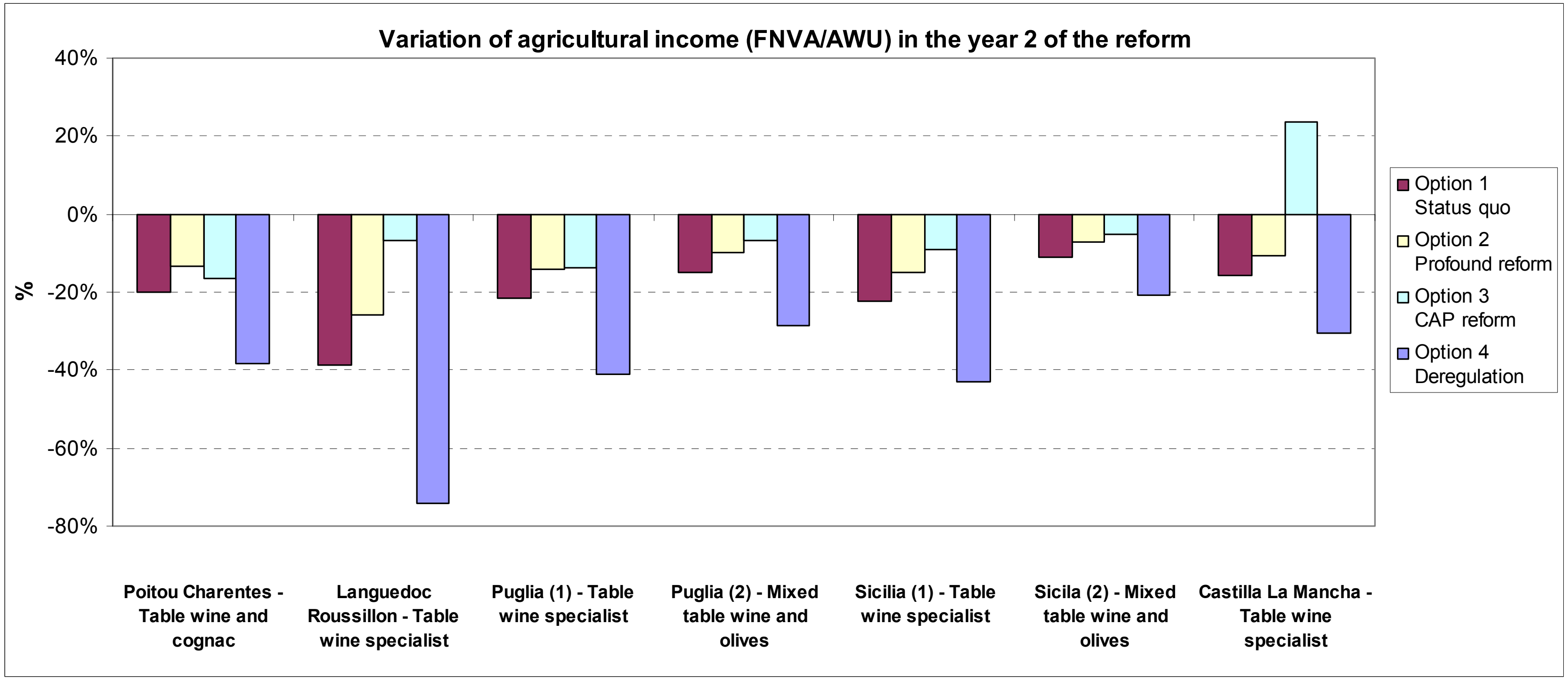
	First year				Second year			
	Option 1 Status quo	Option 2 Profound reform	Option 3 CAP reform	Option 4 Deregulation	Option 1 Status quo	Option 2 Profound reform	Option 3 CAP reform	Option 4 Deregulation
Price variation	-6%	-5%	-8%	-12%	-12%	-8%	-16%	-23%
Income variation								
Poitou Charentes - Table wine and cognac	-10%	-8%	-3%	-20%	-20%	-13%	-17%	-38%
Languedoc Roussillon - Table wine specialist	-19%	-16%	19%	-39%	-39%	-26%	-7%	-74%
Puglia (1) - Table wine specialist	-11%	-9%	0%	-21%	-21%	-14%	-14%	-41%
Puglia (2) - Mixed table wine and olives	-7%	-6%	3%	-15%	-15%	-10%	-7%	-29%
Sicilia (1) - Table wine specialist	-11%	-9%	6%	-23%	-23%	-15%	-9%	-43%
Sicila (2) - Mixed table wine and olives	-5%	-5%	2%	-11%	-11%	-7%	-5%	-21%
Castilla La Mancha - Table wine specialist	-8%	-7%	34%	-16%	-16%	-11%	24%	-30%

Source: DG AGRI - FADN

FNVA/AWU in the second year after the reform



Source: DG AGRI - FADN



Source: DG AGRI – FADN

ANNEX 5:
LIST OF ACRONYMS

AWU	Annual Working Unit
CAP	Common Agricultural Policy
CMO	Common Market Organisation
DG AGRI	Directorate-General for Agriculture and Rural Development
EAGGF	European Agricultural Guidance and Guarantee Fund
EU	European Union
FADN	Farm Accountancy Data Network
FNVA	Farm Net Value Added
GI	Geographical Indications
ICM	Integrated Crop Management
IPM	Integrated Pest Management
ISG	Inter-Service Steering Group
MS	Member States
OIV	International Organisation of Vine and Wine
OP	Oenological Practices
PDO	Protected Denominations of Origin
PGI	Protected Geographical Indications
QWpsr	Quality Wine produced in specified regions
RD	Rural Development
SPS	Single Payment Scheme
TBT	Technical Barriers to Trade
TRIPS	Trade-related aspects of Intellectual Property rights
TW	Table Wine
UAA	Utilised Agricultural Area
WMP	Wine Making practices
WTO	World Trade Organisation.