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TARGETING OF AID FOR THE  
MODERNISATION OF  
AGRICULTURAL HOLDINGS



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# TARGETING OF AID FOR THE MODERNISATION OF AGRICULTURAL HOLDINGS

(pursuant to Article 287(4), second subparagraph, TFEU)

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**REPLY OF THE COMMISSION**

# GLOSSARY

**Axes:** Rural development in the 2007–13 programming period is implemented under four thematic axes, which represent coherent groups of rural development measures.

**CAP:** Common agricultural policy: the set of legislation and practices adopted by the European Union to provide a common, unified policy on agriculture.

**CMEF:** Common Monitoring and Evaluation Framework.

**Community strategic guidelines:** With these strategic guidelines the Council identifies the European Union's priorities under the European Agricultural Fund for Rural Development (EAFRD). It establishes a link with the objectives established by the **Lisbon** and **Göteborg** European Councils and translates them into rural development policy. The idea is to ensure the consistency of rural development with other EU policies, in particular in the field of cohesion and environment, and accompany the implementation of the new common agricultural policy (CAP) and the restructuring involved.

**Deadweight:** A situation where a subsidised project would have been wholly or partly undertaken without the grant aid.

**EAFRD:** European Agricultural Fund for Rural Development.

**EERP:** European Economic Recovery Plan.

**GVA:** Gross value added.

**Göteborg strategy:** The Göteborg strategy was launched in 2001 as the first EU sustainable development strategy.

**'Health Check':** The common agricultural policy was adjusted in 2009 so that farmers would be better placed to respond to market signals, the administration of direct payments would be simplified and farmers would be helped to meet the new challenges of the future, in particular that of climate change. This adjustment is known as the 'Health Check'.

**Lisbon strategy:** The EU strategy for growth and jobs launched in 2000, which aims at generating growth and more and better jobs by investing in skills, the greening of the economy and innovation.

**Measure:** An aid scheme for implementing a policy. A measure defines the rules for the projects that can be financed within an axis.

**M121:** 'Measure 121' — Modernisation of agricultural holdings.

**Operation:** A project, contract or other individual arrangement, co-financed by the EAFRD.

**Programming period:** Multiannual framework to plan and implement EU policies such as rural development policy; the rural development period runs from 2007 to 2013.

**RDP:** Rural development programme, a programming document prepared by a Member State and approved by the Commission to plan and implement the EU's rural development policy. An RDP may be prepared on regional or national level.

## EXECUTIVE SUMMARY

### I.

The European Union (EU) co-finances investment projects on agricultural holdings through its rural development policy. Under the current programming period for 2007–13, 11,1 billion<sup>1</sup> euro is budgeted for a specific investment measure called 'modernisation of agricultural holdings'. EU funding is further complemented by national public expenditure to cover part of the total investment cost.

### II.

The Council has defined in its Community strategic guidelines for rural development specific EU priorities to be addressed through the rural development policy and Member States are requested to target funding on clearly defined objectives reflecting identified needs in the Member States' rural areas.

### III.

In 2009, to further strengthen operations related to the EU's priorities of climate change, renewable energy, water management, biodiversity and the restructuring of the dairy sector, an extra 4,95 billion euro was allocated to rural development measures including modernisation through the 'Health Check' and the European Economic Recovery Plan (EERP).

### IV.

The audit examined **whether EU aid for the modernisation of agricultural holdings was directed to EU priorities and specific needs in Member States.**

### V.

The Court found that:

- (a) Whilst the measure 121 'modernisation of agricultural holdings' was achieving its nominal objective of modernisation, this was almost inevitable as any investment or purchase of new equipment results in some degree of modernisation. The measure has the potential to provide greater value for money if the funds available were better targeted.
- (b) The extent of targeting varies significantly between the Member States reviewed. Some target effectively whereas others did not apply the good selection criteria they had established or have weak targeting systems.

<sup>1</sup> Financial data as at January 2012.



## EXECUTIVE SUMMARY

- (c) Member States' rural development programmes (RDPs) often contain insufficient information to demonstrate that investment aid has been adequately targeted. Information is likewise lacking on the project selection process. Consequently, the Member States' project selection procedures are often not known by the Commission when it approves the RDP.
- (d) The Common Monitoring and Evaluation Framework does not generate the type of data necessary to allow progress in the achievement of EU priorities to be monitored; the data was found not to be reliable and it does not allow comparisons between Member States (and/or regions) to be drawn.
- (e) Further strengthening of operations related to the EU priorities was not achieved by some Member States due to the substitution of the extra funding with funds already programmed for the measures concerned prior to the 'Health Check'.
- (f) The procedures for establishing the viability and sustainability of a holding or the investment project were not effective in all Member States.
- (g) The Court found that the deadweight risk linked to the retroactive approval of investments which had already started persists.
- (c) Where it is the intention to earmark particular measures and budgetary allocations to target specific priorities, as was the case with the 'Health Check', to ensure that the funding has an additional effect the Commission should propose legislation to make this requirement specific in the underlying EU regulations.
- (d) Member States should put effective procedures in place, proportionate to the risks, to ensure that grants are not given to projects where the financial viability of the investment or the sustainability of the holding is in doubt.
- (e) The Commission should encourage Member States to follow good practice whereby project expenditure is eligible only from the date the grant is approved.

### VI.

On the basis of its findings the Court makes the following recommendations:

- (a) The Commission should not approve RDPs unless they demonstrate that the aid is targeted and include clear and relevant selection criteria addressing EU priorities and national or regional needs.
- (b) The Commission should ensure that for the forthcoming programming period relevant and reliable information is obtained to facilitate management and monitoring of the results of the measure and to demonstrate the extent to which the aid given is contributing to the achievement of EU priorities.

# INTRODUCTION

## RURAL DEVELOPMENT — THE FRAMEWORK OF MEASURE 121

1. The EU has set up a common rural development policy, also known as the 'second pillar' of the common agricultural policy (the 'CAP'). The policy is implemented through multiannual programming periods. The current period runs from 2007 to 2013 and payments must be completed by 2015. The policy is based on the co-financing principle: EU funds are complemented by national funding, and also by private funding. The EU co-finances operations through the European Agricultural Fund for Rural Development (EAFRD), for which 96 billion euro was budgeted for the programming period 2007 to 2013. This includes almost 5 billion euro supplementary funding made available following the 'Health Check' and the European Economic Recovery Plan (EERP)<sup>2</sup>.
2. The policy is based on three themes ('axes'), plus a horizontal axis known as Leader. The three axes are:
  - Axis 1: Improving the competitiveness of the agricultural and forestry sector;
  - Axis 2: Improving the environment and the countryside; and
  - Axis 3: Improving the quality of life in rural areas.
3. The Community strategic guidelines set at Community level the strategic priorities for rural development, while the main rules governing rural development policy for the period 2007 to 2013, as well as the policy measures available to Member States and regions, are set out in Council Regulation (EC) No 1698/2005<sup>3</sup>.
4. Within each axis, legislation has defined a set of 'rural development measures' which are specific instruments to implement the axis.
5. The Member States draw up their own rural development programmes (RDP), at national or regional level, in which they define a strategy and propose the measures they wish to use to address their identified needs. These RDPs are the chief programming instrument through which the EU funding is channelled. These programmes are approved by the European Commission. A total of 97 RDPs were approved for the current programming period.

<sup>2</sup> In 2007, the European Commission proposed a 'Health Check' on the CAP which was subsequently adopted by the Council in 2008. Subsequent to the 'Health Check', and as a response to the 2008 economic crisis, the Commission drew up the EERP which was agreed by the Council in December 2008.

<sup>3</sup> Council Regulation (EC) No 1698/2005 of 20 September 2005 on support for rural development by the European Agricultural Fund for Rural Development (EAFRD) (OJ L 277, 21.10.2005, p. 1).

6. In order to monitor and evaluate the implementation of rural development policy, the European Commission and the Member States have defined the Common Monitoring and Evaluation Framework (CMEF). The CMEF provides a set of indicators which are intended to assess, at output, result and impact level, how far the expected objectives have been achieved.
7. This report addresses the specific measure 121 under axis 1, which subsidises investment projects aimed at modernising agricultural holdings.

### **WHAT IS 'MEASURE 121'?**

8. Measure 121 finances investments in agricultural holdings. These investments may range from simple items such as farm tools and wooden fruit boxes up to complex projects such as biogas installations. Its specific EU budget totals 11,1 billion euro (financed through the EAFRD)<sup>4</sup>, which represents, over the whole 2007–2013 programming period, around 11 % of all the EU's planned spending on rural development in the EU. All Member States have chosen to use measure 121.

<sup>4</sup> Financial figures as at January 2012, including 630 million euro from the 'Health Check' and the EERP.

## BOX 1

**EXAMPLES OF THE RANGE AND TYPE OF INVESTMENTS FINANCED BY MEASURE 121**

Photos taken during the audit illustrate how investment items financed through measure 121 range from forklifts ...



... to more complex machinery such as tractors and precision planters ...



... to animal housing equipped with mobile straw-spreading devices.

9. The main rural development regulation sets the standard aid rate for total public aid (that is from the EAFRD and national or regional public budgets) at 40 % of the eligible investment. Member States may set lower rates or maximum eligible costs, thereby limiting the aid. The standard aid rate may, however, be increased in particular circumstances. Thus, a young farmer may receive up to 50 % of the eligible investment. Farmers in mountainous areas, in other disadvantaged areas or in Natura 2000<sup>5</sup> areas may also receive an additional 10 %. In exceptional cases (i.e. in outermost regions and the smaller Aegean islands), the aid rate may reach up to 75 %. No minimum aid rate is defined by the EU regulations.

<sup>5</sup> 'Natura 2000' areas are specific protected areas of conservation.

<sup>6</sup> Recital 21 of Regulation (EC) No 1698/2005.

<sup>7</sup> Article 26 of Regulation (EC) No 1698/2005.

## TARGETING THE AID

### MEASURE 121 SHOULD ADDRESS EU PRIORITIES AND IDENTIFIED NEEDS

10. The Community strategic guidelines establish the EU priorities for improving the competitiveness of agriculture, which include modernisation, innovation and quality. The preamble to the main regulation, Regulation (EC) No 1698/2005, states the purpose of investment aid for modernisation under measure 121 thus<sup>6</sup>:

'the purpose of Community farm investment aid is to modernise agricultural holdings to improve their economic performance through better use of the production factors including the introduction of new technologies and innovation, targeting quality, organic products and on/off-farm diversification, including non-food sectors and energy crops, as well as improving the environmental, occupational safety, hygiene and animal welfare status of agricultural holdings.'

11. The body of the regulation sets out the eligibility criteria, which define that support should be granted only to investments which<sup>7</sup>:
- improve the overall performance of the agricultural holding; and
  - respect the Community standards applicable to the investment concerned.

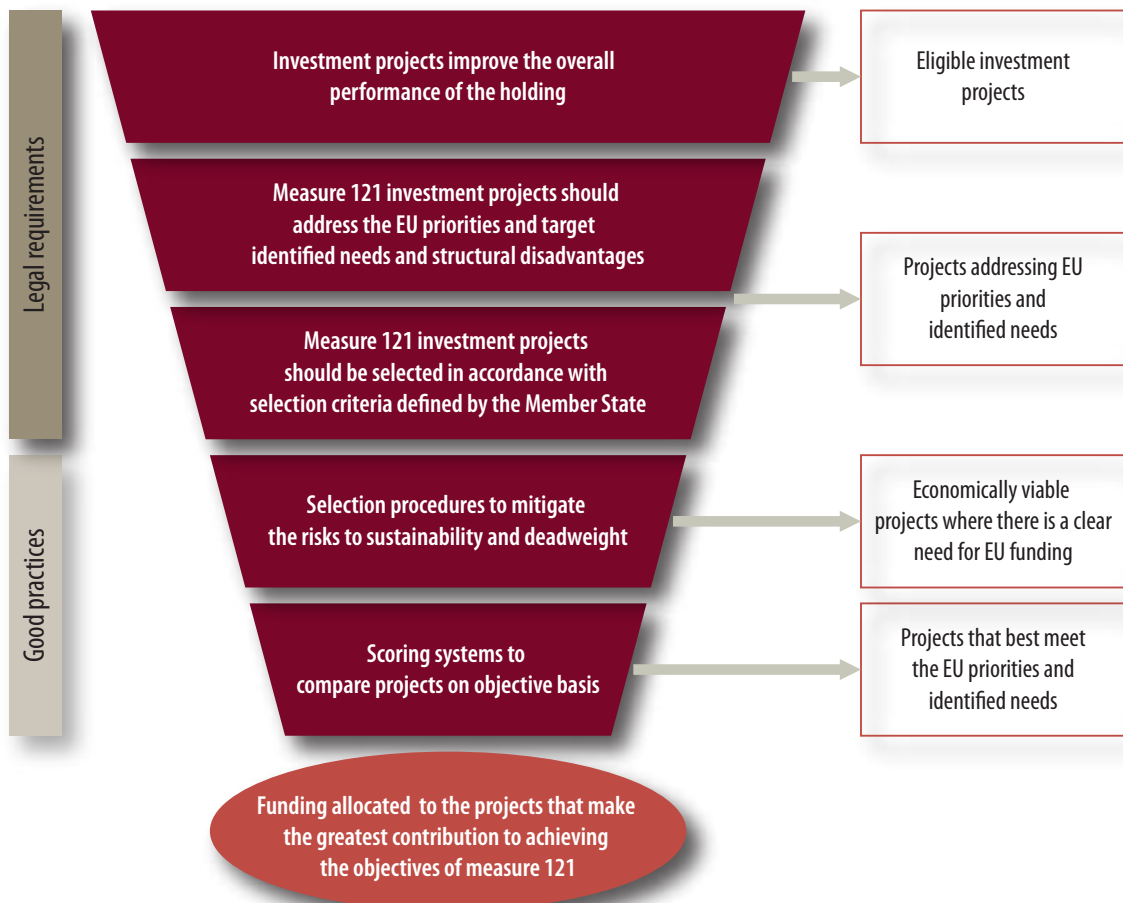
- 12.** The Member States must ensure that investment measures included in their RDPs are targeted on clearly defined objectives reflecting identified structural and territorial needs and structural disadvantages<sup>8</sup>, having regard to the Community strategic guidelines.
- 13.** Member States can take different approaches to achieve this. A first level of targeting may be achieved by setting restrictive eligibility criteria and differentiated aid rates for different types of investment projects, which should be detailed in the RDP. Thus, the Member State may declare certain types of farmers and of agricultural holdings eligible (eligibility of beneficiaries), and set out eligibility criteria for investment projects, either by setting out a 'positive' list of eligible investment types, or defining a 'negative' list of investment items that are not eligible. This can result in regional and sectoral differentiation (by excluding certain sectors from the scope) and setting aid ceilings (linked to the size of projects).
- 14.** The use of basic eligibility criteria, as described in the previous paragraph, may filter out projects that are unrelated to the identified needs and priorities. The regulation, however, requires further targeting: Member States should make a selection from within the population of eligible investment projects submitted, using specific selection criteria<sup>9</sup>.
- 15.** One way of doing this — although not required in the underlying legislation — is to rank project applications by attributing points for each selection criterion addressed. Such scoring systems aim at setting up a list of 'best' projects — those that make the greatest contribution to achieving the objectives set for the measure.

<sup>8</sup> Article 43 of Commission Regulation (EC) No 1974/2006 of 15 December 2006 laying down detailed rules for the application of Council Regulation (EC) No 1698/2005 on support for rural development by the European Agricultural Fund for Rural Development (EAFRD) (OJ L 368, 23.12.2006, p. 15).

<sup>9</sup> Article 71 of Regulation (EC) 1698/2005 requires that projects are selected on the basis of selection criteria to be established by the Member State or region concerned.

16. A diagram of how Member States can target measure 121 is presented in the *Figure*.

FIGURE



## AUDIT SCOPE AND APPROACH

- 17.** The audit examined how the measure ‘modernisation of agricultural holdings’ (measure 121) was being managed by the European Commission and implemented by the Member States. The overall audit question was:

Is EU aid for the modernisation of agricultural holdings directed to EU priorities and specific needs in Member States?

Through this the audit sought to establish if the 11,1 billion euro budgeted for the measure was directed to the projects that best achieve the EU’s priority of modernisation, in particular in the specific respects identified in Regulation (EC) No 1698/2005 (see paragraph 10).

- 18.** The audit also assessed the implementation of the extra funding made available under the ‘Health Check’ and the EERP through measure 121.

- 19.** Finally, the audit assessed whether Member States had introduced effective systems to reduce the risk of financing investments on farms that were not economically viable and to reduce the risk of deadweight.

- 20.** The audit focused on the main stages at which investment aid can be channelled to priorities and identified needs through different aspects of the policy’s framework, namely the EU regulatory framework, the RDP, the Commission’s approval of the RDP and Member States’ implementation of the measure.

- 21.** The audit work covered both the Commission and 10 Member States<sup>10</sup>. At the level of the Commission the design of the measure through the underlying applicable EU legislation<sup>11</sup> and the European Commission’s activities when approving the RDPs submitted by the Member States, and any subsequent follow-up was examined. Seven of the 10 selected Member States (and/or regions in these States) were visited by the audit teams and a further three were subject to a desk review. The audit comprised a documentary review of the underlying RDPs and the relevant national/regional legislation and the procedures put in place for selecting investment projects to be financed by measure 121. To assess the CMEF as a monitoring tool for measure 121, the Court examined the data collected and reported yearly by Member States.

- 22.** The Court reviewed a sample of 100 investment projects approved during 2009<sup>12</sup> by the competent national or regional authorities (10 investment projects for each Member State or region audited) in order to analyse the process by which these projects had been selected. The Court’s auditors visited 21 of the projects in the sample on the spot and interviewed the final beneficiaries.

<sup>10</sup> The audit covered the following national or regional RDPs: Belgium (Wallonia), Germany (Baden-Württemberg), Spain (Catalonia), France (mainland), Italy (Veneto), Luxembourg, Hungary, Poland, Portugal (mainland) and Romania.

<sup>11</sup> Regulation (EC) No 1698/2005 and Regulation (EC) No 1974/2006.

<sup>12</sup> For Italy (Veneto), the sample comprised also projects approved during 2008.



# OBSERVATIONS

## TARGETING THE MEASURE 121 FUNDING TO MEET EU PRIORITIES AND IDENTIFIED NEEDS

### A CERTAIN DEGREE OF MODERNISATION RESULTS FROM THE PURCHASE OF NEW EQUIPMENT OR FACILITIES

- 23.** The Court found that all 100 projects in the sample reviewed had already achieved, or were likely to achieve, the modernisation of the holding and/or the farming sector concerned. This was, however, almost inevitable as investments usually finance new machinery, new equipment, new buildings or the renovation of buildings and a degree of modernisation results from any purchase of new equipment or facilities.
- 24.** Similarly, new investments are likely to automatically address to some extent the EU priorities (see paragraph 10), such as introducing new technologies and improving the environmental, occupational safety, hygiene and animal welfare status of agricultural holdings. Constant advances in technology and environmental standards mean that any new equipment is likely to represent some improvement in energy efficiency and emissions in relation to older equipment. As an example, new animal housing has to meet standards established in EU directives, so will represent some improvement over older facilities in terms of hygiene, animal welfare, occupational safety and environmental protection. However, other EU priorities, such as innovation, quality and diversification, are not necessarily addressed automatically by simply investing in new equipment or facilities.

### CERTAIN MEMBER STATES TARGET THE AID TO PROJECTS THAT ADDRESS IDENTIFIED NEEDS AND EU PRIORITIES ...

- 25.** Where aid is targeted to specific needs in line with the EU priorities, a more effective use of the aid can be achieved. Projects that specifically address agreed priorities and the identified needs should represent better value for money for the EU and national taxpayers who provide the funding.

- 26.** Most Member States applied restrictive eligibility conditions to achieve a basic targeting of the aid. For example:
- in Hungary, the authorities issued calls for project proposals for specific sectors or types of projects such as the modernisation of livestock farms, horticultural equipment, irrigation projects, etc.;
  - in Germany (Baden-Württemberg), field machinery such as tractors was excluded. However, in some Member States such as Poland and Luxembourg, almost any type of farm investment was eligible.
- 27.** Targeting of the aid by giving an incentive to projects that correspond to the needs and priorities identified in the RDP was found in several Member States. For example:
- Luxembourg offered higher rates of aid (an additional 10 % of the project cost) for investments addressing environmental concerns or animal welfare;
  - in Belgium, a 40 % aid rate was applied for projects that improved manure storage and spreading facilities — double the standard rate of 20 %.
- 28.** Two Member States targeted further by selecting the best projects from within those projects they had deemed eligible. Italy (Veneto) and Romania used such selection criteria with other targeting methods in order to address the RDP needs, in line with the EU's priorities.

**BOX 2**

**AN EXAMPLE OF GOOD PRACTICE: ITALY (VENETO REGION) MAXIMISED THE PROBABILITY OF SELECTING INVESTMENT PROJECTS THAT BEST ADDRESS IDENTIFIED NEEDS AND ALSO EU PRIORITIES**

Veneto sets out its selection criteria to choose projects from the eligible applications through a scoring system that takes into account the priorities defined in the regional RDP and defines lists of 'priority investment' types per sector.

These priorities were: environmental benefits; enhancing the value of products; enterprise integration; structural modernisation; access to information and communication technology; reconversion and restructuring of particular agricultural sectors and projects located in mountain areas.

As an example, a project to construct a warehouse and cold storage for apples was selected as it corresponded to the priorities of organic production (which enhances the value); it used photovoltaic panels to reduce energy consumption (environmental benefits) and it was located in a mountain area.

### ... BUT IN PRACTICE LITTLE PRIORITISATION TAKES PLACE

29. In Germany (Baden-Württemberg), Spain (Catalonia), France, Hungary and Portugal (mainland), national procedures established selection criteria against which all projects were assessed. However, regardless of the result of this assessment, all eligible project applications were awarded a grant as the budget for the measure was sufficient.
30. For example, in France, the authorities considered a project for 76 000 euro to construct stables for horses as eligible but it received a score of zero points in the assessment as it did not address any of the priorities established for the measure. Nevertheless, as there was more budget available than total demand from the eligible project applications received at that time, the project was awarded a grant.
31. In Belgium, Luxembourg and Poland, no selection criteria had been established: this was despite the Commission advising Member States that it is a legal obligation to define such selection criteria.

#### BOX 3

### THE POLISH RDP, AN EXAMPLE OF A LACK OF TARGETING

An independent *ex ante* evaluation of the Polish RDP showed that the targeting system was weak and recommended the preparation and implementation of selection criteria. However, the RDP does not set out any selection criteria or other means addressing specific needs or objectives. As the criteria adopted only excluded farms below a certain size, almost all holdings in all agricultural sectors were eligible to apply. This led to a level of demand far exceeding the number of projects that it was possible to finance.

As a result, during the first call for project proposals in 2007, the Polish managing authority applied the 'first-come, first-served' principle. Eligible applications were received in order of their submission until the budget ceiling for the region concerned was reached. This led in some regional offices to queues of applicants waiting in front of the administrative office. During the second call for projects in 2009, the selection of projects was carried out on a random basis. All admissible applications meeting the basic eligibility criteria were selected in random order until the available budget for the region was exhausted. With these selection methods there is no mechanism to target the funding to projects that address identified structural or territorial needs.

From October 2010 onwards the Polish authorities introduced selection criteria for investment projects.

**OVERVIEW OF THE DIFFERENT METHODS OF TARGETING USED BY THE MEMBER STATES (REGIONS) AUDITED**

- 32.** An overview of the different methods of targeting implemented across the 10 Member States is given in **Table 1**, together with the Court's analysis of the degree of targeting achieved through RDP provisions, the national legislation and implementing procedures.

**TABLE 1**

**THE DIFFERENT METHODS AND DEGREES OF TARGETING IN THE 10 MEMBER STATES (REGIONS) AUDITED**

Member State	Restrictive eligibility criteria linked to priorities developed and/or incentives given	Selection criteria defined to target aid	Selection criteria effectively applied	Overall assessment of targeting
Belgium (Wallonia)	√	X	X	weak
Germany (Baden-Württemberg)	√	√	X	limited
Spain (Catalonia)	√	√	X	limited
France (mainland)	√	√	X	limited
Italy (Veneto)	√	√	√	strong
Luxembourg	limited	X	X	weak
Hungary	√	√	X	limited
Poland	X	X	X	weak
Portugal (mainland)	√	√	X	limited
Romania	√	√	√	strong

### THE COMMISSION APPROVED SOME RDPs THAT DID NOT TARGET THE AID TO IDENTIFIED NEEDS AND PRIORITIES

- 33.** The lack of effective targeting observed in paragraphs 29 to 32 above should not arise as the RDPs established by Member States are submitted to the Commission for approval and the legislation requires that they contain sufficient evidence that the investment measures are targeted on clearly defined objectives reflecting identified structural and territorial needs and structural disadvantages<sup>13</sup>. The current legislation does not oblige Member States to disclose in the RDP the selection criteria to be used. These may be adopted by the Member State after the Commission has approved the RDP. However, including in the RDP the key elements the Member State intends to use for the selection of investment projects is essential for the purpose of identifying if and to what extent the required targeting will be achieved.
- 34.** Two of the 10 RDPs examined contained clear evidence of good targeting of measure 121 (Italy (Veneto) and Hungary). Six other RDPs contained little evidence of such targeting (Belgium (Wallonia), Germany (Baden-Württemberg), Spain (Catalonia), France, Romania<sup>14</sup> and Portugal). Two RDPs (Luxembourg and Poland) did not contain sufficient evidence that measure 121 was targeted. All 10 of the RDPs were, however, approved by the Commission.
- 35.** The Commission's services questioned the lack of targeting of measure 121 during their assessment of the proposed Polish RDP in July 2007. In this context, the Commission raised the issue of the proposed 'first-come, first-served' approach. The Polish RDP was not subsequently modified yet the Commission approved it in September 2007 despite the insufficient targeting.
- 36.** Luxembourg's RDP sets out eligibility criteria and differentiated aid rates but it fails to specify the way in which the aid will be targeted to the objectives it has defined to address its particular needs. The Commission has reminded the Luxembourg authorities several times of their obligation to set selection criteria.

<sup>13</sup> Article 43 of Regulation (EC) No 1974/2006.

<sup>14</sup> Although the Romanian RDP contained little evidence of good targeting at the time of its approval by the Commission, investments under measure 121 were strongly targeted in practice due to the implementation of restrictive eligibility criteria and the effective application of relevant selection criteria (see **Table 1**).

- 37.** The cases of Luxembourg and Poland underline the need for the Commission to ensure a sufficient level of targeting evidenced within the RDP submitted for its approval. Once an RDP is approved by the Commission and EAFRD funds are made available to the Member State, it is more difficult for the Commission to retroactively ensure targeting.

**THE DESCRIPTION OF TARGETING ELEMENTS INCLUDED  
IN THE RDP DOES NOT ALWAYS CORRESPOND TO THE  
TARGETING APPLIED IN PRACTICE**

- 38.** The Court found that the selection process implemented and the targeting achieved in practice sometimes differed significantly from the description in the RDP, the chief document on which the Commission bases its decision to approve the overall spending programme. Some Member States described detailed selection systems in their RDP but in practice financed all eligible projects rendering their selection procedures meaningless (France, Hungary). Conversely, other Member States, notably Portugal, developed more detailed targeting systems than were described in the RDP approved by the Commission.

**THE CMEF DOES NOT ALLOW THE EXTENT TO WHICH THE MEASURE  
ADDRESSES ALL THE EU PRIORITIES TO BE MONITORED**

- 39.** The CMEF provides information on progress in programme implementation with respect to indicators of financial inputs, outputs and results. It should, therefore, help identify the results of the targeting of the measure.

40. The CMEF indicators defined for measure 121 (see **Table 2**) are not relevant for monitoring the extent to which certain EU priorities, or the specific actions of the measure, such as quality, on/off-farm diversification and improving the environmental, occupational safety, hygiene and animal welfare status of agricultural holdings, are addressed by the projects financed as no such data is collected.

#### CMEF DATA ON RESULTS ARE OF LOW RELIABILITY

41. The 'New products and/or techniques' result indicator is important for an investment measure the main objective of which is the modernisation of holdings. The audit revealed that it was difficult for Member States to collect data that corresponds to the CMEF definition of this specific indicator<sup>15</sup>. Some Member States decided not to report on it at all (France) or to measure it only partially (Belgium (Wallonia), which refers only to 'new products'). Further, the mid-term evaluation reports identified, for five of the 10 Member States audited, the difficulty of defining 'new techniques' (Belgium (Wallonia), Germany (Baden-Württemberg), France, Luxembourg, Romania). Other Member States applied a definition the scope of which is broader than that of the definition proposed by the CMEF. In Romania, the definition includes any product or technique that is new to the holding. The definition thus includes almost all investment projects supported through the measure (98 % of finalised investments<sup>16</sup>).

<sup>15</sup> CMEF handbook: 'Changes in land use or in agricultural practices that lead to a change in the composition of the basic agricultural products.' (*The Handbook on Common Monitoring and Evaluation Framework, Guidance document*, Directorate-General for Agriculture and Rural Development, September 2006.)

<sup>16</sup> Romania, Annual Progress Report 2009.

TABLE 2

#### CMEF INDICATORS FOR MEASURE 121

Type of indicator	Indicator
Baseline	Labour productivity in agriculture
	Gross fixed capital formation in agriculture
Input	Amount of public expenditure realised (total versus EAFRD)
Output <sup>1</sup>	Number of farm holdings that received investment support (division according to sex, legal status, age category, type of investments — FADN <sup>2</sup> — and type of agricultural branch)
	Total volume of investment (division according to the type of investment — FADN — and type of agricultural branch)
Result	Number of holdings introducing new products and/or techniques (division according to type of redeployment of production)
	Increase in gross value added in supported holdings
Impact	Economic growth
	Labour productivity

<sup>1</sup> According to the CMEF, the number of applications approved will also be provided.

<sup>2</sup> Farm Accountancy Data Network.

- 42.** According to a guidance document issued by the Commission, the 'Increase in gross value added (GVA)' result indicator is intended to measure the improvement of economic performance at the level of holdings supported<sup>17</sup>. Two of the seven Member States visited did not report on the increase in GVA in the period 2007–10 due to difficulties in collecting the necessary data (Luxembourg and France). For the other Member States visited the audit found widely varying definitions and methods for collecting the data. The mid-term evaluation report for Spain (Catalonia) pointed out that the reliability of the 'increase in GVA' indicator is very low, as the necessary accounting information was available only for a very limited sample of beneficiary holdings.
- 43.** A consequence of the low reliability and lack of common definitions is that the data that is collected is not comparable between Member States and cannot meaningfully be aggregated at EU level.

## TARGETING ADDITIONAL FUNDS THROUGH THE 'HEALTH CHECK'

### THE 'HEALTH CHECK' AIMED AT TARGETING ADDITIONAL FUNDS TO 'NEW CHALLENGES'

- 44.** With its 2007 'Health Check' proposal<sup>18</sup>, the Commission identified several 'new challenges' for European agriculture, in the areas of climate change, renewable energy, water management and biodiversity. The Council added the restructuring of the dairy sector as a further challenge. The Council made an additional 4,95 billion euro available<sup>19</sup> through the 'Health Check' and the EERP and underlined the importance of targeting these funds by 'further strengthening'<sup>20</sup> operations related to the EU's new challenges in the Member States' RDPs. Member States which intended to address the new challenges within their RDPs and thus activate the supplementary funding available through the 'Health Check' and EERP from January 2010 onwards had to submit revised RDPs to the Commission for its approval by June 2009. Following this, an estimated additional 630 million euro was programmed for measure 121.
- 45.** The Court's services reviewed the use of measure 121 to address the new challenges by assessing the revised 'Health Check' RDPs approved by the Commission and the national implementation procedures in the 10 Member States reviewed for this audit.

<sup>17</sup> 'Working paper on the CMEF gross value added indicators', European Commission, March 2010.

<sup>18</sup> COM(2007) 722 final of 20 November 2007.

<sup>19</sup> Council Regulation (EC) No 74/2009 of 19 January 2009 amending Regulation (EC) No 1698/2005 on support for rural development by the EAFRD (OJ L 30, 31.1.2009, p. 100).

<sup>20</sup> Recital 6 of Regulation (EC) No 74/2009 states: 'It is important that operations related to these Community priorities are further strengthened in the rural development programmes approved in accordance with Regulation (EC) No 1698/2005.'



**SOME MEMBER STATES DID NOT USE THE ADDITIONAL FUNDING TO 'FURTHER STRENGTHEN' MEASURE 121**

- 46.** Member States may make use of the additional funding to increase aid rates for relevant projects, for example, or by introducing specific sub-measures to address the new challenges. They may also revise their procedures and criteria in order to favour, during the selection process, investments addressing the new challenges.
- 47.** For seven of the 10 Member States covered by the audit<sup>21</sup>, the adoption of the 'Health Check' and the EERP increased the budget allocated to measure 121. In all of these cases, the RDPs had already addressed objectives linked to the new priorities before the 'Health Check'.
- 48.** The seven Member States that increased the budget for measure 121 responded to the new priorities in different ways. Three Member States (Italy (Veneto), Romania and Portugal) revised their selection procedures in order to give greater preference to investment projects under measure 121 addressing the new priorities:
- In Italy, the aid rates and the maximum amount of grant were increased for projects in the dairy sector. The 'new challenge' priorities were added to the priority selection criteria, increasing the likelihood of selecting projects that addressed the new challenges.
  - Romania changed its procedures by attributing additional points for project proposals that invested in renewable energy.
  - The Portuguese authorities opened a specific call for project proposals for the dairy sector in which the aid rates were 10 % higher than the rates for non-priority sectors.
- 49.** Three Member States (Germany (Baden-Württemberg), France and Luxembourg) did not change their procedures. Poland was revising its procedures at the time of the audit.

<sup>21</sup> Three Member States covered by the audit did not allocate additional resources to measure 121 following the 'Health Check' (these are Belgium (Wallonia), Spain (Catalonia) and Hungary).

- 50.** Beyond this, the observations presented in paragraphs 29 to 32 above show that many of the Member States did not implement eligibility rules, selection procedures or criteria that would allow them to target the additional resources to the priorities of climate change, renewable energy, water management and biodiversity.
- 51.** Member States are obliged to ensure that ‘an amount equal’ to the supplementary funding resulting from the ‘Health Check’ and the EERP is spent on operations addressing the new challenges<sup>22</sup>. Member States have to ensure that a separate financial reporting for operations addressing the new challenges allows the Commission to verify that this condition has been respected. Member States are also required to monitor, under the CMEF, to what extent the new challenges were being addressed by operations financed by the EAFRD, from 2010 onwards. However, prior to the ‘Health Check’, operations already addressing the new challenges were not specifically reported upon, under either the financial reporting to the Commission or the CMEF. This makes a comparison between the situation before and after the ‘Health Check’ almost impossible.
- 52.** The Court’s audit identified the risk that Member States, which had planned to finance operations that addressed the new challenges prior to the ‘Health Check’, might use the extra funding for purposes other than further strengthening of the new priorities. This may happen where Member States had planned to address similar priorities such as the dairy sector prior to the new funding being made available. The previously planned spending is then considered as fulfilling the requirements of the ‘Health Check’ and the ‘extra’ ‘Health Check’ monies are used for other purposes.

<sup>22</sup> Article 69(5a) of Regulation (EC) No 1698/2005, introduced by Regulation (EC) No 74/2009.

- 53.** This risk materialised, as in one case examined such a substitution was explicitly described in a 'Health Check' RDP submitted to and approved by the Commission (see **Box 4**).
- 54.** The Commission considers the type of budgetary substitution illustrated in **Box 4** to be in conformity with the provisions of the regulation, as 59,8 million euro will be shown to cover operations addressing new priorities. But, as exactly the same amount will be spent on new priorities as was planned prior to the 'Health Check', it does not result in any 'further strengthening'.
- 55.** The Court therefore highlights the fact that not all the monies made available under the 'Health Check'/EERP will be used to further strengthen the identified priorities and that the actual amount that does indeed strengthen those priorities will be impossible to identify, as compared to the situation prior to the 'Health Check'.

**BOX 4**

**GERMANY (BADEN WÜRTTEMBERG): EXTRA 'HEALTH CHECK' FUNDING REPLACES BUDGETED EXPENDITURE ALREADY ADDRESSING THE NEW CHALLENGES**

Within the revised 'Health Check' RDP submitted to the Commission, following the 'Health Check'/EERP, an additional amount of 59,8 million euro was allocated to the RDP budget for Baden-Württemberg in order to address three new challenges: restructuring the dairy sector, climate change and biodiversity. The funds were exclusively channelled to the existing measures 121 and 214 (agri-environment measure). The restructuring of the dairy sector was to be addressed by measure 121.

The Baden-Württemberg authorities asserted that within the existing measures 121 and 214, as defined in the initial RDP adopted in November 2007, an amount greater than 59,8 million euro had already been committed for operations addressing the new challenges prior to the 'Health Check'. The Baden-Württemberg authorities consequently subtracted an amount of 59,8 million euro from the existing budgets for measures 121 and 214, and reallocated this amount to several existing measures, of which some 18 million euro to measure 121 in order to address specific regional needs.

Within the budget of measure 121, the authorities ring-fenced 26 million euro for the new challenge of restructuring the dairy sector. Pre 'Health Check' expenditure data however indicates that the likely amount of the original budget to be spent on the dairy sector was already some 35 million euro.

## TARGETING THE AID TO AVOID RISKS TO SUSTAINABILITY AND DEADWEIGHT

### INSUFFICIENT VERIFICATION OF THE ECONOMIC VIABILITY OF HOLDINGS AND INVESTMENT PROJECTS SUBMITTED

- 56.** Member States should ensure that the economic viability of the proposed investments on the agricultural holdings can be demonstrated before awarding the grant to avoid giving aid to holdings that are likely to fail and to ensure the sustainability of the investment aided. Despite there being no legal obligation to do so, all Member States (regions) audited required applicants to submit some level of proof of the economic viability of their holding and/or of the project proposal<sup>23</sup>. Nevertheless, the audit found that the level and the extensiveness of such proof varies significantly between Member States.
- 57.** In Luxembourg, an attestation is required for investments above a certain threshold, certifying that the farmer has received economic counselling regarding his investment project — this attestation contains a summary of the holding's gross profit and the project's costs, but not the result of the economic analysis.
- 58.** In Hungary, the quality and soundness of the financial plan to be submitted with the project application are evaluated through a project scoring system based on a computerised comparison with reference data. More than a quarter of the projects selected in a 2008 call for proposals scored zero in one or more criteria in the assessment of the 'realism of the financial plan'. The Court identified that there was no minimum score set for the evaluation of the financial plan and that all projects were accepted regardless of the score obtained.
- 59.** In Poland, the financial soundness of a project has to be demonstrated by the applicant only in cases where the project's objective is specifically aimed at increasing the gross added value of the holding. It is, however, up to the farmer to tick, in his application, if this is the aim of his project, which would automatically initiate a further analysis of his claim by the administration. None of the 10 projects reviewed by the Court had indicated this as an objective, and so no viability check was performed for them.

<sup>23</sup> The regulations require only that the proposed investment improves the overall performance of the holding.

**MEMBER STATES SELECTED PROJECTS THAT HAD ALREADY STARTED, THEREBY ENTAILING THE RISK OF DEADWEIGHT**

- 60.** The Court has identified in previous reports (e.g. on the Leader approach)<sup>24</sup> that a risk to the efficiency of any grant-based programme is that the investment would have been carried out anyway without the public aid. Such investments constitute ‘deadweight’.
- 61.** A strong indication of a possible deadweight effect is where projects had already started or even been completed before the aid was granted. If aid is granted retroactively, the farmer demonstrated, by his initial investment decision, that he was willing to carry out the investment even in the absence of an agreement for public support.
- 62.** For measure 121, there are different approaches regarding the approval of a project for which work has started:
- In Luxembourg, agricultural holdings may apply for investment aid after they have already carried out the investment if the amount is under 100 000 euro, or the project started between the beginning of the programming period and the date of publication of the national implementing law.
  - In other Member States, including Spain (Catalonia), Italy (Veneto) and Portugal, holdings may start the potentially eligible investment on the date they submit their application for aid, without having the certainty that the project will be approved for financing.
  - In Belgium (Wallonia) and Romania, investment project costs are eligible only from the date that the grant was approved, which represents good practice<sup>25</sup>.
- 63.** The audit found that for four of the Member States/regions audited (Spain (Catalonia), Italy (Veneto), Luxembourg and Portugal (mainland)), half of the projects in the sample had started (or had even been completed) before the grant was awarded. In these cases, the deadweight risk, i.e. that the farmer would have carried out the investment even in the absence of public support, is significant.

<sup>24</sup> Special Report No 5/2010 on implementation of the Leader approach for rural development (<http://eca.europa.eu>).

<sup>25</sup> Similar rules applied in Germany, France, Hungary and Poland, although exceptions were allowed.

- 64.** Legislative proposals from the Commission to amend the current rural development regulation<sup>26</sup> specify that expenditure will be eligible only after a grant application has been submitted. This will prevent retrospective approval of the sort permitted in Luxembourg, but does not sufficiently address the risk of deadweight as the investment project could still start before the approval of the application (and even before the application has been submitted, with the provision that costs incurred up to the application date will not be eligible for support).
- 65.** The Commission proposal for the 2014–20 rural development period reiterates this requirement. However, it also foresees good practice in this respect, with the explicit provision that Member States may provide that expenditure is eligible only from the date of grant approval (see **Box 5**).

<sup>26</sup> COM(2010) 537 final of 30 September 2010 — Commission's proposal for a regulation amending Regulation (EC) No 1698/2005; legislative codecision procedure COD/2010/0266.

## BOX 5

### COMMISSION PROPOSAL FOR THE 2014–20<sup>27</sup> RURAL DEVELOPMENT PERIOD

With the exception of general costs [*preparatory costs*]..., in respect of investment operations..., only expenditure which has been incurred after an application has been submitted to the competent authority shall be considered eligible.

Member States may provide in their programmes that only expenditure which has been incurred after the application for support has been approved by the competent authority shall be eligible.

<sup>27</sup> COM(2011) 627 final/2 — Commission's proposal for a regulation of the European Parliament and of the Council on support for rural development by the European Agricultural Fund for Rural Development (EAFRD); presented by the Commission in the legislative framework for the CAP in the period 2014–20.

## CONCLUSIONS AND RECOMMENDATIONS

- 66.** The Court's audit found that rural development investment measure 121, 'Modernisation of agricultural holdings', achieved its nominal objective in that it resulted in the modernisation of holdings. However it concludes that this was almost inevitable given the fact that almost any investment or purchase of new equipment can be considered to modernise to some extent and fulfil the very broad criteria of eligibility (paragraphs 23 to 24).
- 67.** Though Member States are required to target investment aid on clearly identified needs in their rural areas, the extent of targeting varies significantly between the Member States reviewed. Some target the aid very strongly on specific needs and have established selection procedures to choose the best-suited projects from those eligible applicants (paragraphs 25 to 28).
- 68.** Other Member States have awarded grants to all the project proposals received that meet basic eligibility conditions, regardless of the projects' contribution to achieving the objectives set for the measure. Such practices lead to a less effective and efficient use of the public funds, both EU and national. The 11,1 billion euro allocated to this measure by the EAFRD has the potential to provide greater value for money if it were better targeted to EU priorities and identified national and regional needs (paragraphs 29 to 32).
- 69.** The Commission approved rural development programmes (RDP) that did not adequately target the aid and, in particular, that did not specify the process or criteria to be applied for selecting projects (paragraphs 33 to 38).

### RECOMMENDATION 1

- (a) The Commission should propose legislation with clear requirements for Member States to give details in their RDPs of how the measure will be targeted to the identified needs, and overall priorities, including details of the project selection process and criteria to be implemented, and should ensure that these requirements are met when approving the RDPs.
- (b) When implementing their RDPs for the forthcoming programming period, Member States should target the aid through clear and relevant selection criteria, addressing the EU priorities and national or regional needs.

- 70.** The CMEF has been set up as a tool for the Member States and the Commission. The Court found that it does not generate relevant data which can be used for monitoring the results obtained with the funds spent on measure 121. The indicators defined do not allow progress in the achievement of the EU's priorities to be monitored, and the data were found to be of low reliability and do not allow comparisons between Member States (and/or regions) to be drawn (paragraphs 39 to 43).

#### RECOMMENDATION 2

The Commission should ensure that for the forthcoming programming period, relevant and reliable information is obtained to facilitate management and monitoring of the measure and to demonstrate the extent to which the aid given is contributing to the achievement of EU priorities.

- 71.** The 2009 'Health Check' provided some 5 billion euro of extra funding to further strengthen specific EU priorities that were defined as being the EU's new challenges including climate change and biodiversity. The absence of effective targeting mechanisms weakens the potential effectiveness of the additional funds in meeting these challenges. Moreover, the Court's audit revealed instances where a 'further strengthening' will not be achieved due to the substitution of the extra 'Health Check'/EERP funding with funds already programmed for the measures concerned prior to the 'Health Check' (paragraphs 44 to 55).

#### RECOMMENDATION 3

Where it is the intention to earmark particular measures and budgetary allocations to target specific priorities, as was the case with the 'Health Check', to ensure that the funding has an additional effect the Commission should propose legislation to make this requirement specific in the underlying EU regulations.



- 72.** All Member States (regions) audited require applicants to submit some level of proof of the economic viability of their holding and/or of the project proposal. However, some Member States did not take the evidence obtained into account when evaluating the project application (paragraphs 56 to 59).

#### RECOMMENDATION 4

Member States should put effective procedures in place, proportionate to the risk, to ensure that grants are not given to projects where the financial viability of the investment or the sustainability of the holding is in doubt.

- 73.** The Court found that the deadweight risk linked to the retroactive approval of investments which had already started persists (paragraphs 60 to 65).

#### RECOMMENDATION 5

The Commission should encourage Member States to follow good practice whereby expenditure for investments would be eligible only from the date of grant approval.

This Report was adopted by Chamber I, headed by Mr Ioannis SARMAS, Member of the Court of Auditors, in Luxembourg at its meeting of 14 March 2012.

*For the Court of Auditors*



Vítor Manuel da SILVA CALDEIRA  
*President*

**SELECTED RURAL DEVELOPMENT PROGRAMMES (RDP) AND CORRESPONDING MEMBER STATES OR THEIR REGIONS COVERED BY THE AUDIT, TOGETHER WITH THE RESPECTIVE BUDGET FOR MEASURE 121, FOR 2007–13**

RDP	EU's contribution (via EAFRD) 2007–13 (euro)	Total public M121 budget 2007–13 <sup>1</sup> (euro)
Belgium (Wallonia)	28 800 000	96 000 000
Germany (Baden-Württemberg)	84 196 000	168 393 000
Spain (Catalonia)	27 628 000	119 082 000
France (mainland)	687 062 000	1 374 125 000
Italy (Veneto)	87 816 000	190 381 000
Luxembourg	24 574 000	122 871 000
Hungary	1 175 175 000	1 652 571 000
Poland	1 449 672 000	1 919 068 000
Portugal (mainland)	259 874 000	344 923 000
Romania	816 404 000	1 020 506 000

<sup>1</sup> Including national or regional public co-financing.

# REPLY OF THE COMMISSION

## EXECUTIVE SUMMARY

### V. (a)

According to Regulation (EC) No 1698/2005, the purpose of the measure is to modernise agricultural holdings by improving their economic performance through better use of production factors as well as improving the environmental, occupational safety, hygiene and animal welfare status of agricultural holdings.

The Commission considers that when an investment improves the economic performance of the holding or improves the environmental, occupational safety, hygiene or animal welfare status, it fulfils the objective of the measure.

### V. (c)

Regulation (EC) No 1698/2005 stipulates that, in accordance with the principles of subsidiarity and shared management, selection criteria may be defined after programme approval in consultation with the Monitoring Committee and they are not subject to rural development programme (RDP) approval by the Commission.

Selection criteria are not the only way to target the measure to objectives reflecting the structural and territorial needs and structural disadvantages as identified in the SWOT<sup>1</sup> analysis of the RDP. Targeting can also take the form of detailed eligibility rules, regional and sectoral differentiation, differentiation of aid intensities as well as aid ceilings by which Member State can make a preselection among potential beneficiaries.

### V. (d)

The Commission considers that the Common Monitoring and Evaluation Framework (CMEF) is a valid instrument to monitor and evaluate progress towards achieving the EU's rural development policy objectives and turned out to have many strengths, although some difficulties were encountered.

The Commission, Member States and various stakeholders devote much effort to continuously improving the system. This experience is being used for the development of an improved monitoring and evaluation system for the next programming period.

<sup>1</sup> Strengths, weaknesses, opportunities and threats.

## REPLY OF THE COMMISSION

### V. (e)

The legislator formulated Article 69(5a) of Regulation (EC) No 1698/2005 so that an amount equal to the additional 'Health Check' and EERP<sup>2</sup> resources shall be exclusively spent in the period from 1 January 2010 to 31 December 2015 for operations of the types referred to in Article 16a of the regulation ('new challenges').

At the same time, additionality was not required in the aforementioned article. Where the amounts in relation to new challenges were deemed already appropriate by the Member States, they were given the possibility to transfer funds programmed before the 'Health Check'/EERP period for the period 2010–15 to other measures or operations.

### V. (f)

A comprehensive assessment of the viability was deemed to be disproportionate for many types of investment projects and to create an unnecessary administrative burden and costs.

For the next programming period, the Commission has proposed to require a business plan for some measures that provide support for new economic activities (business start-up aid, including young farmers, non-agricultural activities in rural areas and development of small farms and support to producer groups) in order to ensure viability.

### V. (g)

According to the Commission's proposals of September 2010 for the amendment of Regulation (EC) No 1698/2005 and according to the proposal for the next programming period, in respect of investment operations under measures falling within the scope of Article 42 of the Treaty, the Commission has proposed that only expenditure which has been incurred after an application has been submitted to the competent authority shall be considered eligible.

<sup>2</sup> European Economic Recovery Plan.

### VI. (a)

According to the Commission's proposal for the next programming period<sup>3</sup>, strategic programming will be further reinforced, with the result of an improved strategic targeting through the Union priorities for rural development and their focus areas.

The definition and application of selection criteria will be reinforced to ensure equal treatment of applicants, better use of financial resources and targeting of measures in accordance with the Union priorities for rural development.

The proposal provides for improved targeting to investment support to farm restructuring.

### VI. (b)

The monitoring and evaluation system is subject to review by the Commission and Member States in order to improve its efficiency and effectiveness and foster ownership by sharing good practices and building capacity. According to the Commission proposal for future rural development policy, quantified result indicators will be used to assess progress towards targets established *ex ante* at programme level.

### VI. (c)

The Commission has proposed that Member States should have the possibility in the next programming period to design thematic subprogrammes, aimed to address specific needs, by earmarking particular measures and budgetary allocations and setting specific financial and indicator plans.

### VI. (d)

For the next programming period, the Commission has proposed to require a business plan for certain measures that provide support for new economic activities (business start-up aid, including young farmers, non-agricultural activities in rural areas and development of small farms and support to producer groups) in order to ensure viability.

<sup>3</sup> Proposal for a regulation of the European Parliament and of the Council on support for rural development by the European Agricultural Fund for Rural Development (EAFRD), COM(2011) 627 final/2 of 19 October 2011.

## REPLY OF THE COMMISSION

### VI. (e)

In its proposal of September 2010 for the amendment of Regulation (EC) No 1698/2005 and in respect of investment operations under measures falling within the scope of Article 42 of the Treaty, the Commission has proposed that only expenditure which has been incurred after an application has been submitted to the competent authority shall be considered eligible.

A similar requirement has been introduced in Article 67(2) of the Commission proposal for the next programming period. In this context, Member States may also provide in their programmes that only expenditure which has been incurred after the application for support has been approved by the competent authority shall be eligible.

### OBSERVATIONS

#### 23.

According to Regulation (EC) No 1698/2005, the purpose of the measure is to modernise agricultural holdings by improving their economic performance through better use of production factors as well as improving the environmental, occupational safety, hygiene and animal welfare status of agricultural holdings. The Commission considers that when a project improves the economic performance of the holding or improves the environmental, occupational safety, hygiene or animal welfare status, it fulfils the objective of the measure.

#### 24.

Innovation, quality and diversification, are general EU priorities for the competitiveness objective, which is implemented through axis 1 as a whole. The modernisation of agricultural holdings measure contributes to this objective by improving the competitiveness and environmental sustainability of the agricultural production. Not all investments should improve the farm's performance through all means to achieve the main objective of modernisation — each operation will be specific.

### 26. Second indent

In the Luxembourg rural development programme, measure 121 clearly identifies objectives to be achieved based on the SWOT analysis included in the RDPs<sup>4</sup>. Nevertheless, the Commission has insisted on the need for greater selectivity on the occasion of the annual meetings with the Luxembourg authorities. Despite the fact that the RDP identifies clear objectives/needs/disadvantages, selection criteria and targeting could be further strengthened.

### 29–38. Joint reply

According to the principles of subsidiarity and shared management, project selection lies within the responsibility of Member States.

The Commission considers that while it is necessary for the Member States to establish selection criteria, they are not the only way to target the measure to objectives reflecting the structural and territorial needs and structural disadvantages as identified in the SWOT analysis of the rural development programme. Targeting can also take the form of detailed eligibility rules, regional and sectoral differentiation and differentiation of aid intensities as well as aid ceilings by which the Member State can make a preselection among the potential beneficiaries.

Nonetheless, the Commission has insisted on several occasions on the need for greater selectivity, for example, during annual meetings. Notably, at the beginning of the programming period a letter was sent from the Commission to the Managing Authorities of all programmes inviting them to take into account the importance of well-defined selection criteria for an effective implementation throughout the whole period. Furthermore, in 2009, another letter asked Member States to make sure that adequate selection criteria are specified and used for the allocation of funds.

In cases where the selection criteria were already specified in the programme on a voluntary basis, the Commission has invited the national authorities to consult the Monitoring Committee.

<sup>4</sup> See Chapters 3 and 5 of the Luxembourg RDP.

## REPLY OF THE COMMISSION

### Box 3

In the specific case of Poland, the documents provided to the Court show that the initial preference of the Polish authorities was to rely on eligibility criteria that they regarded as being stringent enough to ensure targeting. Subsequent experience proved otherwise and selection criteria were adopted following consultation of the programme Monitoring Committee in June 2009.

### 32.

See reply to Box 3.

### 34.

While individual RDPs may not all contain all elements of targeting, the possibility exists for Member States to subsequently adopt selection criteria in line with the objectives of the RDPs.

As for the Romanian rural development programme, it explicitly identifies the needs in its measure 121 form. Those needs are also presented in the third chapter of the Romanian RDP. Selection criteria were also included in the RDP, e.g. investments in LFA and fostering semi-subsistence farms.

### 40.

Since the purpose of measure 121 is to contribute to the objective of improving competitiveness, the Commission and Member States have agreed during the preparation of the Common Monitoring and Evaluation Framework that the two result indicators 'Gross value added (GVA)' and 'New products and/or techniques' are relevant and suitable to capture the competitiveness dimension and respond to the measure's intended outcome.

Where needed, Member States could complement common indicators with additional indicators to describe the programme's achievements on the basis of specific measure interventions.

### 41.

Given that what constitutes modernisation or innovation differs widely across Member States, a common definition of what is actually 'new' would be neither meaningful nor desirable. Member States develop their own definition and assess projects accordingly.

In relation to the findings of the mid-term evaluation reports, further exchanges with Member States as regards measurement of this indicator are envisaged.

### 42.

Although GVA is considered a valid indicator to capture economic performance at the level of holdings, experience has showed some difficulties in the collection of data in Member States. Therefore, the Commission has taken steps to address the problem and in a working paper of March 2010 provided guidance on the definition and the methodology to be used for measurement of this indicator.

### 43.

For the next programming period, the monitoring and evaluation system is being reviewed and improved to ensure relevance, usability and comparability at EU level of common indicators.

### 49.

The Commission considers that it was not necessary to change the modalities of support (aid rates, eligibility conditions, etc.) where measure 121 had already addressed these new challenges in the previous versions of the rural development programmes in question.

### 50.

The ring-fenced amount of the 'Health Check'/EERP was entirely programmed for related operations as identified under Annex II of Regulation (EC) No 1698/2005.

## REPLY OF THE COMMISSION

### 51.

Prior to the 'Health Check', reporting on operations already addressing the new challenges was not a legal requirement. This is why no comparison is possible.

However, with the 'Health Check', the amounts ring-fenced for new challenges for the period 2010–15 are clearly tracked. Only projects addressing the new challenges and declared to the Commission after the approval of the revised version of the programmes can qualify for 'Health Check'/European Economic Recovery Plan funding. A separate financial table for 'new challenges' was introduced in the financial plan accompanying the Commission decision approving the programme revision and against which the reimbursements are followed.

### 52.

The legislator formulated Article 69(5a) of Regulation (EC) No 1698/2005 so that an amount equal to the additional 'Health Check' and European Economic Recovery Plan resources shall be exclusively spent in the period from 1 January 2010 to 31 December 2015 for operations of the types referred to in Article 16a of the regulation ('new challenges').

At the same time, as additionality was not required in the aforementioned article, it was decided to take into account the previous programming choices of the Member States where resources had already been allocated to support operations in relation to new challenges. Where the amounts were deemed already appropriate by the Member States, they were given the possibility to transfer funds programmed in the pre-'Health Check'/EERP funds period for the period 2010–15 to other measures or operations.

It is not possible to compare amounts pre- and post-'Health Check'/EERP amendment, as the amounts already allocated for similar operations were not ring-fenced before the programme revision.

### 53–54. and Box 4 — Joint reply

The modification following the implementation of the new priorities of the 'Health Check' and the European Economic Recovery Plan was indeed considered in line with Article 69(5a) of Council Regulation (EC) No 1698/2005, as a considerable amount of the EAFRD funds was already committed to addressing the new priorities within the existing measures 121 and 214 defined in the initial RDP.

The Commission considers that further strengthening has taken place as the post-'Health Check' financial allocation to measure 121 has increased by 29 %

The most important effect of the 'Health Check'/EERP modification is that 26.1 million euro is now earmarked and has to be spent for this specific priority within measure 121 for the years 2010–15, regardless of what has already been spent before 2010.

### 55.

See reply to paragraph 52.

### 57.

The rural development programme indicates that the economic counsellor is responsible for establishing the development plan. This is an eligibility criterion for projects of more than 100 000 euro.

### 58.

In Hungary, eligible projects are ranked according to a scoring system. The quality and soundness of the financial plan is one of the elements of this system. Other elements include, for instance, the establishment of a business plan, which should demonstrate that the project would improve the overall performance of the holding through, for instance, the enhancement of the competitiveness of the farm, impact on biodiversity and positive energetic balance. As the purpose of these elements is to rank eligible projects, a zero point for the financial plan does not, as such, predetermine the viability of the project itself which, in fact, remains eligible.

## REPLY OF THE COMMISSION

### CONCLUSIONS AND RECOMMENDATIONS

#### 62.

In its proposal of September 2010 for the amendment of Regulation (EC) No 1698/2005 and in respect of investment operations under measures falling within the scope of Article 42 of the Treaty, the Commission has proposed that only expenditure which has been incurred after an application has been submitted to the competent authority shall be considered eligible.

#### 63.

See reply to paragraph 62.

#### 64.

The legislative proposal for the next programming period<sup>5</sup> foresees that only expenditure which has been incurred after an application has been submitted to the competent authority shall be considered eligible. This mitigates the risk of deadweight, in the Commission's view.

#### Box 5

The first provision of the Commission proposal for the 2014–20 rural development period<sup>6</sup> has been introduced to align the agricultural measures to general state aid rules.

<sup>5</sup> Proposal for a regulation of the European Parliament and of the Council on support for rural development by the European Agricultural Fund for Rural Development (EAFRD), COM(2011) 627 final/2 of 19 October 2011

<sup>6</sup> COM(2011) 627 final/2 — Commission's proposal for a regulation of the European Parliament and of the Council on support for rural development by the European Agricultural Fund for Rural Development (EAFRD), presented by the Commission in the legislative framework for the CAP in the period 2014–20.

#### 66.

According to Regulation (EC) No 1698/2005, the purpose of the measure is to modernise agricultural holdings by improving their economic performance through better use of production factors as well as improving the environmental, occupational safety, hygiene and animal welfare status of agricultural holdings.

The Commission considers that when an investment improves the economic performance of the holding or improves the environmental, occupational safety, hygiene or animal welfare status, it fulfils the objective of the measure.

#### 67.

Targeting of the aid can be achieved in many ways: through selection criteria, detailed eligibility criteria, sectoral or regional differentiation and differentiation of aid intensities by type of beneficiary or by type of investment or by setting aid ceilings.

#### 69.

In accordance with the principles of subsidiarity and shared management, Article 71(2) of Council Regulation (EC) No 1698/2005 stipulates that selection criteria may be defined after programme approval in consultation with the Monitoring Committee and they are not subject to a Commission decision.

See also joint reply for paragraphs 29 to 38.



## REPLY OF THE COMMISSION

### Recommendation 1

According to the Commission's proposal for the next programming period, strategic programming will be further reinforced, with the result of an improved strategic targeting through the Union priorities for rural development and their focus areas.

Besides carrying out a SWOT analysis, Member States/regions will have to establish *ex ante* quantified targets (close to result-type indicators) for the RDP. The content of the programme shall contain a description of the strategy which includes the target setting for each of the focus areas of the Union priorities for rural development included in the programme. Specific needs, linked with specific conditions at regional or subregional level, have to be demonstrated. The programme shall also demonstrate, *inter alia*, that the allocation of financial resources is balanced and adequate and that an appropriate approach has been defined laying down principles with regard to the setting of selection criteria for projects, which takes into account relevant targets.

The definition and application of selection criteria shall aim to ensure equal treatment of applicants, better use of financial resources and targeting of measures in accordance with the Union priorities for rural development.

Moreover, in order to further improve targeting, Member States shall ensure that the *ex ante* evaluator is engaged from an early stage in the process of development of the rural development programme, including the development of the SWOT analysis, the design of the programme's intervention logic and the establishment of the programme's targets.

### 70.

The Commission considers that the Common Monitoring and Evaluation Framework constitutes a relevant and integrated set of indicators that was jointly prepared by the Commission and Member States to capture the policy's objectives. It marks the first time that a comprehensive, yet very demanding, monitoring and evaluation system for rural development has been implemented at EU level. It is the combination of all the measures which should be considered when assessing whether the EU's priorities are well addressed.

Measure 121 should be assessed against the objective of improving competitiveness. The current 'learning by doing' experience shows that the definition of result indicators in this field is challenging and the Commission, Member States and various stakeholders have devoted much effort to continuously improve methodology, reliability and comparability. This experience will also be used for the future monitoring and evaluation system.

### Recommendation 2

The monitoring and evaluation system is subject to review by the Commission and Member States in order to improve its efficiency and effectiveness, especially in terms of reliability and comparability, and foster ownership by sharing good practices and building capacity. According to the Commission proposal for the future rural development policy, quantified result indicators will be used to assess progress towards targets established *ex ante* at programme level.

Furthermore, managing authorities will have to ensure that there is an appropriate secure electronic system to record, maintain, manage and report statistical information on programme implementation, particularly as progress towards the defined objectives and priorities.

### 71.

The legislator formulated Article 69(5a) of Regulation (EC) No 1698/2005 so that an amount equal to the additional 'Health Check' and European Economic Recovery Plan resources shall be exclusively spent in the period from 1 January 2010 to 31 December 2015 for operations of the types referred to in Article 16a of the regulation ('new challenges').

Additionality was not required in the aforementioned article, hence it was decided to take into account the previous programming choices of Member States where resources had already been allocated to support operations in relation to new challenges. In these cases, in order to avoid problems of imbalances and/or inconsistencies across the whole programme, as well as to prevent overfunding to exhaust the measure's limited absorption capacity, Member States were given the possibility to transfer funds programmed in the pre-'Health Check'/EERP period to other measures or operations.

## REPLY OF THE COMMISSION

### **Recommendation 3**

The Commission has proposed that Member States should have the possibility in the next programming period to design thematic subprogrammes within their rural development programmes, contributing to the Union priorities for rural development, aimed to address specific needs identified by earmarking particular measures and budgetary allocations and setting specific financial and indicator plans.

### **Recommendation 4**

A comprehensive assessment of the viability was deemed to be disproportionate for many types of investment projects and to create an unnecessary administrative burden and costs.

For the next programming period, the Commission has proposed to require a business plan for some measures that provide support for new economic activities (business start-up aid, including young farmers, non-agricultural activities in rural areas and development of small farms and support to producer groups) in order to ensure viability.

### **73.**

See reply to Recommendation 5.

### **Recommendation 5**

According to the Commission's proposals of September 2010 for the amendment of Regulation (EC) No 1698/2005 and according to the proposal for the next programming period, in respect of investment operations under measures falling within the scope of Article 42 of the Treaty, the Commission has proposed that only expenditure which has been incurred after an application has been submitted to the competent authority shall be considered eligible.

The Commission has also proposed for the next programming period that the Member States may provide in their programmes that only expenditure which has been incurred after the application for support has been approved by the competent authority shall be eligible.





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THE EUROPEAN UNION CO-FINANCES INVESTMENTS THAT AIM AT MODERNISING FARMS. SUBSIDISED INVESTMENTS RANGE FROM SIMPLE FARM MACHINERY TO COMPLEX BUILDING PROJECTS.

IN THIS REPORT, THE COURT IDENTIFIES THE IMPORTANCE OF TARGETING AID TO PROJECTS THAT ADDRESS CLEARLY IDENTIFIED STRUCTURAL NEEDS IN THE MEMBER STATES AND THE PRIORITIES SET OUT AT THE EU LEVEL.

EFFECTIVE TARGETING SHOULD DIRECT THE FUNDING TO VIABLE PROJECTS THAT HAVE A GREATER CHANCE OF ACHIEVING THE OBJECTIVES SET, THEREBY PROVIDING BETTER VALUE FOR MONEY FOR THE EUROPEAN AND NATIONAL TAXPAYERS.

THE COURT FOUND THAT THE TARGETING OF THE FUNDING VARIES SIGNIFICANTLY; WHILST SOME MEMBER STATES HAVE DEVELOPED SYSTEMS FOR SELECTING THE BEST PROJECTS, OTHERS FAIL TO TARGET THE AID EFFECTIVELY.

THE COURT ALSO UNDERLINES THE IMPORTANT ROLE OF THE COMMISSION IN ENSURING THAT MEMBER STATES HAVE PROVIDED FOR THE TARGETING OF THE AID WHEN IT APPROVES THE MEMBER STATES' RURAL DEVELOPMENT PROGRAMMES.



EUROPEAN COURT OF AUDITORS



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