

I

(Information)

COURT OF AUDITORS

SPECIAL REPORT No 4/2003

concerning rural development: support for less-favoured areas, together with the Commission's replies*(pursuant to Article 248(4), second subparagraph of the EC Treaty)**(2003/C 151/01)*

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GLOSSARY

EAGGF	European Agricultural Guidance and Guarantee Fund (Guarantee Section)
LFA	less-favoured area
RDP	rural development plan
UAA	usable agricultural area
ABU	adult bovine unit

SUMMARY

I. The support scheme for less-favoured areas (LFAs) grants aid to 55,8 % of the EU's agricultural holdings. The annual cost is some 2 000 million euro of which roughly 50 % is financed from EU Funds. The area classified as less favoured increased steadily from 36 % in 1975 to 56 % in the year 2000, due partially to the successive enlargements of the EU in this period, with a number of countries having a much higher proportion of less-favoured areas, reflecting their natural conditions.

II. The objectives of the audit were to establish whether the support scheme for less-favoured areas is managed by the Commission in a way that legal and regular implementation is ensured, whether it is appropriately monitored, whether relevant knowledge on its impact is available and whether timely action is undertaken to correct deficiencies. The audit examined key areas of the support scheme, focusing on the definition and respect of eligibility criteria, in particular good agricultural practices and the classification of LFAs.

III. The main findings of the audit are that:

- (a) the Commission has insufficient evidence that the classification of the LFAs is valid. Following observations from the Court in 1990 the Commission commenced a review of existing classifications, but this review was not finalised due, in part, to opposition from Member States. Subsequently, although certain macroeconomic and socioeconomic indicators have developed noticeably and certain classifications may no longer be valid, the Commission has not proposed that the existing regulatory framework should be amended (see paragraphs 22 to 29);
- (b) Member States use a wide range of indicators to determine whether areas are less favoured or not; this may lead to differences in the treatment of beneficiaries (see paragraphs 30 to 37);
- (c) the Commission does not have enough sound information on the impact of the measure and, in particular, on whether the level of compensation is justified; in the absence of such knowledge, overcompensation may occur (see paragraphs 38 to 42);
- (d) the notion of 'good agricultural practice' is now an important eligibility criterion. However, without clear and verifiable definitions and consistent application, compliance with this criterion is difficult to verify and the checks carried out in this context are not as effective as they should be (see paragraphs 43 to 57);
- (e) monitoring of the LFA scheme is poor due to a lack of relevant data; information from Member States is late or incomplete (see paragraphs 58 to 63);
- (f) beneficiaries believe that aid for LFAs has enabled them to continue farming in an area which they might otherwise have had to leave but, in the absence of an overall evaluation, no definite conclusion can be drawn; an assessment of the outcomes is near impossible because the Commission, contrary to the provisions of the Financial Regulation, has not set quantified objectives specific to this measure in favour of less-favoured areas; although there have been recent improvements in setting the framework for evaluating the measure, an overall evaluation of its impact is, after 30 years of operation, still lacking (see paragraphs 38 and 64 to 74).

IV. The report concludes that various aspects of the support scheme should be reviewed in order for it to be a more effective, efficient and economic contribution to rural development (see paragraphs 75 to 83).

GENERAL BACKGROUND

Introduction

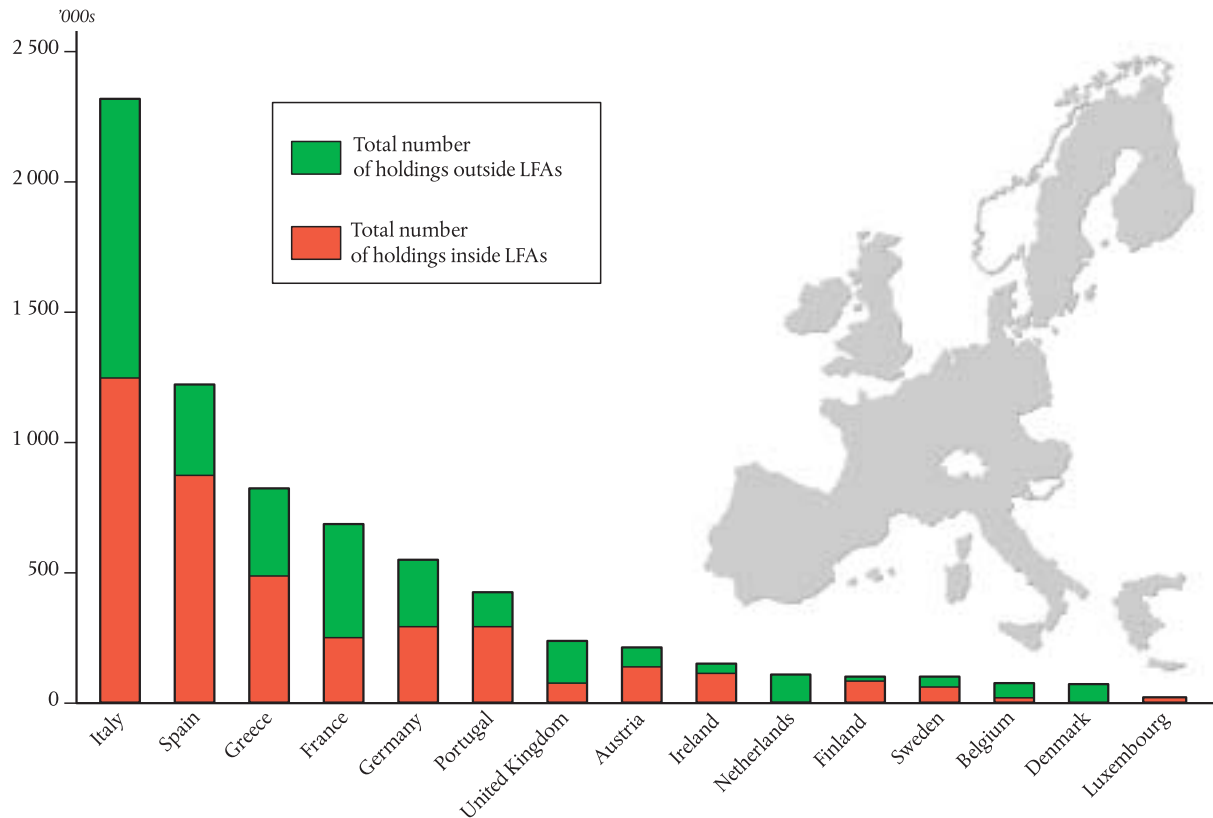
1. Support for rural development constitutes the second pillar of the common agricultural policy (CAP). It accompanies and supplements the CAP's other traditional instruments for the management of markets, which fall under the first pillar. Its general objectives are not only those of the CAP (Article 33 of the Treaty establishing the European Union), but also those of other provisions of the Treaty, in particular economic and social cohesion (Article 158) and environmental protection (Article 174).

2. In 1999, rural development support underwent a significant reform aimed at making it more consistent. The nine Regulations that governed it were grouped together in a single document (Council Regulation (EC) No 1257/1999 ⁽¹⁾, which lays

down the support framework and establishes 22 aid measures. One of these measures (Article 13 (ff)) concerns the support given to farmers in the LFAs. The aid is paid from the EAGGF –Guarantee Section and is implemented, along with other Guarantee payments, by means of a total of 89 rural development plans (RDPs), covering the period 2000 to 2006, which have been developed by the Member States' authorities and approved by the Commission.

3. Around 56 % of the agricultural area in use in the Union (UAA) is classified as less favoured. This scheme benefits some 3 900 000 agricultural holdings, or 55,8 % of the total. In 2001, its overall cost amounted to around 2 000 million euro (an average of 500 euro per holding), of which around a half is borne by the budget of the European Union. EU expenditure on the less-favoured-areas scheme represents 18,7 % of the overall budget authorised by the Berlin Council over the period 2000 to 2006 (32 906 million euro) ⁽²⁾.

Holdings in less-favoured Areas



Source: Eurostat 1997

Graph 1

⁽¹⁾ Council Regulation (EC) No 1257/1999 of 17 May 1999 (OJ L 160, 26.6.1999, p. 60).

⁽²⁾ Subheading 1(b) of the relevant Financial Perspectives.

Audit field

4. Community aid for less-favoured areas goes back to 1975, with the publication of the first Directive ⁽¹⁾, which established 'the particular nature of agricultural activity, which results from the social structure of agriculture and from structural and natural disparities between the various agricultural regions' and defines the notion of less-favoured areas.

5. Subsequent regulations, which concerned the improvement of the efficiency of agricultural structures ⁽²⁾ or rural development aid, only adapted this definition.

6. Current Community regulations ⁽³⁾ distinguish between three categories of less-favoured regions:

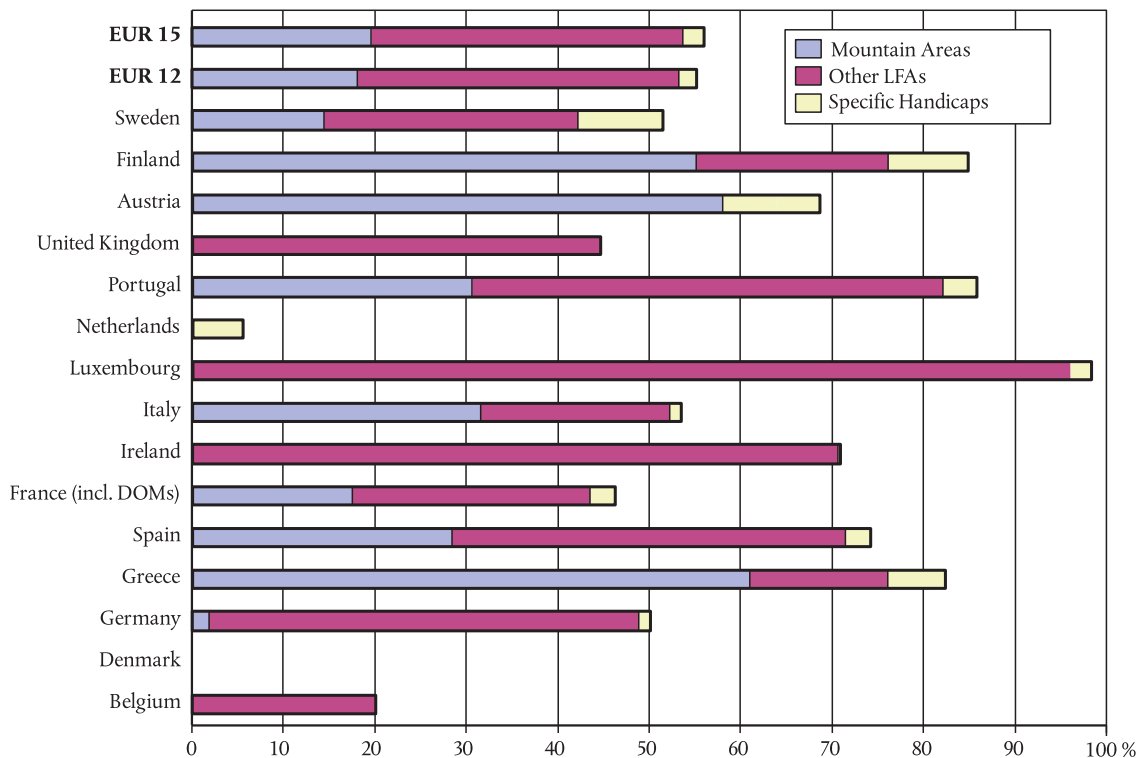
- (a) mountain areas, characterised by a considerable limitation of the possibilities for using the land and an appreciable increase in the cost of working it due to altitude or slope; areas north of the 62nd parallel and certain adjacent areas are assimilated to mountain areas;

- (b) other less-favoured areas, which are areas with poor productivity which are in danger of abandonment and where the accelerated decline in activity calls into question the viability of the area and its continued habitation;

- (c) areas affected by specific handicaps, in which farming needs to be continued, subject, where necessary, to certain conditions, in order to conserve or improve the environment, maintain the countryside and the area's tourist potential or protect the coastline.

7. While, overall, the areas classified as LFAs account for 56 % of the Community's UAA ⁽⁴⁾, this rate varies considerably from one Member State to another, ranging from 1 % for Denmark to more than 98 % for Luxembourg. In addition to the particular disadvantages of mountainous areas, Member States have identified other zones as being less favoured in their view. All but three Member States have also identified zones with specific handicaps resulting from, for example, the need to preserve the tourist potential, maintain the countryside or protect the coastline.

LFAs as a proportion of total UAA per Member State



Source: Document of the STAR Committee VI7675/98. Situation as of March 1998.

Graph 2

⁽¹⁾ Council Directive 75/268/EEC of 28 April 1975 on mountain and hill farming and farming in certain less-favoured areas (OJ L 128, 19.5.1975).

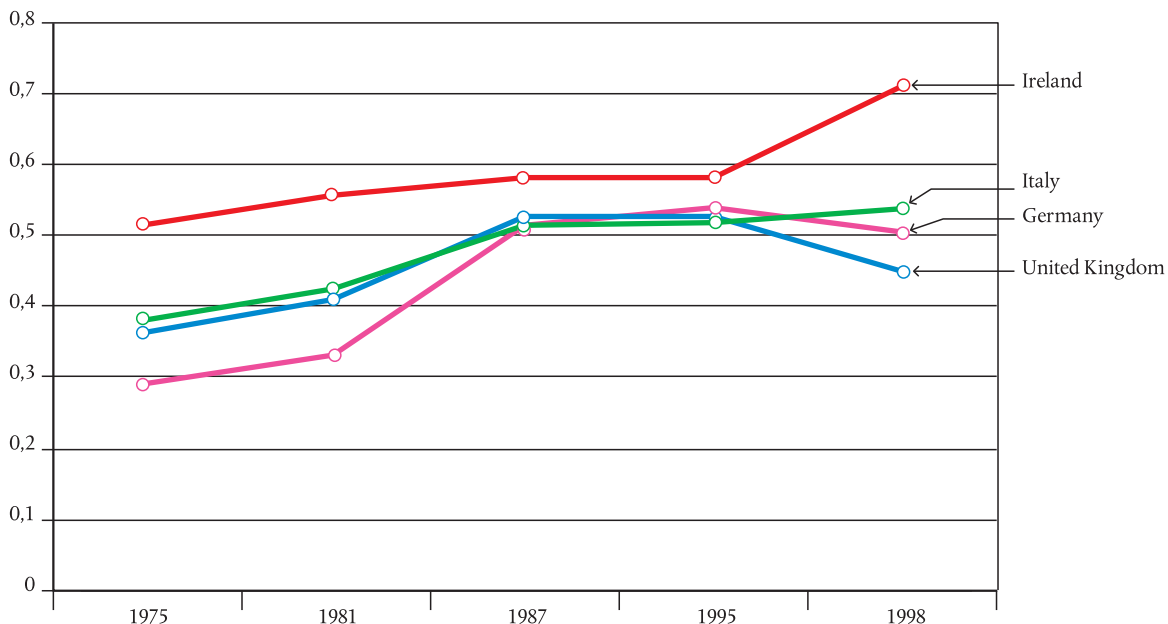
⁽²⁾ Council Regulation (EC) No 950/97 of 20 May 1997 (OJ L 142, 2.6.1997).

⁽³⁾ Council Regulation (EC) No 1257/1999 of 17 May 1999, Article 17 (OJ L 160/80, 26.6.1999).

⁽⁴⁾ Commission Document DG AGRI reference: STAR VI/7675/98.

8. For some Member States, this rate has varied considerably over time. Thus, between 1975 and 1998, it went up from 37,7 % to 53,6 % for Italy and from 51,2 % to 70,9 % for Ireland. Given that mountainous areas have not changed, the increases are all the more remarkable in view of the advances in soil improvement and varietal development. Since 1998, these percentages of land identified as less favoured have not changed.

Development of the percentage of less-favoured areas in the Member States where it was the most significant

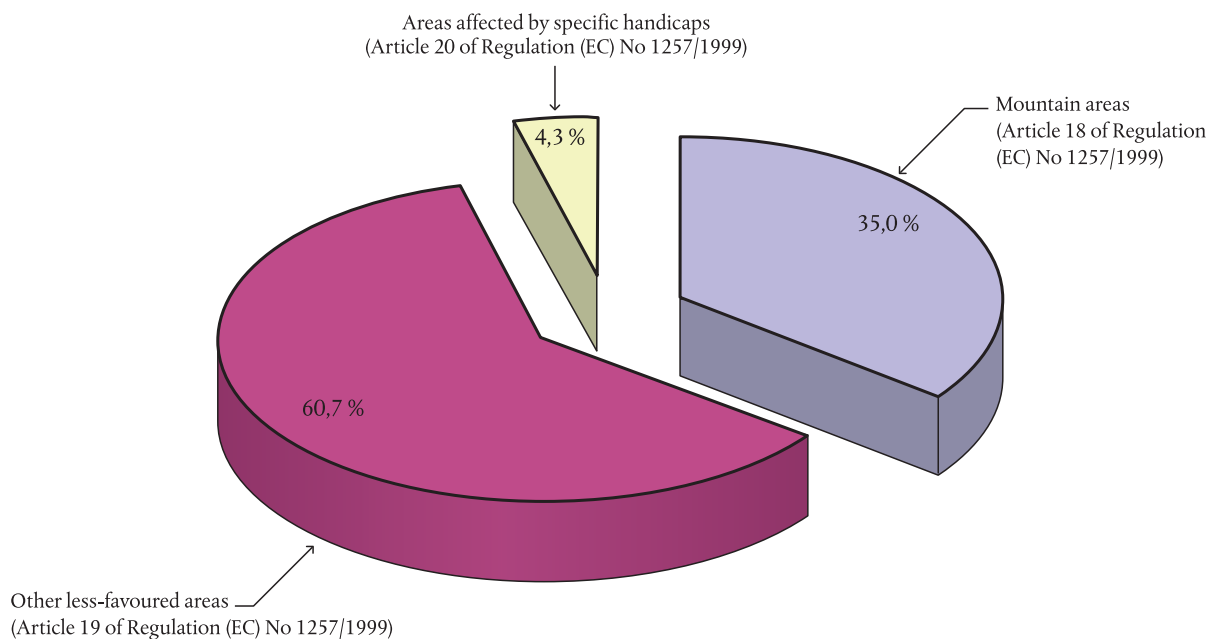


Source: STAR Committee Document, Ref: VI7675/98.

Graph 3

9. In terms of land area, the second category mentioned in paragraph 6 (other less-favoured areas) is considerably larger. For this important category, the Regulation does not provide clear common criteria.

Distribution between the three categories of less-favoured areas in 1998



Source: STAR Committee Document, Ref: VI/7675/98.

Graph 4

Scope of the audit

10. The objective of the audit was to examine to what extent the Commission:

- (a) has taken appropriate steps to correct any shortcomings, in particular with regard to classification decisions and the impact of the measure (see paragraphs 22 to 42);
- (b) has a reasonable assurance that the payments made for aid for less-favoured areas comply with the criteria of legality and regularity (see paragraphs 43 to 57);
- (c) has introduced a monitoring and evaluation system that makes it possible to appraise the effectiveness of the measure (see paragraphs 58 to 74).

11. The data available to the Commission were examined to assess the implementation of the measure both at the financial level and in terms of its objectives. This work was supplemented with a documentary check centred on both the degree of support offered to less-favoured areas and the administrative and control systems set up by the Member States, at local, regional and national level, in particular in the context of the RDPs.

12. On-the-spot checks looked at the systems for the management of the measure in a region of each of the four Member States (France, Finland, Austria and Germany) selected on the basis of their financial significance ⁽¹⁾, the eligibility conditions in force and a preliminary assessment of the administrative and control systems in place. The first stage of the audit work consisted of tests on the key controls ⁽²⁾ and was carried out in each region on a sample of 30 beneficiaries (agricultural holdings), selected on a random basis.

13. The audit work carried out in the holdings was divided among documentary checks, the physical examination of the factors that governed the granting of the aid (pasture land, fodder crops, livestock, etc.) and the verification of the actual payment of the aid. Subsequently, checks were carried out at the main public bodies involved in management (in particular at the administrative accounting and audit levels), concerning in particular the accuracy of payment procedures and the payments made and their compliance with the applicable regulations.

⁽¹⁾ In relation to the budget estimates for the 2000 to 2006 programming period.

⁽²⁾ A key control is a control procedure aimed at identifying operational shortcomings; they are identified via a risk analysis of the systems in place.

Eligibility and financing conditions*Eligibility conditions*

14. In addition to the geographical criteria related to the location of the holding, for the 2000 to 2006 programming period, beneficiaries must fulfil three requirements, whilst, at the same time, complying with the rules on the use of phytosanitary sprays, etc., and veterinary products.

They must:

- farm a minimum area (established by each Member State),
- carry out their agricultural activity in a less-favoured area for at least five years from the first payment of aid,
- apply usual good agricultural practices compatible with the need to safeguard the environment and maintain the countryside, in particular by sustainable farming.

Financial framework

15. Under the scheme provided for in Regulation (EC) No 950/97, the Member States could choose between two systems: the aid could be paid out either on the basis of the number of animals, expressed in adult bovine units (ABUs), or on the basis of the land area farmed. Since the entry into force of Regulation (EC) No 1257/1999, compensatory amounts must be calculated on the basis of the number of hectares, with, however, the possibility of a transition period limited to the year 2000 for those Member States that have hitherto used the per head criterion. At the same time, the financing of the Community contribution passed from EAGGF-Guidance to EAGGF-Guarantee (see paragraph 57).

16. The aid consists of a compensatory allowance, the unit value of which is established by the Member States within a range of 25 to 200 euro per hectare ⁽³⁾. It should be sufficient to compensate for existing handicaps whilst avoiding overcompensation. The maximum amount may be exceeded in individual cases, provided that the average level of aid paid out by each Member State respects this limit.

17. Expenditure for the financial years 2000 and 2001 were 674 million euro and 919 million euro, respectively. As the following table shows, there were significant developments in certain Member States. While the differences between expenditure in 2000 and 2001 may be partly due to delays in the preparation and approval of RDPs, this does not explain the large differences, particularly as the measure itself has been operating for many years.

⁽³⁾ Council Regulation (EC) No 1257/1999, Annex 1.

Table: Expenditure incurred over the period 2000 to 2001

	2000		2001		Change 2000 to 2001 (%)
	mio EUR	%	mio EUR	%	
Belgium	0,14	0,02	—	—	- 100
Denmark	0,04	0,01	0,34	0,04	+ 750
Germany	109,62	16,26	108,95	11,75	- 1
Greece	4,50	0,67	8,42	0,91	+ 87
Spain	1,76	0,26	53,41	5,76	+ 2 935
France	212,17	31,47	198,33	21,40	- 7
Ireland	45,10	6,69	110,98	11,97	+ 146
Italy	13,34	1,98	38,48	4,15	+ 188
Luxembourg	0,42	0,06	3,89	0,42	+ 826
Netherlands	0,04	0,01	0,38	0,04	+ 850
Austria	102,70	15,23	104,81	11,31	+ 2
Portugal	0,00	0,00	74,86	8,08	—
Finland	143,67	21,31	128,26	13,48	- 11
Sweden	1,76	0,26	16,08	1,73	+ 814
UK	38,94	5,78	72,40	8,60	+ 86
Total	674,22	100,00	919,59	100,00	

Source: Commission, revenue and expenditure account.

The breakdown of responsibilities

18. The Council establishes rural development policy by adopting the basic Regulation.

19. The Commission adopts the procedures for its implementation. In particular, it approves the rural development plans, for whose monitoring and evaluation it is also then responsible. From the accounting point of view, it records the expenditure declared each month by the Member States and reimburses them the Community's share of the funding.

20. The Member States are responsible for establishing the less-favoured areas, designating the authorities responsible for drawing up rural development plans and implementing the measure both from the administrative and control points of view. They also supply the Commission with the necessary data to enable effective monitoring of the implementation of rural development programming.

Previous observations by the Court

21. The Court has previously looked at support measures for less-favoured regions. The results of its last audit on the subject were published in 1991 ⁽¹⁾. On that occasion, it noted the continuous extension of less-favoured areas and spoke out in favour of a regular evaluation of criteria for appraising handicaps. Since then, the Court has examined various aspects of the measure, in particular in the context of its work on the annual Statement of Assurance.

⁽¹⁾ OJ C 324, 13.12.1991, p. 141.

THE CLASSIFICATION OF AREAS AS LESS FAVOURED AND ITS CONSEQUENCES

Classification criteria whose validity remains to be shown

The current situation of classification decisions

22. As indicated in paragraph 6, certain eligibility characteristics apply for a specific area to qualify as less favoured. Until 1999 this was done on the basis of a reasoned request by the Member States to the Commission. The Council, on the basis of a proposal by the Commission, then adopted the list of LFAs. The Court examined the documentary evidence held by the Commission in support of these classification decisions.

Evidence to justify classification decisions

23. *Annex I* shows, by Member State, the documents found at the Commission that contain evidence to justify the classification of certain areas as less favoured. Documentary evidence in support of classification decisions during the period 1975 to 1985 could not be presented to the Court during the audit. Only rarely ⁽¹⁾ could evidence be found of a review of the continuing validity of the classification.

24. In its Annual Report for the year 1990, the European Court of Auditors found '... the continuous growth of the less-favoured areas', and stated that '... the possibility cannot be ruled out that a regular assessment of the actual level of handicap in all the less-favoured areas of the Community will lead to the discovery that, in certain parts of these areas, there are no longer any handicaps left'.

25. In 1993, following the Court's observations, the Commission undertook a review of LFA classifications by asking Member States to supply an underlying justification of their own classification. However, this operation faced several difficulties and delays. Some Member States submitted incomplete data, data containing errors or nothing at all; also, in several cases, the requested information was submitted late.

26. Internal notes of the Commission, analysed by the Court, show that the Commission was faced with serious opposition from Member States to examine properly the continuing validity of underlying data for classification. Indeed extensive correspon-

dence took place and, at various Management Committee (Committee on Agricultural Structures and Rural Development) meetings, the lack of justification data was discussed. In the last analysis, the Court could not find any evidence that the review was properly finalised.

27. Although the Commission has indicated that there is 'permanent pressure of Member States to extend the LFAs' ⁽²⁾, it did not propose amending the existing arrangements in its proposal in 1996 on improving the efficiency of agricultural structures ⁽³⁾. On the contrary, this proposal led to the adoption of Council Regulation (EC) No 950/97 ⁽⁴⁾, subsequently replaced by Regulation (EC) No 1257/1999 which, in the latter text, states that all Council and Commission directives adopting lists of LFAs shall remain in force.

28. Moreover, since the entry into force of Regulation (EC) No 1257/1999, decisions adopting or modifying lists of less-favoured areas are no longer taken at the Community level, but by the Member States, who then notify the Commission. Thus, the Commission no longer holds the final responsibility for the validity of these classifications, a major component of the aid scheme. The Court considers that this is a major weakness in the Regulation, particularly in view of the coming accessions.

The consequences of the current situation

29. The inability to carry out an objective assessment of the decisions adopting the lists of less-favoured regions may have a considerable impact on their validity. This can be illustrated by the case of Luxembourg. The less-favoured areas of this country were established in April 1975 ⁽⁵⁾. At that time, more than 96 % of the total UAA was classified as less favoured because of the threat of abandonment and a further 2,45 % was classified as having a specific handicap. Since then, no change has been made to this classification. However, recent data from Eurostat show that certain macro- and socioeconomic indicators have changed considerably and that large areas would no longer satisfy the eligibility criteria ⁽⁶⁾.

⁽²⁾ European Commission Directorate General for Agriculture (DG VI), CAP 2000 working document, 'Rural Developments', July 1997, p. 59.

⁽³⁾ OJ C 115, 19.4.1996, p. 34.

⁽⁴⁾ Council Regulation (EC) No 950/97 of 20 May 1997 (OJ L 142, 2.6.1997).

⁽⁵⁾ Council Directive 75/274/EEC of 28 April 1975 concerning the Community list of less-favoured farming areas within the meaning of Directive No 75/268/EEC (Luxembourg) (OJ L 128, 19.5.1975, pp. 226 to 228); the criteria used were, *inter alia*, farm income (below 80 % of Community average).

⁽⁶⁾ In 1975, average farm income in Luxembourg was below 80 % of average farm income in the Community as a whole, but in 2000, it was some 20 % higher.

⁽¹⁾ See Annex I, only for two out of 10 Member States.

A multitude of indicators leading to disparities

No uniform identification of less-favoured areas by the Member States

30. The Court also examined the criteria used by Member States to qualify certain areas as less favoured. As indicated in paragraph 9, the most important category concerns the areas in danger of abandonment (Article 19 of Regulation (EC) No 1257/1999). This category alone represents 60,7 % of the LFAs. The Court therefore looked more particularly at this category in its examination of the criteria used.

31. The aforementioned Regulation ⁽¹⁾ identifies three common criteria used for identifying areas in danger of abandonment:

- (a) land productivity (the presence of land of poor productivity, unsuitable for cultivation and with a limited potential which cannot be increased except at excessive cost, and mainly suitable for extensive livestock farming);
- (b) economic performance (the production which results from the low productivity of the natural environment is appreciably lower than the average with regard to the main indices of economic performance in agriculture);
- (c) population (either a low or dwindling population, which is predominantly dependent on agricultural activity, the accelerated decline of which would jeopardise the viability of the area concerned and its continued habitation).

32. Thirteen Member States identified areas corresponding to these criteria. Denmark and the Netherlands did not identify areas under this category.

33. *Annex II* shows that Member States use a wide variety of indicators to define the three aforementioned criteria. No fewer than 17 indicators are used for land productivity, 12 for economic performance and three for population. Almost all Member States use their own unique indicator(s) for the criteria of land productivity and economic performance. The Commission has not studied the impact of these various indicators to ensure that the concept of common criteria, as indicated in the 25th preamble of the Regulation, is applied.

34. With regard to the population, a great disparity was noted in respect of the thresholds adopted. Thus, the reference figure for overall population density ranges from 27 inhabitants/km² (Ireland) to 130 inhabitants/km² (Germany), and the agricultural population rate varied between 15 % (applied by five Member

States ⁽²⁾ and 50 % (Greece). Austria, Finland and Sweden, who joined the EU together in 1995, did not set a threshold for agricultural population, the requirement only being that the proportion of the agricultural population should be 'significant'.

A wide range of indicators leading to disparities in treatment

35. This variation in indicators as the result of different national priorities may lead to disparities in treatment among beneficiaries. The Court was informed during its audit on the spot that the beneficiaries, especially in border areas, wondered why, in apparently similar local situations, Member States had taken decisions which led to considerable differences in the allocation of compensatory allowances.

36. The Commission itself noted in a 1997 working document ⁽³⁾ on the previous LFA scheme that, 'Community legislation allows Member States a considerable leeway in the implementation of the LFA scheme. [...] The different priorities identified by Member States or regions lead to different criteria being established for the eligibility of beneficiaries [...], for example:

- (a) the average payment per beneficiary holding varies from 4 437 ecu in Luxembourg to 410 ecu in Portugal;
- (b) beneficiary holdings as a proportion of those in eligible areas varies between 84 % and 99 % in many northern Member States to 9 % in Italy.'

37. The report continues, 'Analysis shows that, whereas incomes in LFAs are lower in comparison with non-LFAs within the same national boundaries, they can be higher than incomes in non-LFAs in other countries' ⁽⁴⁾.

Support measures where there is a risk of overcompensation

38. Most of the beneficiaries visited by the Court ⁽⁵⁾ believed that the receipt of compensatory allowances had allowed them to continue farming and living in areas which they otherwise might have been obliged to leave. However, in the absence of proper overall evaluation results (see paragraph 72), no definitive conclusion can be drawn on the effectiveness of the compensatory allowances. An assessment of the policy outcomes is made difficult because the Commission has set no specific quantified objectives for this measure, despite this being a requirement of the Financial Regulation ⁽⁶⁾.

⁽²⁾ Belgium, France, Germany, Italy and Luxembourg.

⁽³⁾ European Commission Directorate General for Agriculture (DG VI), CAP 2000, working document, 'Rural Developments', July 1997, p. 54.

⁽⁴⁾ European Commission Directorate General for Agriculture (DG VI), CAP 2000, working document, 'Rural Developments', July 1997 p. 55.

⁽⁵⁾ Thirty beneficiaries selected per region audited.

⁽⁶⁾ Article 27(4).

⁽¹⁾ Council Regulation (EC) No 1257/1999.

39. Articles 15(1) and 16 of Regulation (EC) No 1257/1999 require compensatory allowances to be fixed at a level which makes an effective contribution towards compensating for existing handicaps yet avoids overcompensation. The Regulation does not specify the level of compensation any further. Thus, neither the Member States nor the Commission are in a position to evaluate objectively whether overcompensation exists. This is compounded by the fact that the same Regulation gives Member States a considerable degree of freedom in adapting the scheme to local priorities.

40. There is no indication in the legislation as to who is actually responsible for monitoring overcompensation. The division of responsibilities between Member States and the Commission is not defined. As a result, there are insufficient arrangements for verifying whether or not systematic overcompensation occurs in practice. The Court considers that the Commission should examine how, within the context of checking the implementation of the regime in the Member States, the possible incidence of such overcompensation can be identified.

The measures taken by the Member States

41. Without any common guideline on how overcompensation may be identified, Member States have adopted their own measures, which may put some farmers at a disadvantage compared to others. The requirements in rural development plans include:

- (a) limiting the total sum receivable through LFA aid regardless of entitlement ⁽¹⁾;
- (b) specifying certain stocking densities for particular areas ⁽²⁾;
- (c) restricting payments to certain eligible forage areas farmed by producers who keep extensively grazed sheep breeding flocks and suckler-cows ⁽³⁾;
- (d) limiting full payment to only part of the LFA area, excluding certain types of farming or allowing lower than permitted aid rates ⁽⁴⁾.

⁽¹⁾ Bavarian rural development plan.

⁽²⁾ Various rural development plans.

⁽³⁾ Rural development programme for England.

⁽⁴⁾ Payment of LFA aid at full rate only on the first 350 hectares. The following 350 hectares receive half rate (50 %) payments. Land in excess of 700 hectares receives no payments. Exclusion of LFA land used for certain enterprises: LFA payments are not be made on land used for dairy or other livestock production, except extensive sheep breeding and suckler cows.

Setting rates for compensatory allowances for moorland and common land at below the minimum of EUR 25/ha in order to reflect the typically larger farm size and limited agricultural vocation of such land.

42. Thus, when some Member States have identified the need for certain measures to limit aid, the Commission has not carried out an objective examination to ensure that:

- (a) the measures taken effectively remove the risk of overcompensation;
- (b) types of overcompensation identified in one Member State do not occur in others.

THE IMPLEMENTATION, MONITORING AND EVALUATION OF MEASURES IN SUPPORT OF LESS-FAVOURED AREAS

Weaknesses in the implementation of support measures

43. The quality of the implementation of the support scheme depends not only on the implementing provisions contained in the RDPs but also on the surveillance, management and control systems. It is therefore essential for the Commission to have a sufficient guarantee as to the quality of each of these components.

Rural development plans and good agricultural practices

44. Implementation procedures are laid down at national or regional level in the RDPs that are put forward by the Member States, approved by the Commission and specified in various implementation documents issued by the competent authorities. Good agricultural practices should be defined by the Member States ⁽⁵⁾. During its work on the verification of their consistency with Community rules and their applicability, the Court found the following:

- (a) good agricultural practices were often synonymous with mere compliance with the rules already applicable to agricultural holdings (nitrate Directive, etc.);
- (b) certain Member States, like France and Austria, added the notion of stocking density by introducing a condition relating to level of the stocking rate, an indicator that expresses the density of the herd(s) present on the holding in ABUs per hectare;
- (c) in France, however, the optimum stocking density was determined on the basis of usual practices already in place; moreover, the exclusion of certain types of livestock (particularly pigs and poultry), whose waste is therefore spread over the land of the holding, is questionable;

⁽⁵⁾ Commission document VI/10535/99.

- (d) some Member States include respect for the well-being of the animals among their good agricultural practices, but they do not clearly define the criteria for assessing it (France and Austria).

45. The Court notes that, at the moment, there is no verifiable, clear and consistent definition of 'good agricultural practices' for the purpose of assistance to the LFAs. In the absence of clear definitions and a consistent application, it is difficult to understand how this notion can constitute an objective basis for assessing the eligibility of aid financed from the Community budget.

46. Generally speaking, it was found that the provisions of the RDPs were consistent with the Community's rules. However, in the case of good agricultural practices, they too often merely borrow from other regulations and are not therefore in any position to promote farming procedures that are more demanding from the environmental point of view.

Surveillance systems

47. In order to be able to assess the legality and regularity of the allowance paid out, the Commission should be satisfied that the managers have relevant and precise information to guarantee the accuracy of the situations declared. The Commission should ensure that information systems exist to enable it to pronounce on compliance with the eligibility criteria.

48. During the compliance tests carried out by the Court during its on-the-spot audits, it examined the availability of this information and found the following:

- (a) in some Member States, there is no rule requiring the keeping of a register to show pest-control treatments, the spreading of waste and the use of fertiliser on the various parcels (France, Austria and Germany);
- (b) in Germany, some farmers carried out soil analyses by taking samples. Particularly high levels were sometimes found for nitrates or other substances. Little or no attention was given to the results, because this Member State has no stocking criterion ⁽¹⁾ in its definition of good agricultural practice;
- (c) in France, the procedure for verifying the area of land declared by the applicant and checking that it is actually the applicant who works the land does not enable the reliability of stocking rates to be guaranteed;
- (d) as a general rule, animals other than cattle, sheep and goats, such as poultry, pigs and horses, are not recorded.

⁽¹⁾ Reflecting livestock density.

Management and control systems

49. The management and control systems put in place by the Member States should make it possible to prevent, detect and correct any errors and significant weaknesses in good time. Their quality was evaluated by the Court by analysing the anomalies detected during the tests carried out on the representative sample of payments to beneficiaries.

50. In respect of procedures, the following was found in individual cases:

- (a) the information in the national database used for counting the cattle was not reliable (France); there was no systematic reconciliation between the data given on the aid application forms and those given in the livestock registers (Austria);
- (b) corrections made by beneficiaries to the histories of their cattle herds were inadequately verified (France);
- (c) compliance with the beneficiaries' commitment to continue their farming activity for five years was not systematically monitored (France and Austria);
- (d) the selection of the beneficiaries checked by the authorities did not take into account the risk factors specific to the measure (France) or the declarations were not always subject to appropriate administrative checks (Finland);
- (e) checks over the good maintenance of pasture land, which is one of the conditions for eligibility, were insufficient (France);
- (f) the documentation of checks on good agricultural practices was unsatisfactory and the bodies making the checks had little or no assurance that the relevant conditions were complied with (all the Member States visited); furthermore, checks sometimes lacked relevance and the follow-up given is sometimes uncertain (Austria);
- (g) the amount of the aid is determined by an indicator forwarded by the tax authorities, whose components and calculation procedures are unknown to the management body; it also depends on the nature of the crops, whose verification is very difficult without an appropriate register (Germany);
- (h) the possession, on the part of the beneficiary, of a manure-spreading certificate, which is one of the national conditions for the allocation of the allowance, was not systematically checked (Germany).

51. With regard to individual transactions, it came to light that:

- (a) in Austria, the animal numbers recorded were often wrong;
- (b) also in Austria, mountain pastures were significantly over-declared;
- (c) in France, in one third of the holdings audited, the cattle numbers recorded differed by more than 3 % as compared with the number calculated on the basis of the information contained in the departmental register.

The errors found do not necessarily have a financial effect, as the compensatory allowances may be capped.

52. Generally speaking, the reliability of the management and control systems was inadequate. The main cause of this was the poor quality of the data taken over from other management systems. The scale and the effect of the anomalies observed in each Member State are directly influenced by the degree of strictness of the conditions laid down (after approval by the Commission) by each of them. The stricter the conditions, the higher the risk of non-compliance. Moreover, the effectiveness of these management and control systems is also hampered by the fact that it is difficult to verify certain criteria relating to good agricultural practices, like, for example, the well-being of the animals.

53. The Commission also noted some of these shortcomings ⁽¹⁾ following an enquiry into the systems of management and control and the penalties introduced or envisaged by the Member States in the field of rural development.

54. Nevertheless, the Commission should more clearly ⁽²⁾ specify the characteristics that the eligibility criteria set by each Member State should have, in particular with regard to compliance with good agricultural practices, and ensure that they are verifiable.

Payments and the recording and booking of expenditure

55. The completeness and annuality of records are two generally accepted accounting principles. The correct booking of the transactions for the period was verified by examining the date of the payment of the aid due in the 2001 EAGGF year ⁽³⁾.

56. During the on-the-spot checks in the Member States, it was found that:

- (a) for all of France, according to the paying body's data at 31 March 2002, payments made after the closing date of the EAGGF year amounted to 18,1 million euro, or 8,5 % of all

the payments carried out under this year; moreover, no recoveries were made for the 2001 EAGGF year, because, according to the authorities, they were waiting for the various national regulations to be made consistent with one another;

- (b) in Finland, recoveries were only declared to the Commission when they were finalised; partial recoveries were not taken into consideration;

- (c) in Austria, only 75,5 % of the allowances due were paid out under the 2001 EAGGF year; indeed, although the beneficiaries had been notified of the total amount of the allowance to which they were entitled, the paying body, on the instructions of the ministry responsible, only paid out a fraction of the sum due; according to the authorities concerned, this was because of the introduction of a new system for the identification of handicaps (Berghöfekataster); according to the data supplied by the paying body, the remaining amount was 65 million euro, 32,7 million euro of which were chargeable to the Community budget, and was only paid out in June 2002; the Commission has not yet been officially informed by the Member State of the existence of the deferment of this payment.

57. Thus, in three of the four Member States visited, the Court identified significant anomalies in terms of the budgetary principles of completeness and annuality, even though they do not constitute irregularities in terms of the specific regulations for the measure.

Shortcomings in monitoring by the Commission and the Member States

58. According to Article 48 of Regulation (EC) No 1257/1999 the Commission and the Member States must ensure effective monitoring of implementation of rural development programming. The objective of monitoring is to assess the timely and proper implementation of the measure in both financial and physical terms. It must be carried out by way of jointly agreed procedures and by reference to specific physical and financial indicators agreed beforehand and written analyses. Member States are required to draw up annual progress reports containing information on monitoring activities ⁽⁴⁾.

⁽¹⁾ See the synthesis report of 20 August 2001 No AGR 019399.

⁽²⁾ It should be noted that, during 2002, the Commission and the Member States examined a document containing guidelines in the control field.

⁽³⁾ The 2001 EAGGF year ran from 16 October 2000 to 15 October 2001.

⁽⁴⁾ The annual progress reports should contain the following information (Article 53 of Regulation (EC) No 445/2002):

- changes in the general conditions of relevance to the implementation of the measure and in major socioeconomic trends;
- changes in national policies,
- the progress of measures and priorities,
- the action taken by the management authority and the monitoring committee, if any, to ensure high-quality and effective implementation,
- measures taken to ensure compatibility with Community policies.

Monitoring indicators

59. Pursuant to Article 53(2) of Regulation (EC) No 445/2002 ⁽¹⁾ and its predecessor ⁽²⁾ the Commission has adopted guidelines on common indicators for monitoring the rural development programming and expenditure for 2000 to 2006 ⁽³⁾.

60. In examining these guidelines on financial monitoring, it was noted that:

- (a) the annual progress reports to be submitted to the Commission are required to be produced on a calendar-year basis ⁽⁴⁾; this reference period differs from the EAGGF-Guarantee financial year ⁽⁵⁾, thus making budgetary monitoring of LFA expenditure more difficult and less transparent;
- (b) financial data included in the annual progress reports concern commitments made under Regulation (EC) No 1257/1999, rather than payments; payment data would be more appropriate, reflecting actual expenditure incurred.

The data supplied by the Member States

61. Apart from the general weakness in the reporting system, there were also shortcomings in the data transmitted by the Member States. They are required to submit the progress reports before 30 April of the following year. Only a few Member States submitted their reports by this deadline. Some were submitted half a year later. Most provided financial and other information for the LFA measure, but the written analyses of changes in general conditions, progress with implementation and actions taken by the management authority were often incomplete or non-existent.

62. The fact that the lateness and absence of information had adversely affected monitoring was confirmed by the Commission, which stated in its guidelines that 'several apparent difficulties and inconsistencies in completing the indicator tables were observed' and 'the quantity and quality of common monitoring data received for the year 2000 would be unlikely to permit effective monitoring of the implementation of the measure or provide reliable aggregation of monitoring data at Community level'. From the end of 2001 to the spring of 2002, the Commission, together with the Member States, examined the monitoring indicators in order to improve them.

⁽¹⁾ Regulation (EC) No 445/2002 of 26 February 2002 (OJ L 74, 15.3.2002, p. 1).

⁽²⁾ Commission Regulation (EC) No 1750/1999 of 23 July 1999 (OJ L 214, 13.8.1999, p. 31).

⁽³⁾ Commission working document VI43512/02.

⁽⁴⁾ Article 53 of Regulation (EC) No 445/2002.

⁽⁵⁾ The EAGGF year runs from 16 October of year n-1 to 15 October of year n.

The Commission's use of data

63. The Commission could not fully exploit the progress reports presented by the Member States for the year 2000 because of the little information supplied. With regard to the data for 2001, the deadline for the submission of the annual reports was changed to the end of June 2002 to enable Member States to adapt to the revised system of monitoring indicators. As a result, at the end of the audit in July 2002, the Commission had not analysed these reports.

Improvements to be made in the implementation and use of assessments

64. Article 49 of Regulation (EC) No 1257/1999 requires that the measures covered by the RDPs should be evaluated. The objective of evaluation is to assess the results and impact of the aid schemes, and to analyse their effectiveness. The Commission has a key role in ensuring the effectiveness of evaluation and its dissemination.

Guidelines on evaluation

65. The Commission has prepared guidelines for evaluation of the measures for the programming period 2000 to 2006 as required under Article 54(2) of Regulation (EC) No 445/2002, concerning mid-term and *ex post* evaluations ⁽⁶⁾. The guidelines consist of common evaluation questions together with criteria and indicators. The Court made an analysis of these indicators for the LFA measure by comparing them with the overall evaluation approach followed by the Commission ⁽⁷⁾. In general, they are adequate, with the exception of questions and criteria relating to the effectiveness of the measure in avoiding overcompensation for handicaps (see also paragraphs 38 to 42).

The quality of evaluations

66. According to Article 49 of Regulation (EC) No 1257/1999, rural development measures must be carried out on the basis of the principles laid down in Articles 40 to 43 of Regulation (EC) No 1260/1999. This implies that they should be subject to *ex ante*, mid-term and *ex post* evaluation.

The quality of the ex ante evaluations for the LFAs measure for the new programming period

67. According to Article 55(1) of Regulation (EC) No 445/2002 and its predecessor, the RDPs are required to include an *ex ante* evaluation analysing the disparities, shortcomings and

⁽⁶⁾ Commission document VII2004/final.

⁽⁷⁾ MEANS evaluation approach.

potentials of the current situation, assessing the consistency of the proposed strategy with the situation and targets and to take into account the issues raised in the common evaluation questions. They must also assess the expected impact of the selected priorities for action and quantify their targets where possible as well as verify both the proposed implementing arrangements and consistency with the CAP and other policies.

68. The Court found that the relevance of the information provided in the *ex ante* evaluations by Austria, Finland, France and Germany (Bavaria) for the programming period 2000 to 2006 on LFAs was particularly limited. Although, in most cases, they follow the required structure, appropriate information on the above-mentioned elements is rare.

The quality of the evaluations for the previous programming period

69. Article 6 of Regulation (EEC) No 2052/88 ⁽¹⁾ provides the legal basis for the evaluation of the measure under the previous programming period (1994 to 1999). By June 2002, the Commission had received evaluations from 10 Member States and it performed a quality assessment on three of these reports: Austria, Finland and France. This quality assessment indicates that various aspects of the evaluations should be improved, in particular the methodology applied, the quality of the data used and the drawing up and the validity of the conclusions.

70. The Court's analysis of the RDPs for the new programming period shows that the conclusions and recommendations made in the mid-term evaluations have been taken into account by the Member States concerned. For example, the Finnish and French evaluators had recommended the change from the per-head-based system for calculating the aid to a hectare-based system.

71. However, at the same time instances were noted where no impact could be identified on the design of the RDPs:

- (a) the French evaluators had highlighted the need to perform a review of the classification of the eligible areas, as the socio-economic situation in certain regions has changed and therefore the classification (outside mountain areas) is no longer necessarily valid;
- (b) the German evaluators had recommended ensuring better coordination of the environmental aspects of the compensatory allowances with the agri-environmental scheme.

Ex post evaluation of the measure during the previous programming period(s)

72. Although support for LFAs has been provided since 1975, no complete evaluation of the measure has so far been made. It is

⁽¹⁾ Council Regulation (EEC) No 2052/88 of 24 June 1988 (OJ L 185, 15.7.1988, p. 9).

therefore to be welcomed that the Commission included an overall evaluation of the measure in its evaluation programme for 2002. The results are expected to be available at the end of 2003.

73. The Commission did, however, perform an interim evaluation of the measures for Structural Fund Objective 5a (including the LFA scheme) in 1999. This was done on the basis of reports supplied by the Member States ⁽²⁾ and was mainly limited to analysing monitoring data. The report does not include any specific results or conclusions concerning the LFA measure. However, there were common conclusions that the procedures, including those for LFAs, should be simplified, and that the indicators were too general in nature to allow a relevant assessment. A number of programmes were criticised for not having a clear strategy.

74. The Court could find no evidence of the extent to which the results of the information obtained through this evaluation had been taken into account in designing the Regulation for the new programming period.

CONCLUSIONS AND RECOMMENDATIONS

75. Support for LFAs has become a key constituent of rural development policy, and it is of prime importance that the Commission should:

- have proper evidence to judge the validity of the classification of the various areas as less favoured,
- have sound information on the impact of the measure, in particular the extent to which it avoids overcompensating for handicaps,
- have appropriate assurance as to the legality and regularity of expenditure,
- use the information on implementation efficiently and in good time in order to monitor the measure effectively.

Since 1993 the Commission has called into question the relevance of existing LFA classifications and their durability. However, this has not led to any changes in the rules.

76. The Commission has insufficient evidence that the LFA classification decisions are still valid, which affects the efficiency

⁽²⁾ Commission document, dated 1 November 1999 called 'Interim evaluation of rural development programmes (objectives 5(a) and 5(b))'.

and effectiveness of the implementation of the aid scheme (see paragraph 23). This may lead to a classification that is no longer justified, as was explained in paragraph 29, and thus to an unjustified allocation of aid. Member States use a wide range of indicators to determine whether areas are less favoured or not (see paragraph 33), which may lead to disparities in the treatment of beneficiaries.

77. The Commission should:

- (a) perform a complete and in-depth review of existing classifications of all LFAs;
- (b) develop, in close collaboration with the Member States, a more appropriate set of indicators for identifying LFAs that would be consistent and guarantee an equitable treatment of the beneficiaries.

78. The Commission is insufficiently informed on the impact of the LFA support scheme. In the absence of an appropriate overall evaluation (see paragraph 72), it is not possible to give a definitive judgement on the effectiveness of the compensatory allowances in compensating for existing handicaps and therefore guarantee that resources are being used properly.

79. The Commission should:

- (a) try to obtain relevant information on the impact of the scheme;
- (b) examine how, within the context of checking the implementation of the regime in the Member States, the possible incidence of overcompensation can be identified and, if necessary, propose the changes needed to prevent this phenomenon.

80. The quality of the management and control systems put in place by the Member States suffers from the weak control environment due to the impossibility of satisfactorily verifying one of the key eligibility criteria (compliance with good agricultural practices) (see paragraph 52); the procedures for the recording and payment of aid do not always follow the accounting principles of completeness and annuality (see paragraph 57). Furthermore, objective information on compliance with the eligibility criteria is not always available (see paragraph 48). The weaknesses

in these management and control systems adversely affect the legal and regular implementation of the measure.

81. The Commission should:

- (a) ensure that Member States provide a definition of 'good agricultural practices' which is clear and can be conveniently verified; if this is not possible, the Commission should propose a system of support for LFAs which relies on a more clear and controllable concept than 'good agricultural practices';
- (b) develop an inventory of existing regional/local practices in relation to specific farming conditions;
- (c) give full guidance to Member States on the requirements of an effective control system;
- (d) ensure that the checks performed are effective;
- (e) ensure that the Member States comply with the general accepted accounting principles, in particular as regards annularity and completeness, for recording and paying the EAGGF-Guarantee compensatory allowances.

82. During the years 2000 and 2001, Member States did not supply the Commission with complete and timely information, which was necessary for appropriate monitoring (see paragraphs 61 to 62). The Commission did not make proper use of the data made available (see paragraph 63).

83. The Member States should present complete and timely information required for monitoring.

The Commission should:

- (a) ensure that the Member States comply with the obligation to present complete data in good time;
- (b) re-examine the relevance of the indicators used for monitoring the measure.

This Report was adopted by the European Court of Auditors in Luxembourg at its meeting of 10 April 2003.

For the Court of Auditors
 Juan Manuel FABRA VALLÉS
 President

ANNEX I

Existence of underlying data for LFA classification and Commission's review of that data

	1975-80			1981-85			1986-90			1991-95			1996-		
	cl.	data	review	cl.	data	review	cl.	data	review	cl.	data	review	cl.	data	review
Belgium	I, M	+	+												
France	I, M	-	-	M	-	-	M	+	+	M	+	-	M	+	+
Germany	I, M	-	-	M	-	-	M	+	+	M	+	+	M	+	+
Ireland	I, M	-	-	M	-	-				M	+	+	M	+	+
Italy	I	-	-	M	-	+	M	-	+	M	+	-			
Luxembourg	I	+	+												
Netherlands	I	-	-	M	-	-	M	+	+	M	+	+			
UK	I	-	-	M	-	-	M	+	+						
Greece				I, M	-	+	M	-	-	M	+	+			
Portugal							I, M	+	-						
Spain							I, M	-	-	M	+	+	M	+	-
Austria										I	+	+	M	+	+
Finland										I	+	+	M	+	+
Sweden										I	+	+	M	+	+
Denmark													I	+	+
+/Total		2/8	2/8		0/7	2/7		5/8	5/8		10/10	8/10		8/8	7/8

cl.: classification

I: initial classification

M: modification/extension

data: underlying data for classification/modification

review: Commission review of underlying data and justifications

+: evidence found in the Commission archives

-: evidence not found in the Commission archives.

ANNEX II

Indicators used for the common criteria for less-favoured areas in danger of depopulation

(Source: STAR document, ref.: VI7675/98)

Criteria	Indicators used		MSs that apply the indicator	Limit value
Land productivity	1.	agricultural comparability index (BZ)	1	30
	2.	number of days without frost	1	150
	3.	production from bovine animals	1	70 %
	4.	Nikula index	1	440
	5.	potential natural yield index	1	
	6.	final agricultural production per ha	1	80 %
	7.	agricultural comparability index (LVZ)	1	28
	8.	yield	4	66 to 84 %
	9.	percentage of ploughed area	1	7,8 %
	10.	stocking rate (LU/ha)	3	1 to 1,19
	11.	farm rent	2	65 %
	12.	at least 50 % of the UAA of the 'Concelho' is affected by serious handicaps	1	50 %
	13.	productivity index 'L. Turc'	1	30
	14.	arable land/productive area	1	50 %
	15.	standard index of yields	1	80 %
	16.	gross value added of holdings per annual work unit	1	80 %
	17.	grassland/total UAA	1	70 %
Economic performance	1.	agricultural comparability index (BZ)	1	30
	2.	earned income per work unit	1	77 %
	3.	Nikula index	1	440
	4.	potential natural yield index	1	
	5.	agricultural comparability index (LVZ)	1	28
	6.	farm income per labour unit	3	80 %
	7.	indices related to livestock density	2	66 % or 0,2
	8.	net value added at factor cost per agricultural worker	1	80 %
	9.	standard gross margin (SGM)	1	80 %
	10.	standard index of yields	1	80 %
	11.	gross value added of holdings per annual work unit	1	80 %
	12.	labour income per man-work unit	1	80 %
Population	1.	population density	13	27 to 130/km ²
	2.	depopulation rate	7	0,5 to 2 %
	3.	agricultural population	13	15 to 50 %

THE COMMISSION'S REPLIES

SUMMARY

- III. (a) The bulk of the work on designating less-favoured areas (LFAs) was completed during the previous programming period (1994 to 1999) on the basis of the information provided by the Member States. Under the new rules for the current programming period 2000 to 2006, the designations have remained largely unchanged (see replies to point 28).
- (b) The use by Member States of different indicators within the general criteria established by the Regulation to determine LFA designation reflects the less-favoured character in relation to the productive agricultural areas within the Member State or region concerned (and not in comparison with other Member States).
- (c) During the process of approving the rural development programmes, the Commission examines the system and level of aid proposed. Several elements of Council Regulation (EC) No 1257/1999 minimise the risk of overcompensation (see point 40).
- (d) The Commission is aware of the complexity of the concept of good farming practices (GFPs), which depends on complex rules governing a variety of sectors.

That is why a practical approach was proposed to the Member States in 2000 in a guidance document ⁽¹⁾ (see reply to point 47).

Following its experiences of the definition and implementation of good farming practices in the first years of the programming period, the Commission has now proposed drawing up a Community framework for the statutory standards to be applied in farming (point 48) as part of the CAP reform.

- (e) The Commission shares certain concerns of the Court regarding the timing, quantity and quality of annual reports and the associated monitoring indicators provided by Member States.

However, 2000 was the first year in which the common monitoring system was completed under the new rural development programming structure introduced under Agenda 2000 and clearly this is a learning process.

- (f) A Community summary of the *ex post* evaluations is to be completed by the end of 2003. Furthermore, the evaluation methodology for rural development, including LFA, has been reinforced for the current programming period in cooperation with the Member States.

Pursuant to Regulation (EC) No 1257/1999, Member States quantify (where possible for the various measures (including LFA measures) in their rural development programmes (RDPs)) objectives which allow progress in implementing the monitoring process to be measured, and which provide a benchmark for the evaluations (see replies 38 to 71).

- IV. The LFA measure has provided substantial financial support to farmers living in the most disadvantaged areas of the European Union. It will continue to play an important role in maintaining sustainable agriculture and viable rural communities.

Following the Court's comments in its 1990 report, the Commission made a number of changes. It welcomes the present report and will take into account the observations and recommendations for the further development of the LFA measure as part of rural development policy.

GENERAL BACKGROUND

8. The increase occurred because these Member States decided to introduce the criteria for classifying eligible areas gradually, in the light of their priorities and available budget resources.

9. The Regulation provides a framework of common characteristics for classification of this type of area. Within the existing legislation, each Member State uses its own set of objective indicators.

17. The years 2000 and 2001 were atypical of the new programming period as most RDPs were not approved until the second half of 2000 and the switch from the Guidance to the Guarantee Section changed the funding mechanism. Much of the funding for programmes approved in year 2000 was paid in 2001 under the Guarantee Section.

21. See point 9.

Following the Court's comments in its 1990 report and as part of its continuing aim of improving checks on agricultural expenditure, the Commission has made a number of changes (introduction of minimum inspection standards, introduction of computer files on holdings, changes to the system by moving from a head-area payment to an area payment).

⁽¹⁾ Document VI10535/99. Version Rev. 7 was the latest update in December 2002. However, Rev. 2, distributed to the Member States in June 2000, included the recommendations on GFP.

THE CLASSIFICATION OF AREAS AS LESS FAVOURED AND ITS CONSEQUENCES

24 to 27. Like the Court, the Commission regrets that its efforts to review classification have proved unsuccessful.

28. The areas classified as less favoured in the Member States have undergone only very minor modifications since 1999 and are therefore effectively stable. Under the implementing rules for Regulation (EC) No 1257/1999 (second indent of point 9. B.3. V. B of Annex II to Commission Regulation (EC) No 445/2002), Member States must give specific information on amendments to the lists of the less-favoured areas adopted or amended by Council and Commission Directives, and the lists of the areas with environmental restrictions with the necessary justification. Under this procedure the Commission checks every amendment. For the new Member States the initial classification of LFAs will form part of the approval of their rural development programmes.

29. The classification of the LFAs must be seen in the light of the particular situation in each Member State. Regulation (EC) No 1257/1999 does not prevent the use of different indicators (with the general criteria listed in the Regulation) by the various Member States. For each Council Directive, the Commission checks the relevance of the indicators used by the Member States under Article 19.

33. Directive 75/268/EEC and now Regulation (EC) No 1257/1999 set down the common characteristics of the different types of mountain and less-favoured areas. In its Explanatory Memorandum to the Council ⁽¹⁾ the Commission indicated the type and/or quantitative level of the indices to allow the most accurate judgement of the various Member State proposals made at the time, having regard to the Directive. In the course of its contacts with the Member States, the Commission strove to convince them of the need to make the definitions listed in the characteristics concise and harmonised. The indications given in the paper quoted have been used in all subsequent discussions of LFA classification with the Member States. Since 1999 there have been few amendments to the less-favoured areas, but, while there is no formal approval, the Commission checks each proposal notified to verify its conformity with the Directive previously approved for the Member State in question.

34. Because of the varying demographic situations in the Member States, the density of population indicator may be used differently by each provided it remains within the scope of the Regulation. This means that this comparison among the Member States is of only limited usefulness in judging whether the measure is being applied correctly.

35. Under the legislation referred to above, each Member State has a free choice in deciding the importance it wishes to attach to the LFA measure among all the rural development measures and what compensatory allowance is needed to offset local handicaps within its borders.

36. The differences noted in this 1997 text reflect the priorities accorded by Member States to this measure, the financial resources mobilised, the farm structures in Member States and the systems and levels of aid used rather than the range of indicators employed for the classification of areas.

- (a) It should also be noted that the average size of holdings varies considerably from one Member State to another (the document mentioned quotes EUR 111 per hectare for Luxembourg and EUR 52 per hectare for Portugal).
- (b) In Italy the lack of national part-financing means that not all of the beneficiaries in an LFA receive the allowance.

37. See reply to point 36.

The status of LFAs must be considered with reference to conditions in a single Member State. The general economic situation may vary considerably from one Member State to another.

Depending on budget allocations and priorities some Member States have succeeded in equalising incomes between less-favoured areas and others have not.

38. National evaluations have been made for each Member State concerned. The measures for the previous programming period (including those for the LFAs) were subject to a mid-term review and *ex post* evaluation. A general summary will be available before the end of 2003. The evaluation requirements for all measures in the current programming period have been stepped up.

Pursuant to Regulation (EC) No 1257/1999, the Member States quantified the objectives for measures in their rural development programmes, which also contain justifications for differences in the rates of compensatory allowance used by each Member State.

The monitoring and annual reports (see reply to point 62) measure, *inter alia*, the progress made in implementing the programmes against the quantified objectives.

40. Several elements in Regulation (EC) No 1257/1999 minimise the risk of overcompensation. A Member State's total funding for its rural development programme is fixed for the programming period and this has to be allocated across all such

⁽¹⁾ COM (74) 222 final, of 18 December 1974.

measures which it wishes to apply. The Regulation also puts a ceiling of EUR 200/ha on the compensatory amount. If this limit is exceeded, the Commission requires supplementary information. Under the procedure for approving the RDPs, the Commission examines the system and level of aid proposed. Because of the decentralised way in which the measure operates, the Member States are best placed to prevent risks of overcompensation.

41. Article 37(4) of Regulation (EC) No 1257/1999 allows the Member States to lay down further or more restrictive conditions for granting Community support for rural development. These conditions may not have the aim of disadvantaging certain farmers as compared with others.

42. See replies to points 40 and 41.

The Commission notes that the Member States differentiate allowances as permitted by Article 15(2) of Regulation (EC) No 1257/1999.

THE IMPLEMENTATION, MONITORING AND EVALUATION OF MEASURES IN SUPPORT OF LESS-FAVoured AREAS

44. Expenditure is correct and eligible for the following reasons:

- (a) under Regulation (EC) No 1257/1999, good farming practice (GFP) may reflect only the Community and national legislation in force (minimum requirement);
- (b) minimum and maximum stocking densities are normally part of good farming practice to avoid under- or over-grazing;
- (c) the exclusion of pig and poultry farming is justified by the fact that the criterion used seeks to ensure good management of the grass areas which are the virtually exclusive use of these areas, seeking to avoid over-grazing or under-utilisation in systems which are too extensive. Intensive stock-raising is to be found mainly outside less-favoured areas and is in any case subject to the legislation on nitrates and the disposal of effluent;
- (d) the Commission has noted the Court's comment and will consider this point in future audits.

45. A definition of GFP exists in every rural development programme. Under Agenda 2000, it was deliberate policy to define GFP at the level of each Member State or region in order to deal with actual local conditions. In view of the very different environmental situations from region to region, a common code of GFP defined at Community level is not appropriate.

When approving the RDPs containing a definition of GFP, the Commission also insisted on clear indications on how the respect of GFP is checked and verified by the national and regional authorities, via verifiable standards to be included in the programme.

The Commission is aware of the complexity of the concept of good farming practice, which relies on complex rules in the various sectors.

Accordingly, a practical approach was proposed to the Member States in a guidance document in 2000. The Commission considered that there was an objective basis for assessing the eligibility of the aid which had two parts: the definition of a 'reasonable series of essential practices' to be checked during on-the-spot inspections of beneficiaries and a system of cross-notification among the specialist expert departments and those inspecting aid financed by the EAGGF.

46. As a minimum, all codes of GFP as defined in the rural development programmes respect Community legislation, which already provides a certain base level.

Following its experiences of the definition and implementation of GFP in the first years of the programming period, the Commission has now proposed drawing up a Community framework for the statutory standards to be applied in farming as part of the CAP reform.

47. The effective implementation of the systems for management, inspection and penalisation by the Member States is assessed as part of the audits carried out by the Commission.

48. (a) In the case of France, the keeping of registers on treatments and the spreading of waste applies as regards agri-environmental measures under the PDRN (national rural development plan), but it is not a priority under the criteria selected by France for its LFAs.

(d) A requirement to register all poultry, pigs and equines would be a major complication. It would not be useful in practice as those animals are less present in LFAs and do not use forage areas.

50. The Commission is already aware that a number of improvements are needed in the Member States. The Commission has noted the Court's findings and will follow them up in its future audits.

(f) Austria has a sophisticated inspection system which is, however, new and will be improved with a supplementary system of cross-checks.

52. As stated under point 45, practical guidelines on how to inspect rural development measures (including those for LFAs) have been worked out with the Member States. As experience on the ground increases, these guidelines will be further adapted.

The Commission is well aware that an increase in the number and complexity of requirements increases the risk of error.

53. The Commission had in fact identified some of these potential weaknesses during an enquiry carried out from September 2000 to June 2001 prior to the introduction of a new system. At that time, the actual introduction of the systems of management, inspection and penalisation was not audited because these systems were being developed.

54. The variety of local situations makes it inappropriate to lay down common characteristics at Community level as regards good farming practice. However, these practices should be verifiable, as provided for in Regulation (EC) No 445/2002. The Commission has proposed a way of doing this (see reply to point 45) and will ensure that such checks are made in the course of future audits.

56. (a), (b) and (c). The fact that some payments due for 2001 were paid in 2002 is not contrary to the specific regulations, as the Court notes under point 57, and Member States were under no legal obligation to pay these aids in 2001.

(c) In 2001 Austria presented a programme modification in which the financing for the LFAs measure was reduced. As the figures in the changed financial tables correspond with the actual sums spent, there are no consequences for the EU budget.

57. The fact that these cases do not constitute irregularities in the context of the specific regulations shows that the rules applied to EAGGF Guarantee Section have been correctly applied.

60. The Commission's monitoring system concerns both financial and physical aspects (Article 48 of Regulation (EC) No 1257/1999). The framework drawn up by the Commission together with the Member States was designed to cover all rural development measures in a single system and so is not specific to the LFAs measure.

(a) The purpose of the annual report is to follow the physical and financial implementation of programmes (which are based on a calendar year) against objectives. While annual reports can contribute to budgetary control, this is not their key purpose.

Monitoring on a calendar-year basis ensures a coherent approach for programming financed by both the Guidance and Guarantee Sections of the EAGGF. The issue has not proved problematical until now. If in the future it does, the Commission will examine it further.

For programming financed by the EAGGF Guarantee Section, Member States are also required to submit each September separate financial reporting based on the EAGGF budget year (Article 47 of Regulation (EC) No 445/2002).

(b) The separate financial reporting under Article 47 of Regulation (EC) No 445/2002 already provides measure-level information on expenditure actually incurred (payments).

In the case of the LFAs measure, there is in practice little difference between commitments and payments, as payments are made annually and normally declared to the Commission in the same financial year. The Commission considers that it is more appropriate for monitoring purposes to use commitment data as this gives a clearer picture of the extent to which the various measures are being taken up on the ground.

61. The Commission shares certain concerns of the Court regarding the timing, quantity and quality of annual reports and the associated monitoring indicators provided by Member States.

At the time of the audit the only reports available were for 2000. This was the first year of reporting and in many cases an atypical year where programme approval was still in progress and/or where implementation of measures on the ground was only just beginning.

62. The quotation is taken from the explanatory guidelines for the common monitoring indicators for rural development. It assessed the completeness and quality of the common monitoring indicators agreed at Community level (as opposed to annual reports, which include also programme-specific text and in some cases additional programme-specific indicators) supplied for 2000. This critical assessment concerned whether the Commission could fulfil its obligations to produce regular Community-level synthesis reports, as requested by the European Council at the Gothenburg Summit in June 2001.

While there is still further scope for improvement, the Commission considers the quantity and quality of monitoring indicators since provided for 2001 a considerable improvement on those supplied for 2000.

63. For 2000 and 2001, written comments have been sent to Member States and regions to clarify or request further information on certain aspects.

With regard to 2001, the first Community-level synthesis report is now under preparation. It was not possible to produce it by the end of 2002 due to the late submission and, in certain cases, incompleteness of the data from Member States. The analysis is now underway as regards 2001 monitoring data for RDPs (Guarantee Section) and will, subject to receipt of revised data requested from Member States, be completed for 2000. This matter has been discussed with Member States in the context of the Special Committee on Agriculture.

64. Regulation (EC) No 1257/1999 introduced a whole new system of evaluation (*ex ante*, mid-term, *ex post*) and a new common methodology which is a clear improvement on evaluations in the previous period.

68. *Ex ante* rural development evaluation has only been made obligatory for the 2000 to 2006 programming period. No experiences of systematic *ex ante* evaluations in this area existed before. However, the evaluation guidelines issued by the Commission provide for a revision of the *ex ante* evaluation and, where needed, its supplementing in the context of the mid-term evaluation.

69. Up to the end of 2002, the Commission had received from Member States a total of 17 *ex post* evaluations reports for Regulation (EC) No 950/97.

Most of these reports were assessed by the geographical units responsible. The quality assessments serve as a tool for the four European-level *ex post* summary evaluations of the 1994 to 1999 programming period, which are currently being carried out.

The Commission is continuing to take steps to improve the quality of Member States' evaluation reports using guidelines, seminars and coordination meetings.

71. Member States should draw conclusions from the evaluation reports. The Commission uses the same reports to examine critically the national programming documents under the following programming period.

73. The Commission's European-level mid-term evaluation of Objective 5(a) measures suffered from a lack of systematic and comprehensive data. Not all Member States had submitted evaluation reports, and common evaluation questions had not yet been developed. For the new programming period new evaluation guidelines have been set in cooperation with Member States, including a set of common evaluation questions with related criteria and precise indicators.

As to the lack of clear strategy, in the 1994 to 1999 programming period, measures under Regulation (EC) No 950/97, other than those in regions eligible under Objectives 1 and 6, were subject to financial programming only. In the new period 2000 to 2006 the measure is included in the overall strategy of each rural development programme.

74. The results were one of the inputs for the new programming period. Based on the experience gained the system of compensatory allowances was modified with payments solely on a per hectare basis and the requirement to observe GFP.

CONCLUSIONS AND RECOMMENDATIONS

75. The evaluation of the results of the current programmes will provide information on the need for a review of the classification criteria.

The monitoring and evaluation system put in place has improved the availability of relevant information.

With the EAGGF Guarantee Section inspection system and the guidelines for the Member States on the inspection control of rural development measures, including less-favoured areas, the necessary framework was put in place in July 2002 to provide assurance of legality and correctness of expenditure.

The new evaluation system introduced by Regulation (EC) No 1257/1999 will provide the information required for a possible review of the designation criteria and of other elements of the Regulation.

76. The current classification complies with Regulation (EC) No 1257/1999. The classification of less-favoured areas should be considered in the light of the particular situation in each Member State. Regulation (EC) No 1257/1999 does not prevent the use of different indicators.

77. (a) The Commission will consider whether the present system should be changed for the period after 2006.

(b) See replies to points 75 and 76.

78. Evaluations of Member States' programmes of the previous programming period, including the LFAs measure, are available and are being examined, in order to produce an overall analysis before the end of 2003. The evaluation system for rural development for the current programming period will provide more detailed information on all measures, including the LFAs measure, than was available for the previous period.

79. (a) See reply to 78.

- (b) The LFAs measure uses a flat-rate approach. The system itself already contains built-in safeguards (see reply III(c)). When looking at the evaluations of the rural development programmes the Commission will consider whether they are sufficient.

80. Guidelines on the inspection of GFP were issued in 2002. In view of the relative novelty of GFP as an instrument, a certain learning process is inevitable.

The procedures adopted by Member States in declaring expenditure complied with existing EAGGF Guarantee Section requirements.

81. (a) When approving the rural development plans containing the definition of GFP, the Commission also insisted on clear indications on how compliance is monitored and verified by the national and regional authorities via the verifiable standards to be included in the programme.
- (b) A further step in CAP reform proposes the use of GFP as an instrument by providing a Community framework for the base level of statutory standards it is to respect.
- (c) Practical guidelines on how to inspect rural development measures (including those for less-favoured areas) have

been worked out with the Member States. These guidelines will evolve as more experience on the ground is gained.

- (d) The Member States' inspection systems will continue to be audited. The audit service of DG Agriculture works on a multi-annual plan based on risk analysis, as demanded by the Court. It takes into account the remarks of the Court when developing its audit programme.

- (e) See paragraph 80.

82. The monitoring system for rural development was new for the Member States. Monitoring performance has improved and will continue to improve as the Member States gain experience. A first report by the Commission on the implementation of the rural development programmes in the first two years of the programming period is under preparation and a computer system (CAP-IDIM) for the collection and processing of monitoring data will become operational in 2003.

83. (a) The Regulation clearly states which monitoring and evaluation data the Member States have to send to the Commission and when. The Commission reminds them regularly of this requirement.
- (b) Some of the monitoring indicators may need to be adjusted as more experience is gained in their application.
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