Reports of Cases

JUDGMENT OF THE GENERAL COURT (Third Chamber)

19 September 2012*

(ERDF — Reduction of financial assistance — Operational programme falling within Objective 1 (1994-1999), concerning the Land Thüringen (Germany))

In Case T-265/08,

Federal Republic of Germany, represented by M. Lumma, T. Henze, C. Blaschke and K. Petersen, acting as Agents, assisted by U. Karpenstein, lawyer,

applicant,

supported by

Kingdom of Spain, represented initially by J.M. Rodríguez Cárcamo, subsequently by N. Díaz Abad and J.M. Rodríguez Cárcamo, and finally by A. Rubio González, acting as Agents,

by

French Republic, represented by G. de Bergues and N. Rouam, acting as Agents,

and by

Kingdom of the Netherlands, represented by C. Wissels, Y. de Vries, B. Koopman, M. Bulterman and J. Langer, acting as Agents,

interveners,

v

European Commission, represented by A. Steiblyté and B. Conte, acting as Agents,

defendant,

ACTION FOR ANNULMENT of Commission Decision C(2008) 1690 final of 30 April 2008 reducing the financial assistance granted from the European Regional Development Fund (ERDF) to the Operational Programme in the Objective 1 area of *Land* Thüringen (Germany) (1994-1999), in accordance with Commission Decision C(94)1939/5 of 5 August 1994,

THE GENERAL COURT (Third Chamber),

composed of O. Czúcz, President, I. Labucka (Rapporteur) and D. Gratsias, Judges,

* Language of the case: German.

Registrar: T. Weiler, Administrator,

having regard to the written procedure and further to the hearing on 27 September 2011,

gives the following

Judgment

Backround to the dispute

1 On 3 September 1993, the German Government applied to the Commission of the European Communities for Community financial assistance in financing the Operational Programme in the Objective 1 area of the *Land* of Thüringen (1994-1999), providing support for productive investments by small and medium-sized enterprises (SMEs).

2 On 29 July 1994, the Commission adopted Decision 94/628/EC on the establishment of the Community support framework for Community structural assistance in the German regions concerned by Objective 1, which are Mecklenburg-Vorpommern, Brandenburg, Sachsen-Anhalt, Sachsen, Thüringen and Berlin (East) (OJ 1994 L 250, p. 18). That decision made it possible to set up the operational programme in the new *Länder*.

3 By Decision C(94) 1939/5 of 5 August 1994, the Commission approved the operational programme for *Land* Thüringen falling under Objective 1 in Germany (Arinco No 94.DE.16.005) ('the assistance in question') providing for a structural funds contribution of ECU 1 021 771 000, increased to EUR 1 086 827 000 by Decision C(99) 5087 of 29 December 1999, with co-financing by the European Regional Development Fund (ERDF) of a maximum amount of EUR 1 020 719 000. The Ministry of Economy and Transport of the *Land* of Thüringen was designated as the managing authority.

4 In relation to measure 2.1 concerning support for productive activities of SMEs, Decision C (99) 5087 fixed the total amount of expenditure at EUR 674 104 000 and the ERDF contribution at EUR 337 052 000.

5 In the course of 2001, the Commission systematically examined *Land* Thüringen's management and control systems, on the basis of Article 23(2) of Council Regulation (EEC) No 4253/88 of 19 December 1988, laying down provisions for implementing Regulation (EEC) No 2052/88 as regards coordination of the activities of the different Structural Funds between themselves and with the operations of the European Investment Bank and the other existing financial instruments (OJ 1988 L 374, p. 1), and on the basis of Article 14 of Commission Regulation (EC) No 2064/97 of 15 October 1997 establishing detailed arrangements for the implementation of Regulation No 4253/88 as regards the financial control by Member States of operations co-financed by the Structural Funds (OJ 1997 L 290, p. 1).

6 On 30 January 2002, the Commission submitted its final report on the operational programmes of the *Länder* of Thüringen and Sachsen-Anhalt, with recommendations.

7 On 24 June 2002, the statement provided for under Article 8 of Regulation No 2064/97 was drawn up by a firm of auditors and sent to the Commission.

8 By letter of 18 July 2002, the German authorities submitted their request for final payment concerning the assistance in question. On 27 June 2003, the Commission wound up the assistance in question and made the final payment at the level of the amount requested.

9 After the assistance was wound up, inter alia from 27 to 31 October, from 10 to 21 November, from 1 to 5 December and on 11 December 2003, the Court of Auditors of the European Communities carried out a number of audit visits. In the course of 2004, it undertook the analysis of the weaknesses of the intervention in question, in the context of the examination of the 2003 statement of assurance. 28 measure 2.1 projects were examined.

10 On 22 June 2004, the Court of Auditors sent its provisional audit report to the German authorities. By letters of 31 August and 13 October 2004, the German authorities sent the Court of Auditors additional information.

11 By letter of 17 January 2005, the Court of Auditors sent its audit report ('the audit report of 17 January 2005') to the national authorities. The report referred to specific cases of irregularities and systemic irregularities, such as the financing of undertakings which do not fall within the definition of SMEs, the declaration of ineligible expenditure (future leases, VAT, rebates), errors in the calculation of the maximum assistance and the lack of supporting evidence for certain types of expenditure such as general expenses or own funds. The report concluded that there were shortcomings in the management and control systems in relation to the assistance in question. The error rate of the 28 measure 2.1 projects was 31.36%.

12 By letter of 19 October 2006, the Commission sent the German authorities the first results of its examination of the audit report of 17 January 2005, requesting comments by those authorities.

13 On the basis of the analysis of the weaknesses carried out by the Court of Auditors, the Commission informed *Land* Thüringen of financial corrections amounting to EUR 135 million. Following bilateral discussions with that *Land*, certain objections were however withdrawn.

14 By letter of 5 January 2007, the German authorities replied to the Commission's letter of 19 October 2006, objecting to the application of extrapolated financial corrections while providing additional supporting documents to show the eligibility of certain expenditure.

15 By decision C(2008) 1690 final of 30 April 2008 ('the contested decision'), the Commission reduced by EUR 81 425 825.67 the ERDF financial contribution to the assistance in question because of the specific and systemic irregularities determined in the context of the 2.1 measure, applying Article 24 of Regulation No 4253/88. The Commission carried out an extrapolation of the error rate with regard to measure 2.1 as a whole, taking an error rate of 23.88% as the basis. It calculated a sum of EUR 1 232 012.70 in relation to specific irregularities and EUR 80 193 812.97 with regard to systemic irregularities.

16 According to the contested decision, the systemic errors found to exist were as follows:

— funding of a non-SME company (Maxit Baustoffwerke GmbH, arcon II Flachglasveredelung, Gothaer Fahrzeugwerk and CeWe Color AG projects);

— final recipient not having satisfied the national criteria applicable to SMEs for 15% additional funding (Tralag Landmaschinen GmbH project);

— ineligible expenditure declared in connection with leasing contracts (TelePassport Service GmbH and Schuster Kunststofftechnik GmbH projects).

Procedure and forms of order sought by the parties

17 By application lodged at the Registry of the Court on 4 July 2008, the Federal Republic of Germany brought the present action.

18 The Federal Republic of Germany claims that the Court should:

— annul the contested decision;

— order the Commission to pay the costs.

19 The Kingdom of Spain, the French Republic and the Kingdom of the Netherlands were given leave to intervene in the present proceedings in support of the form of order sought by the Federal Republic of Germany and were permitted to submit their observations at the oral procedure in accordance with Article 116(6) of the Rules of Procedure of the Court.

20 The Commission contends that the Court should:

— dismiss the action;

— order the Federal Republic of Germany to pay the costs.

21 Upon hearing the report of the Judge-Rapporteur, the Court (Third Chamber) decided to open the oral procedure.

22 By letter lodged at the Registry of the Court on 6 September 2011, the Federal Republic of Germany made certain observations on the report for the hearing concerning the status of the Commission's internal guidelines of 15 October 1997 concerning the net financial corrections in the context of the application of Article 24 of Regulation No 4253/88 ('the internal guidelines') and the interpretation to give to certain aspects of the audit report of 17 January 2005.

23 The oral arguments of the parties and their replies to the questions posed by the Court were heard at the hearing which took place on 27 September 2011.

Law

24 In support of its action, the Federal Republic of Germany relies on five pleas in law alleging, respectively, with regard to the first and the second pleas, infringement of Article 24(2) of Regulation No 4253/88, with regard to the third plea, the absence of on-the-spot audit by the Commission, with regard to the fourth plea, infringement of the principles of the protection of legitimate expectations, legal certainty and cooperation and, with regard to the fifth plea, infringement of the principle of proportionality.

1. *The first plea in law, alleging infringement of Article 24(2) of Regulation No 4253/88 because the required conditions for a reduction are not satisfied*

The first branch of the first plea, alleging that administrative errors attributable to the national authorities cannot be classified as irregularities within the meaning of Article 24(2) of Regulation No 4253/88

Arguments of the parties

25 The Federal Republic of Germany maintains that the objections made by the Commission, assuming them to be substantively correct, cannot be classified as irregularities, because they are only simple administrative errors, not falling within the scope of Article 24(2) of Regulation No 4253/88, unless they significantly change the operation or measure in question and that change is not communicated to the Commission.

26 The Federal Republic of Germany submits that, under Article 1(2) of Council Regulation (EC, Euratom) No 2988/95 of 18 December 1995 on the protection of the European Communities' financial interests (OJ 1995 L 312, p. 1), an irregularity is any infringement of a provision of Community law resulting from an act or omission by an economic operator. It notes that, in the Dutch language version, there is a requirement that the economic operator must have been at fault. The Federal Republic of Germany considers that that definition is applicable to all the sectoral regulations, including Regulation No 4253/88, in the light of the fact that the same term, that is 'irregularity', is used, in each of the language versions, in Article 24(2) of Regulation No 4253/88 and Article 1(2) of Regulation No 2988/95. According to it, to interpret the concept of irregularity differently in the two regulations would be to disregard the principle of the uniformity of Community law.

27 In addition, the Commission's position that the concept of irregularity must be interpreted differently in Regulation No 2988/95 and Regulation No 4253/88 does not appear in the contested decision, which states in paragraphs 26 and 27 that the irregularities arise from the actions or omissions of the final beneficiaries.

28 The Federal Republic of Germany considers that, in the light of Regulation No 2988/95 and Article 23(1) of Regulation No 4253/88, public authorities cannot be treated in the same way as economic operators, which are public or private undertakings competing for goods or services. Thus, the Commission's objections amount only to pure administrative errors such as the formal recording of non-SMEs under priority 2.1 of the operational programme of *Land* Thüringen, or the grant of allegedly excessive State aid to two economic operators in the context of a hire purchase arrangement, the aid being granted pursuant to specific administrative acts based on provisions of an administrative nature.

29 The Federal Republic of Germany adds that it follows from the statement in the Council of the European Union minutes and from footnote 10 to the Commission's practical guidelines of 11 April 2002 on the obligation to communicate irregularities that the acts and omissions of State authorities cannot constitute irregularities because they cannot be imputed to economic operators.

30 The Federal Republic of Germany also disputes the relevance of the reference in paragraph 28 of the contested decision to the judgment of the Court in Case C-199/03 *Ireland* v *Commission* [2005] ECR I-8027, because the existence of the irregularities committed by economic operators was not contested by the Irish Government.

31 According to the Federal Republic of Germany, the parallel drawn by the Commission in paragraphs 25 and 28 of the contested decision with the legal basis of the European Agricultural Guidance and Guarantee Fund (EAGGF) is not any more relevant since, with regard to the EAGGF, the right to carry out financial corrections on account of administrative errors or weaknesses in the management or control systems is expressly recognised by the Community legislature, whereas for the ERDF a significant change to the operational programme is required. The only legal basis authorising the reduction of the Community assistance carried out in the present case by the Commission is Council Regulation (EC) No 1260/1999 of 21 June 1999 laying down general provisions on the Structural Funds (OJ 1999 L 161, p. 1) which is valid only in relation to subsequent financial periods.

32 The Federal Republic of Germany refuses, in the light of the principle of limited competence, derived from Article 5 EC, to accept that the case-law regarding the application of Article 8 of Council Regulation (EEC) No 729/70 of 21 April 1970 on the financing of the common agricultural policy (OJ, English Special Edition 1970 (I), p. 218) can be relied upon in order to justify powers of recovery under Regulation No 4253/88.

33 The Federal Republic of Germany also claims that there is no provision of Community law which authorises the Commission to carry out financial corrections on the ground of purely national administrative errors, because Article 1(1) of Regulation No 2988/95 expressly requires an infringement of Community law. The general principle of cooperation in good faith, based on Article 10 EC, cannot justify a derogation from that fundamental division of competences, but is based on the institutional and procedural autonomy of the Member States.

34 The Commission disputes those arguments.

Findings of the Court

35 Article 24(2) of Regulation No 4253/88 authorises the Commission to reduce or suspend assistance for an intervention if the examination carried out under Article 24(1) confirms an irregularity. However, that article does not state who is responsible for an irregularity committed when the operation or measure financed by the funds is implemented.

36 With regard to the argument of the Federal Republic of Germany which draws a parallel between Article 24(2) of Regulation No 4253/88 and Article 1(2) of Regulation No 2988/95 to the effect that an irregularity is exclusively an infringement of a provision of European Union law resulting from an act or omission of an economic operator, those provisions must be interpreted in an autonomous manner, because they pursue different objectives and their scope is not the same. In essence, Regulation No 2988/95 puts in place a general legal framework intended to combat fraud which, by definition, cannot be committed by a national authority, whereas Regulation No 4253/88 concerns the relationship between the European Union and the Member States (see, by analogy, judgment of 22 November 2006 in Case T-282/04 *Italy* v *Commission*, not published in the ECR, paragraph 83).

37 It must also be noted that it is the responsibility of the national authorities to ensure correct use of Community funds, and it is they which must in accordance with national provisions laid down by law, regulation or administrative action, take the measures necessary inter alia to satisfy themselves that the transactions financed by the fund are actually carried out and are executed correctly. The Commission exercises only a supplementary function (see, by analogy, Case C-366/88 *France* v *Commission* [1990] ECR I-3571, paragraphs 19 and 20).

38 It is also agreed that Article 24 of Regulation No 4253/88 does not make any distinction of a quantitative or qualitative nature concerning the irregularities which may give rise to reductions in assistance. The Court has held that even irregularities which do not have a specific financial impact

may be seriously prejudicial to the financial interests of the European Union and to compliance with Community law and for that reason justify the application of financial corrections by the Commission (*Ireland* v *Commission*, paragraph 29 et seq.).

39 An administrative error linked to differences between the amounts laid down in the financing plan and those in the application for payment may for example constitute an irregularity justifying a reduction in assistance (Case T-74/07 *Germany* v *Commission* [2009] ECR II-107, paragraph 34 et seq.).

40 Furthermore, the fact that the national authorities have a central role to play in the implementation of the structural funds supports a broad interpretation of the concept of 'irregularity'. An error committed by those authorities must be considered to be an 'irregularity' within the meaning of Article 24(2) of Regulation No 4253/88 in the light of the principles of sound financial management, referred to in Article 274 EC and of cooperation in good faith, referred to in Article 10 EC, which do not authorise immunity for the Member States, and taking into account the fact that Article 24 of Regulation No 4253/88 is the only provision which allows the amount of assistance to be reduced where the intervention did not take place as originally envisaged (Case C-500/99 P *Conserve Italia* v *Commission* [2002] ECR I-867, paragraph 88).

41 Finally, regarding the argument of the Federal Republic of Germany alleging that there is no provision of European Union law which authorises the Commission to make financial corrections in respect of purely national administrative errors in the context of the Community system of subsidies, it should be noted that the recipient must comply with a series of obligations the definition and review of which fall, to a large extent, to the national authorities. Any other interpretation would be difficult to reconcile with the principles of sound financial management and cooperation in good faith. In addition, even if the Commission criticises the Federal Republic of Germany for national administrative errors, they concern the grant of European Union financial assistance.

42 Consequently, it must be held that an interpretation of Article 24(2) of Regulation No 4253/88 which excludes from the concept of 'irregularity' errors committed by national authorities would undermine the effectiveness of the rule laid down by that provision.

43 Thus, it follows from the above that infringements of European Union law attributable to national administrative authorities fall under Article 24(2) of Regulation No 4253/88. Given that the national authorities have a central role to play in the implementation of the structural funds, an infringement committed by those authorities must be considered as an 'irregularity' within the meaning of Article 24(2) of Regulation No 4253/88.

44 This branch of the first plea in law must therefore be rejected.

The second branch of the first plea in law, submitted in the alternative, contesting the existence of the irregularities found to exist by the Commission in the contested decision

45 In essence, the Federal Republic of Germany submits that the competent authorities did not commit any irregularities and that the Commission's objection with regard to the effectiveness of the systems of management and control is unfounded.

Classification errors by the Commission concerning the ineligibility of expenditure concerning projects relating to non-SMEs

– Arguments of the parties

46 The Federal Republic of Germany maintains that no relevant administrative error has been made given that, first, it was possible to fund and record the projects according to the same criteria as under priority 1.1 of the operational programme and, second, the Community budget was not prejudiced, whereas that is a requirement under Article 23(1) of Regulation No 4253/88.

47 The Federal Republic of Germany takes the view that the recording and management of the financial assistance for non-SMEs under priority 2.1 did not lead, even potentially, to undue expenditure. The Federal Republic of Germany considers that the five undertakings referred to in priority 2.1 satisfied the condition of cross-regional turnover required under priority 1.1, providing expressly that productive investment could be given 'independently of the size of the business'. In that context, the Court of Auditors' criticism concerned not illegal financial assistance for certain undertakings but only the recording of the aid under the operational programme.

48 The Commission contests those arguments.

– Findings of the Court

49 The objections made by the Federal Republic of Germany to the contested decision concern a number of projects.

50 With regard to the Tralag Landmaschinen project, as stated in point 46 of the table annexed to the contested decision, it is not the definition of SME contained in the Community support framework established by Decision 94/628 which was infringed, but the definition contained in the 24th joint framework programme for the 'improvement of regional economic structures' for the period 1995-1999, adopted by the planning committee of the Bundestag (Federal Parliament, Germany) on 27 April 1995, which must be complied with in the light of the principle of cooperation in good faith which appears in Article 10 EC. That provision provides for additional funding of 15% for undertakings which do not employ more than 250 persons, which is not the case for Tralag Landmaschinen, which however received such funding. Thus, that undertaking was not eligible for 15% additional funding.

51 With regard to the project concerning the latter and the four other projects concerning Maxit Baustoffwerke GmbH, arcon II Flachglasveredelung, Gothaer Fahrzeugwerk and CeWe Color AG, it should be recalled that, as is apparent from the second paragraph of Article 52(5) of Regulation No 1260/1999, applications for final payment in respect of project assistance for the 1994-1999 period had to be submitted to the Commission by 31 March 2003 at the latest, with no possibility to change them subsequently. The five projects at issue were recorded under measure 2.1. As stated in paragraph 8 above, the application for final payment was submitted to the Commission on 18 July 2002 and honoured by the latter on 27 June 2003, so that the German authorities cannot reasonably claim that the abovementioned projects were eligible under measure 1.1. In those circumstances, the erroneous recording constitutes a declaration of ineligible expenditure under measure 2.1 of the intervention in question, which cannot be amended after 31 March 2003.

52 As has already been held by the Court, the existence of those irregularities is sufficient for the imposition of a financial correction, without specific financial damage to the Community budget being required (see, to that effect, *Ireland* v *Commission*, paragraphs 25 to 27, 31, 58 and 59).

53 Finally, the Court of Auditors did not limit itself to criticism of the financing of non-SMEs, in the context of measure 2.1, but held that the transactions in question were 100% ineligible for Community assistance.

54 This argument of the applicant must therefore be rejected.

Distinction between hire purchase and leasing and the inapplicability of the datasheets and of international accounting standard 17

– Arguments of the parties

55 Concerning the No 38 TelePassport Service GmbH and No 44 Schuster Kunststofftechnik GmbH transactions, the expenditure for which was considered ineligible, the Federal Republic of Germany contests the distinction made by the Commission between hire purchase and leasing, on the one hand, and the applicability of datasheet No 20 annexed to Commission Decision 97/321/EC of 23 April 1997 modifying the decisions approving the Community support frameworks, the single programming documents and the Community initiative programmes in respect of Germany (OJ 1997 L 146, p. 9) ('datasheet No 20') and international accounting standard 17, on the other hand.

56 The Federal Republic of Germany asserts that hire purchase is not a 'specific type of leasing' as the Commission would have it. The essential purpose of the hire purchase contract is the acquisition of an economic asset which takes effect, from an accounting point of view, when the contract is concluded. The purpose of leasing, on the other hand, is limited merely to making an asset available for use, the rent being the remuneration for making the asset available. Thus, to restrict Community financial assistance to 60 hire purchase instalments is unjustified. Moreover, the price calculated for the hire purchase does not correspond to the making available for use, but to an instalment of the purchase price, meaning that the Commission's approach would lead to not differentiating according to whether the lender is a bank or the seller of a machine.

57 The Commission contests those arguments, insisting that the Community law terms receive an autonomous interpretation and on the fact that the acquisition of assets by hire purchase cannot be considered as a contract of sale, taking into account the fact that the final beneficiaries only acquired full ownership of the assets at the end of the 60 month period, having paid all the instalments, which in relation to the projects concerned occurred only after the winding-up of the Community intervention.

– Findings of the Court

58 It is settled case-law that the terms used in a provision of European Union law which make no express reference to the law of the Member States must, for the purpose of determining the meaning and scope of that provision, be given an autonomous and uniform interpretation, taking into account the context of the provision and the purpose of the legislation in question (Case C-287/98 *Linster* [2000] ECR I-6917, paragraph 43, and Case 327/82 *Ekro* [1984] ECR 107, paragraph 11). In addition, as correctly noted by the Commission, the fact that its Decision 97/231 concerning the eligibility of the expenditure is addressed to the Federal Republic of Germany does not justify the lack of an autonomous and uniform interpretation of its terms, given that that decision is part of a series of 15 similar decisions addressed on the same day to the then 15 Member States and which were published simultaneously.

59 With regard to the essence of the Federal Republic of Germany's argument, the purchase of property by hire purchase cannot be considered as a fully eligible contract of sale because the final beneficiaries did not pay the full purchase price during the eligibility period. Thus, the final beneficiaries did not

acquire full ownership of the assets until the end of the 60-month period, having made all the payments, which in relation to the projects concerned occurred only after the Community assistance was wound up.

60 With regard to international accounting standard 17, the reference made to that standard in recital 30 in the preamble to the contested decision is not in any respect conclusive, in so far as the contested decision refers to it in a subsidiary fashion, as a generally accepted accounting standard, in order to interpret the term 'finance-lease'.

61 Finally, with regard to the applicability of the datasheets which entered into force on 1 May 1997 (to the extent that the provisions of those datasheets, annexed to Decision 97/321, impose new or increased burdens on the Member States or on the recipients), it must be noted that the concept of ineligibility was not introduced by that decision and that the datasheets annexed to that decision merely codify existing practice, by setting out in relation to leasing expenditure the pre-existing rule whereby future expenditure is not eligible. Thus, there can be no question of applying datasheet No 20 retrospectively.

62 This argument of the Federal Republic of Germany must therefore be rejected.

The Commission's allegedly incorrect classification of some irregularities as systemic

– Arguments of the parties

63 The Federal Republic of Germany maintains that the Commission proceeds upon the wrong assumption that the Court of Auditors categorised assistance for non-SMEs pursuant to priority 2.1 of the operational programme as a systemic error. In that regard, it criticises the Commission for having extrapolated the error rate of 23.88% in relation to all the expenditure pursuant to priority 2.1 of the operational programme on account of the systemic nature of the errors, whereas the Court of Auditors did not object to any of the five abovementioned projects on the ground that they contained such errors. In the absence of that material error, the basis for the calculation would have been entirely different. It also cannot be inferred from the contested decision that the Commission departed from the Court of Auditors' assessment, as it alleges.

64 The Commission disputes those arguments.

– Findings of the Court

65 With regard to the alleged contradiction between the contested decision and the Court of Auditors' findings, it is not apparent from the wording of Article 24 of Regulation No 4253/88 that, when exercising its powers under that article, the Commission is bound by the observations of that review body. On the contrary, it is for the Commission to give its own evaluation of the irregularities found to exist. Thus, the contested decision reflects the Commission's assessment and not that of the Court of Auditors.

66 Furthermore, the erroneous recording with regard to non-SMEs is systemic in character in so far as it reflects insufficient management, control or audit, shortcomings which occurred a number of times and which can probably be found in a series of similar cases. The Commission was therefore correct in categorising such erroneous recording in relation to non-SMEs as systemic irregularities.

67 Consequently, this argument of the Federal Republic of Germany must be rejected.

The allegedly incorrect classification by the Commission of the 5% controls as insufficient and the conclusion that the management and control systems contained weaknesses

– Arguments of the parties

68 The Federal Republic of Germany contests the Commission's objection that there were insufficiencies in the implementation of the 5% controls, in accordance with Regulation No 2064/97, and considers that it is unable to justify the finding that there is an irregularity.

69 First, the Federal Republic of Germany claims that it is apparent from the final external statement issued under Article 8 of Regulation No 2064/97 that the '5% controls' were in essence reliable and met the requirements of Article 3 of that regulation. Neither the Court of Auditors nor the external accounting experts complained that the authorities of the *Land* Thüringen failed to comply with the conditions laid down by the Commission for its control of the system.

70 Second, the Federal Republic of Germany contests the Commission's criticism that the 'checklists' used for the 5% controls did not incorporate the guidelines contained in the datasheets. It considers that the guidelines, even if not explicitly contained in the checklists, are of course and indisputably an integral part of the 5% controls.

71 Third, the Federal Republic of Germany considers that the Commission's approach is contradictory because it did not make that complaint either in the 'Ventura' protocol of 23 July 1998 or in the Commission report of 30 January 2002.

72 Fourth, the Federal Republic of Germany points out that the simple fact that the 5% controls showed a lower error rate than the Court of Auditors' investigations does not in itself call into question the competent authorities' systems of management and control. The difference results from the fact that the Court of Auditors carried out an analysis of the obvious weaknesses in the systems of management and control, whereas the 5% controls were based on random checks, as required by the regulation. While the sample control is representative, the weaknesses analysis carried out by the Court of Auditors aims to identify risks.

73 The Commission disputes those arguments by stating that no financial correction was applied in response to weaknesses in the systems of management and control found by the Court of Auditors.

– Findings of the Court

74 It is apparent from the contested decision that the reference to weaknesses, found by the Court of Auditors, in the systems of management and control of the assistance in question, relied upon by the Commission on the basis of recital 11 in the preamble to the abovementioned decision, does not constitute an autonomous ground for reduction of the financial assistance. The reduction of the financial assistance, in the contested decision, was based on the correction of specific irregularities and on an extrapolated financial correction for systemic irregularities. No financial correction was applied in response to weaknesses in the systems of management and control found by the Court of Auditors. The present argument is therefore misplaced.

75 Accordingly, the first plea in law must be rejected in its entirety.

2. *The second plea in law, alleging infringement of Article 24(2) of Regulation No 4253/88 owing to the calculation of the amount of the reduction by extrapolation*

The first branch of the second plea, alleging the unlawfulness of the extrapolation method for calculation of the amount of the reduction pursuant to Article 24(2) of Regulation No 4253/88

No right of extrapolation on the basis of Article 24 of Regulation No 4253/88

– Arguments of the parties

76 The Federal Republic of Germany claims that pursuant to Article 24(2) of Regulation No 4253/88, which must be read in the light of its heading, the Commission may only reduce, suspend or cancel the operation or measure concerned. Article 24(1) refers to a specific case and Article 24(3) to repayment of the sum unduly paid. It follows from this that a financial correction is expressly limited to the amounts which have clearly been unduly paid.

77 It adds that Regulation No 4253/88 is to be distinguished from the clearance of EAGGF accounts under Regulation No 729/70, Article 5(2)(c) of which expressly authorises the Commission to take into account in the calculation of the financial correction the degree of the discrepancies found, the nature and gravity of the infringement and the financial loss suffered by the European Community.

78 The Federal Republic of Germany considers, in essence, that before the publication of Regulation No 1260/1999, valid for the 2000-2006 financing period, there was no detailed legal framework clearly defining the reciprocal rights and obligations, with the result that it is questionable whether extrapolated financial corrections are permitted. Regulation No 2064/97 does not constitute a legal basis and moreover does not provide for an extrapolation procedure in order to carry out financial corrections.

79 The Federal Republic of Germany adds that the fact that it is often impossible to put a precise figure on systemic irregularities does not authorise the Commission to have recourse to extrapolation on the basis of Regulation No 4253/88.

80 The Kingdom of Spain accepts that, according to the case-law, the Commission enjoys a certain amount of discretion with regard to Article 24(2) of Regulation No 4253/88. However, the use of an extrapolation method results in the reduction of the assistance granted to a project on the basis of a presumption and not on the basis of an examination. Not only is such a possibility not provided for by the article in question; it runs counter to its spirit and purpose. Contrary to the Commission's assertion, the Court, in Case C-443/97 *Spain* v *Commission* [2000] ECR I-2415, did not vindicate the application of the extrapolation method. Furthermore, the Kingdom of Spain notes that extrapolation requires a finding of systemic irregularities on the basis of a representative sample, which is not the case here.

81 The Kingdom of the Netherlands also maintains that Article 24 of Regulation No 4253/88 does not contain any legal basis for extrapolation and points out that it does not see how the principles of sound financial management and the duty to cooperate in good faith, on which the Commission relies, could lead to a broad interpretation of the aforesaid article. Moreover, the Commission may not arrogate to itself new powers pursuant to internal guidelines which cannot constitute a basis for extrapolation. It is not the Commission which determines the extent of its rights and powers; that is the remit of the European legislature. No different conclusion can be drawn from the judgment in *Spain* v *Commission*. Finally, extrapolation must maintain procedural guarantees, since the legislation in force at the relevant time did not contain any rule of law in that regard.

82 The French Republic considers, first, that in respect of the 1994-1999 funding period, the Commission was not entitled, in the absence of a legal basis, to apply any financial correction. It is apparent from the very wording of Article 24 of Regulation No 4253/88 that it may make financial corrections only in respect of specific cases. That is what distinguishes the rules applicable to financial corrections in the ERDF for the 1994-1999 funding period from those applicable to the clearance of accounts under the EAGGF-Guarantee. In that regard, the French Government notes that, in the context of the EAGGF-Guarantee, the Court accepted application of the extrapolation method (Case C-118/99 *France* v *Commission* [2002] ECR I-747 and Case C-344/01 *Germany* v *Commission* [2004] ECR I-2081). Thus, according to the case-law, the application of the extrapolation method is not in principle prohibited. By contrast, Article 24 of Regulation No 4253/88 provides expressly that the Commission is authorised only to apply specific financial corrections in relation to the irregularity established. Only by virtue of Regulation No 1260/1999 would the Commission be authorised to apply extrapolated corrections. It follows, according to the French Republic, from the foregoing that the application of the extrapolation method is prohibited in principle by Regulation No 4253/88.

83 Second, the French Republic considers that the Commission may not apply financial corrections by extrapolation in the context of Regulation No 4253/88, where, first, that regulation does not provide the conditions for the implementation of the extrapolation method and, second, that regulation does not lay down a framework of strict procedural guarantees for that method. Thus, the Commission may apply corrections by extrapolation only where it uses a random sample representative of transactions with homogeneous characteristics. The conditions and guarantees must be provided for pursuant to a binding act and it is not sufficient for them to be provided for by mere Commission guidelines, and the Commission may not rely upon them in order to justify access to the extrapolation method. As the Court held in *Spain* v *Commission*, those internal guidelines do not have legal effects and are not binding. Consequently, they may not serve as a legal basis for extrapolation.

84 The Commission disputes those arguments.

– Findings of the Court

85 According to the wording of Article 24(2) of Regulation No 4253/88, the Commission may reduce the assistance for the operation or measure concerned where it establishes, following the hearing of those concerned provided for under Article 24(1), an irregularity, and in particular a significant change affecting the nature or conditions of the operation or measure. Article 24(2) of Regulation No 4253/88 does not make any distinction of a quantitative or qualitative nature in relation to the irregularities which can give rise to such a reduction of assistance.

86 That provision therefore confers a power of reduction and substantial discretion on the Commission, without mentioning any limits regarding the choice of methods which the Commission may use in order to establish the amount of the reduction.

87 It must therefore be examined whether use of the extrapolation method can be justified in the present case.

88 First, the question whether Article 24(2) of Regulation No 4253/88 authorises the Commission to carry out financial corrections using that method depends on the interpretation of the wording ‘reveals an irregularity’ contained in that provision.

89 When exercising the power to impose financial corrections, the method used by the Commission to determine the amount to be repaid must be in conformity with the objective pursued by Article 24(2) of Regulation No 4253/88.

90 That objective is to allow a financial correction to be made where the expenditure in respect of which funding has been requested was not in conformity with the rules of European Union law. In the light of that objective, Article 24(2) of Regulation No 4253/88 must be interpreted in a manner which enables the Commission to reduce the assistance appropriately.

91 More specifically, as the Commission correctly states in recital 25 in the preamble to the contested decision, the amount of the correction depends on the financial loss sustained by the budget of the European Union, ascertained by the audit. That loss must be corrected in its entirety since any failure of implementation would constitute an infringement of the principle of sound financial management, to which the Commission and the Member States must adhere under Article 274 EC. Thus, the Commission must be able to reduce the assistance to an extent which reflects the dimension of the irregularity which it established after the hearing of those concerned under Article 24(1) of Regulation No 4253/88.

92 In addition, according to settled case-law, the Commission may not limit itself to presuming that the irregularities in question exist but must prove to the requisite legal standard that those irregularities were not limited to the specific cases examined by it. Thus, in order to show that the irregularities are not limited to the specific cases which it examined, it is sufficient for it to adduce evidence which gives rise to a serious and reasonable doubt as to the lawfulness of the entirety of the checks carried out by the Member State concerned. It is not obliged to demonstrate exhaustively that all the checks are inadequate (see, by analogy, Case C-334/01 *Germany* v *Commission*, paragraph 58).

93 That lightening of the burden of proof can be explained by the fact that the rules in Regulation No 4253/88 do not provide for systematic checking by the Commission, which in any case it could not in practical terms carry out, since it is not close enough to the economic agents to obtain the information it needs from them.

94 Where the Commission has adduced sufficient evidence to give rise to a serious and reasonable doubt concerning all the national checks, it is for the Member State concerned to show that the Commission's claims are inaccurate by adducing more detailed evidence regarding the actual nature of its checks. Should the Member State fail to adduce such evidence, the Commission will establish that the irregularities were not limited to the specific cases examined by it.

95 The reduction decision must reflect that systemic dimension of the irregularities. Furthermore, the Commission lacks the information regarding the entirety of the controls carried out by the Member State concerned. In such a case, use of the extrapolation method is the most appropriate method by which to guarantee the objectives pursued by Article 24(2) of Regulation No 4253/88. Once the systemic nature of the irregularities has been established, the reduction of the assistance does not therefore rest on a mere presumption by the Commission but on a proven fact.

96 The Commission nevertheless remains subject to the obligation to comply with the rules of European Union law resulting inter alia from the principle of proportionality. The question whether it has observed that principle by adopting the contested decision will be examined below in the context of the fifth plea in law.

97 It must therefore be held that Article 24(2) of Regulation No 4253/88 does not prohibit the Commission from using the extrapolation method in order to establish a financial correction.

98 In addition, while Regulation No 2064/97 does not provide for the extrapolation of financial corrections, that can be explained by the fact that that regulation is an implementing regulation based on the fourth subparagraph of Article 23(1) of Regulation No 4253/88, laying down the minimum requirements to be satisfied by the financial control systems put in place by the Member States in relation to measures co-financed by the structural funds.

99 This argument of the Federal Republic of Germany must therefore be rejected.

No right to extrapolation based on internal guidelines

– Arguments of the parties

100 The Federal Republic of Germany also takes the view that the Commission may not have recourse to extrapolation based on its internal guidelines, in particular owing to the fact that they have only internal effects and no legal effects vis-à-vis third parties.

101 Equally, the content of those guidelines was not accepted by the Member States, which repeatedly opposed them. The Commission may not rely upon a text not approved by them.

102 Finally, contrary to what is stated in paragraph 25 of the contested decision, the Federal Republic of Germany argues that the conditions and the maximum amount of the flat-rate corrections or of the extrapolations are not laid down, and no other calculation method is mentioned.

103 The Commission contests those arguments.

– Findings of the Court

104 First, it must be noted that the contested decision is based on Article 24 of Regulation No 4253/88. Second, it is not apparent from the contested decision that the Commission employed the internal guidelines as a legal basis for that decision.

105 In any event, the Court already examined the effect of the internal guidelines in *Spain* v *Commission*. The Kingdom of Spain had requested the annulment of the internal guidelines, considering that they imposed upon the Member States the threat of new pecuniary sanctions and that the Commission did not have the power to adopt such a measure.

106 The Commission had raised an objection of inadmissibility, maintaining that the internal guidelines did not impose any additional obligations on the Member States compared to those already provided for under Article 24 of Regulation No 4253/88, that they did not affect their pre-existing legal situation or produce legal effects.

107 Under Article 24(2) of Regulation No 4253/88, the Commission has the power to reduce or suspend the assistance. The Court notes that there is nothing to prevent the Commission from adopting internal guidelines concerning the financial corrections in the context of the application of Article 24 of Regulation No 4253/88 or from instructing the services concerned to apply them. The internal guidelines thus indicate the general lines along which, pursuant to Article 24 of Regulation No 4253/88, the Commission envisages subsequently adopting individual decisions whose legality may be challenged before the European Union judicature by the Member State concerned. According to the case-law, such an act of the Commission, which reflects only its intention to follow a particular line of conduct in the exercise of the power granted to it by Article 24 of Regulation No 4253/88, cannot therefore be regarded as intended to produce legal effects (Case 114/86 *United Kingdom* v *Commission* [1988] ECR 5289, paragraph 13, and Case C-180/96 *United Kingdom* v *Commission* [1998] ECR I-2265, paragraph 28).

108 Such guidelines merely express the Commission's intention to follow a particular line of conduct in the exercise of the power granted to it by Article 24 of Regulation No 4253/88.

109 That reasoning leads the Court to hold that the internal guidelines cannot be regarded as a measure intended to produce legal effects, with the result that the action for annulment by the Kingdom of Spain must be dismissed as inadmissible.

110 Thus, in holding the action inadmissible on the abovementioned grounds, the Court drew a distinction between the internal guidelines and the individual decisions adopted on the basis thereof.

111 It follows from the case-law referred to above that the Commission was entitled to refer to the internal guidelines in order to reinforce the transparency of the individual decisions addressed to the Member States. Moreover, as was noted in paragraph 104 above, Article 24 of Regulation No 4253/88 is the only legal basis given by the Commission to the contested decision.

112 This argument of the Federal Republic of Germany must therefore be rejected as misplaced.

113 The first branch of the second plea in law must therefore be rejected in its entirety.

The second branch of the second plea in law alleging, in the alternative, that the Commission should not have carried out an extrapolation in the present case

Arguments of the parties

114 The Federal Republic of Germany maintains that the extrapolation is based on a non-representative sample. More precisely, it considers that nothing in the contested decision shows that the checks by the Court of Auditors on which the Commission bases its extrapolations were obtained in the course of a representative sampling control procedure, a procedure which the Court of Auditors is not bound to follow. Whereas the statistical sampling procedure is designed to achieve an overall assessment on the basis of standard representative cases, the analysis of weaknesses entails a preliminary choice of the control topics and the objectives pursued. The Commission thereby follows an approach which is contrary to that which it laid down for itself in point 6 of its internal guidelines, and in paragraph 11 of the contested decision.

115 Concerning the parallel drawn by the Commission with the EAGGF-Guarantee, the Federal Republic of Germany points out that the guidelines applicable in that sector allow an extrapolation of a maximum of 10% only in the case of the risk of a very high and generalised loss. However, in the present case, the rate is 23.88% and no argument is made that such a risk exists.

116 The Commission disputes those arguments.

Findings of the Court

117 According to the file, in order to establish the sample on the basis of which it carried out its checks, the Court of Auditors proceeded in conformity with the Statement of Assurance 2003 control plan and with its own internal guidelines, by selecting 30 transactions, 28 of which fall within measure 2.1, the scale of the sample being selected on the basis of the type of the fund.

118 It follows that the controls carried out by the Court of Auditors are appropriate, objective and representative and that the Court of Auditors worked on the basis of a method of representative sampling, meaning that the Commission was entitled to carry out an extrapolation.

119 In addition, the EAGGF-Guarantee guidelines do not apply in the present case, all the more because the rates stated by the Federal Republic of Germany apply to flat-rate corrections, and not to extrapolations. The aim of extrapolation is, however, to avoid flat-rate corrections in favour of extrapolation of the error rate in a representative sample to the entire population on the basis of which the sample was constituted.

120 The second branch of the second plea in law must therefore be rejected, as must the second plea in law in its entirety.

3. *The third plea in law, alleging the lack of on-the-spot checks by the Commission before the reduction*

Arguments of the parties

121 According to the Federal Republic of Germany, the fact that the Commission bases itself on the analysis of the weaknesses is a significant procedural error, infringing Article 23(2) of Regulation No 4253/88, a binding rule of procedure which requires an on-the-spot and sample check of the actions financed by the structural funds. An analysis of weaknesses by the Court of Auditors cannot replace a control procedure by representative sampling carried out by the Commission's services.

122 The Commission contests those arguments.

Findings of the Court

123 With regard to the criticism expressed by the Federal Republic of Germany concerning the absence of checks carried out by the Commission itself, it should be recalled that Article 24(1) of Regulation No 4253/88 provides that, if an operation or measure appears to justify only part of the assistance allocated 'the Commission shall conduct a suitable examination'.

124 Nonetheless, to infer from that wording an obligation on the Commission to carry out the required controls exclusively by itself would be too strict an interpretation which, resulting in a splitting of the controls and thus causing loss of Community resources, would be contrary to the principle of sound administration.

125 Furthermore, it is common ground that the Commission, when exercising its task of supervising the use of Community funds, may use diverse sources of information. The Court has already acknowledged that recourse only to evidence gathered by the national authorities was sufficient. Thus, as was held in Case T-199/99 *Sgaravatti Mediterranea* v *Commission* [2002] ECR II-3731, paragraph 45, when the national authorities have carried out an in-depth check of whether a recipient of Community assistance has complied with its financial obligations, the Commission may legitimately rely on their detailed findings of facts and determine whether those findings serve to establish the existence of irregularities justifying penalties pursuant to Article 24(2) of Regulation No 4253/88, as amended. That case-law was confirmed in the judgment of 17 December 2008 in Case T-154/06 *Italy* v *Commission*, not published in the ECR, paragraph 42.

126 By contrast, it is essential to ensure that the Member States are not prejudiced, in a procedural or substantive sense, by the choice of the control method or of the persons who carry them out. It is thus necessary to establish whether the procedural guarantees and the effects in practice of the controls carried out by the Court of Auditors and by the Commission are equivalent.

127 With regard to the procedural guarantees, it should be noted that the two types of checks – carried out by the Commission and by the Court of Auditors – are comparable. In both cases, the rights of the defence must be observed, high-level audit standards are applied, the Member State must be informed

before an on-the-spot inspection takes place, the officials of the national authorities may participate in the check and the Member State concerned must be asked to submit its observations on the results of the check.

128 By contrast, the foreseeable effects of those checks in practice are not comparable, given that the Court of Auditors' report is not binding and the financial corrections cannot be imposed directly on the basis thereof.

129 The Court of Auditors and the Commission have distinct roles in the Community's budgetary procedure. According to Article 246 EC, the Court of Auditors is to carry out the audit. Under Article 248(1) EC, it is to examine all revenue and expenditure of the Community and to provide the European Parliament and the Council with a statement of assurance as to the reliability, legality and regularity of the underlying transactions. Accordingly, the Court of Auditors must in particular check how the Commission manages the resources of the Community funds. The Court of Auditors establishes what the situation is and also formulates recommendations in order to optimise management of the financial resources. It is also the Commission's task to recover resources where irregularities have been found in the implementation of projects.

130 Accordingly, from a systemic perspective, the two institutions do not share the same role or task and the Commission may not automatically adopt the Court of Auditors' findings.

131 As a general rule, it follows that the control required by Article 24(1) of Regulation No 4253/88 need not necessarily be carried out by officials or agents of the Commission. The Commission is however obliged, first, to ensure that the corrections made by it on the basis of checks carried out by a third party are not automatic, but based on the analysis, in partnership with the Member State concerned, of the data and of the results of the checks and, second, to adopt its own decision on the basis of those checks and subsequent consultations.

132 It must therefore be examined whether, during the administrative procedure, in partnership with the national authorities, the Commission gave the Member State concerned the genuine possibility of commenting on the Court of Auditors' findings and on the corrections the Commission intended to impose on the basis of those findings.

133 According to the contested decision, following on from the audit, the Commission services, in accordance with Article 24(1) of Regulation No 4253/88, examined the reasons for the Court of Auditors' findings and requested the German authorities to provide them with information and additional evidence. The Commission services sent the results of that assessment to the German authorities by letter of 19 October 2006. The German authorities responded by letter of 5 January 2007, objecting to the application of extrapolated financial corrections in the context of the operational programmes for the period 1994-1999. By letter of 23 April 2007, the Commission invited the German authorities to a bilateral meeting which took place on 8 May 2007 in Brussels. The hearing on the application of a corrected financial extrapolation did not enable an agreement to be reached. However, the German authorities undertook to provide, within two weeks of the meeting, other conclusive proof that certain expenditure and actions were eligible. That information was passed to the Commission by letter of 22 June 2007.

134 Thus, the Commission afforded the Federal Republic of Germany a sufficient possibility of commenting on the Court of Auditors' findings and carried out a suitable examination of the case in the framework of the partnership, within the meaning of Article 24(1) of Regulation No 4253/88, reducing in particular the financial corrections initially foreseen (see paragraph 13 above).

135 Following that procedure, the Commission then in fact adopted the results of the Court of Auditors' controls and compliance with the procedural guarantees of the Member State was, in any event, ensured.

136 Accordingly, this plea in law must be rejected.

4. *The fourth plea in law, alleging infringement of the principles of the protection of legitimate expectations, legal certainty and cooperation in the light of the lack of any objections by the Commission to the wrongful recording of non-SMEs*

Arguments of the parties

137 The Federal Republic of Germany considers that the Commission did not raise any objection, whether in its decision of 5 August 1994, that of 10 October 1996 or that of 20 December 1999, regarding the recording of undertakings employing more than 500 employees as SMEs, giving the German authorities legitimately to understand that the Commission had no objection in that regard. That being so, the Commission was in part responsible for the points it criticises. For the Commission to impose an extrapolation based on the existence of systemic weaknesses, constituted by the erroneous recording of financial assistance to SMEs, without taking its own responsibility into account, clearly infringes the principles of legal certainty and the duty to cooperate in good faith.

138 It considers that the Commission's omission is all the more significant in that in 1997 and 1999 the Commission received annual reports on the evaluation of ERDF assistance, which included recording of undertakings employing 500 or more employees under the SME measure, without any criticism thereof being made. Nor is any objection made in the 2002 final report on that point.

139 The Commission disputes those arguments.

Findings of the Court

140 As was noted in the examination of the previous pleas in law (see paragraphs 37 and 39 above), the Member States are primarily responsible for ensuring the proper implementation of the transactions financed by the ERDF.

141 In addition, Regulation No 4253/88 does not provide for any rule of procedure making the Commission's right to reduce or suspend the assistance conditional upon having raised doubts concerning the sound administration of the project before the winding-up of the intervention, as is apparent from paragraph 79 of the judgment of 8 July 2008 in Case T-176/06 *Sviluppo Italia Basilicata* v *Commission*, not published in the ECR.

142 Furthermore, it must be reiterated that the right to rely on legitimate expectations requires three conditions to be satisfied. First, precise, unconditional and consistent assurances originating from authorised and reliable sources must have been given to the person concerned by the European Union authorities. Second, those assurances must be such as to give rise to a legitimate expectation on the part of the person to whom they are addressed. Third, the assurances given must comply with the applicable rules (see Case T-347/03 *Branco* v *Commission* [2005] ECR II-2555, paragraph 102 and the case-law cited, and Case T-282/02 *Cementbouw Handel & Industrie* v *Commission* [2006] ECR II-319, paragraph 77).

143 It must be held that the Federal Republic of Germany has not proved that the Commission gave it an assurance that undertakings employing 500 or more employees would be considered to be SMEs and could as a result benefit from financial assistance. Consequently, the principle of legal certainty was not infringed.

144 In addition, it is settled case-law that the toleration of former irregularities does not give rise to any right, based on the principle of legal certainty or the principle of the protection of legitimate expectations, for the Member State to demand that the same position be taken in relation to current irregularities (*Ireland* v *Commission*, paragraph 68).

145 The fourth plea in law must therefore be rejected.

5. *The fifth plea in law, alleging infringement of the principle of proportionality owing to the excessive reduction of the assistance by the Commission*

Arguments of the parties

146 The Federal Republic of Germany argues that the Commission infringed the general principle of proportionality, having carried out an excessive reduction, based on an extrapolation applicable to the whole of the funding period. The errors found by the Court of Auditors cannot, according to it, justify the general complaint of malfunctioning of the systems of management and control of the *Land* Thüringen in the years 1994 to 1999. That finding is inconsistent with the findings of the Commission in 1998 and 2002 and with the final opinion of a firm of auditors, to which the Commission made no objection. The final payment of 23 June 2003 was made precisely because the Commission failed to raise any substantive objections to the system of management and control.

147 In addition, even if leasing and hire purchase were treated alike, it claims that the Commission made leasing subject to restrictions only from 1 May 1997.

148 Concerning Tralag Landmaschinen GmbH, the Federal Republic of Germany considers that an extrapolation is also not acceptable, since that undertaking received an additional 15% assistance under the 24th Framework Plan, although that plan was applied only from 17 March 1995.

149 The Commission contests those arguments.

Findings of the Court

150 Regarding the argument according to which, before adoption of the contested decision, the Commission failed to raise any substantive objections to the system of management and control, that argument concerns, in reality, the principle of the protection of legitimate expectations. According to settled case-law, the right to claim protection of legitimate expectations requires three conditions to be satisfied. First, precise, unconditional and consistent assurances originating from authorised and reliable sources must have been given to the person concerned by the European Union authorities. Second, those assurances must be such as to give rise to a legitimate expectation on the part of the person to whom they are addressed. Third, the assurances given must comply with the applicable rules (*Branco* v *Commission*, paragraph 102 and the case-law cited, and *Cementbouw Handel & Industrie* v *Commission* , paragraph 77).

151 It is not apparent from the case-file or from the applicant's arguments that it received that type of precise, unconditional or consistent assurance from the Commission. That argument must therefore be rejected.

152 With regard to the principle of proportionality, it requires that the European Union institutions do not exceed what is appropriate and necessary to achieve the intended purpose. In particular, the infringement of obligations observance of which is of fundamental importance to the proper

functioning of a Community system may be penalised by forfeiture of a right conferred by European Union legislation, such as entitlement to financial assistance (*Sgaravatti Mediterranea* v *Commission*, paragraphs 134 and 135).

153 In that regard, according to settled case-law concerning EAGGF matters, which is applicable *mutatis mutandis* in the present case, the Commission may even refuse to charge to the fund the whole of the expenditure in question if it finds that there are no adequate control procedures (Case C-263/98 *Belgium* v *Commission* [2001] ECR I-6063, paragraph 125). The Commission, must, however observe the principle of proportionality which requires that measures adopted by Community institutions are not to exceed what is appropriate and necessary to attain the objective pursued (Case 15/83 *Denkavit Nederland* [1984] ECR 2171, paragraph 25). If, then, in its function of clearing the accounts the Commission, instead of refusing the entire expenditure, endeavours to draw up rules to differentiate according to the degree of risk posed by different levels of defective supervision, the Member State must show that those criteria are arbitrary and unfair (Case C-50/94 *Greece* v *Commission* [2006] ECR I-3331, paragraph 28).

154 The Commission was therefore not precluded from imposing financial corrections.

155 In addition, the Commission stated by means of paragraph 6 of its internal guidelines that, where it provides for an extrapolation it must take into account the specific nature of the administrative structure responsible for the weakness, the probable extent of the abuses, their frequency and effects.

156 As already previously found (see paragraph 85 above), the Commission enjoys a certain degree of discretion conferred upon it by Article 24(2) of Regulation No 4253/88 which enables it to take decisions capable of ensuring that the principle of sound financial management stated in Article 274 EC and the principle of proportionality are observed.

157 As also stated above, the Commission analysed the results of the checks carried out by the Court of Auditors and in fact reduced the amount of the corrections initially envisaged.

158 In the present case, a large part of the irregularities found following consultation of the German authorities, such as the erroneous recording of non-SMEs or the inadmissible nature of the expenditure declared in connection with leasing contracts, reveals a systemic deficiency in management, control or audit concerning measure 2.1 during the whole 1994-1999 period of funding. It is also highly probable that that deficiency can be found in a series of similar cases. The Commission was therefore correct to apply the extrapolation method, in particular taking into account the importance given to the sound functioning of the national administration which, in the first instance, is responsible for ensuring the proper implementation of the projects financed by the funds (see paragraphs 37 and 39 above) and which, as noted at a number of points in Regulation No 4253/88, is supposed to work in partnership with the Commission.

159 Accordingly, the fifth plea in law must be rejected and the action as a whole dismissed.

Costs

160 Under Article 87(2) of the Rules of Procedure, the unsuccessful party is to be ordered to pay the costs if they have been applied for in the successful party's pleadings.

161 Since the Federal Republic of Germany has been completely unsuccessful, it must be ordered to pay the costs, as applied for by the Commission in its pleadings.

162 In accordance with Article 87(4) of the Rules of Procedure, the interveners are to bear their own costs.

On those grounds,

THE GENERAL COURT (Third Chamber)

hereby:

1. Dismisses the action;

2. Orders the Federal Republic of Germany to bear its own costs and to pay those incurred by the European Commission;

3. Orders the Kingdom of Spain, the French Republic and the Kingdom of the Netherlands to bear their own costs.

Czúcz Labucka Gratsias

Delivered in open court in Luxembourg on 19 September 2012.

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