



EUROPEAN COURT OF AUDITORS

Special Report No 6

2013

HAVE THE MEMBER STATES AND THE
COMMISSION ACHIEVED VALUE FOR MONEY WITH
THE MEASURES FOR DIVERSIFYING THE RURAL
ECONOMY?



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

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Special Report No 6 // 2013

More information on the European Union is available
on the Internet (<http://europa.eu>).

Cataloguing data can be found at the end of this publication.
Luxembourg: Publications Office of the European Union, 2013

ISBN 978-92-9241-292-0
doi:10.2865/88553

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Printed in Luxembourg

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REPLY OF THE COMMISSION

GLOSSARY

Axes: Rural development in the 2007–13 programming period is implemented under three thematic axes, which represent coherent groups of rural development measures, and one horizontal axis dedicated to the Leader approach (Leader axis).

CMEF: Common Monitoring and Evaluation Framework.

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

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

Displacement: The degree to which an activity promoted by public support is offset by reductions in activity elsewhere.

EAFRD: European Agricultural Fund for Rural Development.

FTE: Full-time Equivalent, a unit used to measure employed persons in a way that makes them comparable although they may work a different number of hours per week. The unit is obtained by comparing an employee's average number of hours worked to the average number of hours of a full-time worker.

GVA: Gross value added.

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

Measure 311: The measure for 'diversification into non-agricultural activities'.

Measure 312: The measure for 'business creation and development intended for microenterprises'.

Measure 313: The measure for 'encouragement of tourism activities'.

MTE: Mid-term evaluation report.

NSP: The National Strategy Plan is a document prepared by a Member State which shall ensure that Community aid for rural development is consistent with the Community strategic guidelines and that Community, national and regional priorities all coordinate. The national strategy plan shall be a reference tool for preparing EAFRD programming. It shall be implemented through the rural development programmes.

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

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

EXECUTIVE SUMMARY

I.

The EU rural development policy intends to address rural problems such as depopulation, scarcity of economic opportunities and unemployment. It provides funding in order to support growth, employment and sustainable development in rural areas.

II.

One of the three thematic axes of EU rural development policy aims to improve the quality of life in rural areas and diversify the rural economy; it is known as axis 3. Under this axis, three specific measures are intended to diversify the rural economy:

- diversification into non-agricultural activities ([measure 311](#));
- support for the creation and development of micro-enterprises with a view to promoting entrepreneurship and developing the economic fabric ([measure 312](#)); and
- encouragement of tourism activities ([measure 313](#)).

III.

The EU budget for these measures amounts to 5 billion euro for the period 2007–13. This EU funding is supplemented by a further 2 billion euro programmed to come from national funds.

IV.

The Court's audit examined whether the Commission and the Member States achieved value for money with the measures for diversifying the rural economy. In particular, the Court assessed whether these three measures were designed and implemented in such a way as to make an effective contribution to growth and jobs and whether the most effective and efficient projects were chosen for financing. Furthermore, the Court assessed whether the available monitoring and evaluation information provided reliable, complete and timely information on the outcomes of the measures.

V.

The Court concludes that overall the Commission and the Member States have, only to a limited extent, achieved value for money through the measures for diversifying the rural economy, as the aid was not systematically directed to the projects that were most likely to achieve the purpose of the measures. This was due to a lack of clear needs for intervention or specific objectives set in the RDPs, broad eligibility criteria adopted that did not limit the projects to those most likely to achieve diversification and selection criteria that did not choose the most effective projects or were not applied at all. Too often, and particularly at the start of the programming period, the selection of projects was driven more by a need to spend the allocated budget than by the quality of the projects themselves. In some Member States, all eligible projects were funded where sufficient budget was available regardless of how the project was assessed.

VI.

Member States did not sufficiently mitigate the risks of deadweight and displacement, thus they did not ensure the most efficient use of resources. Member States checks on reasonableness of costs did not sufficiently reduce the risk of inflated costs and there were examples of an excessive administrative burden on applicants and delays in payments.

VII.

There was a lack of effective monitoring and evaluation of the measures so that there is a real risk that the results of the funding allocated to the projects will not be known. The EU's strategic priority of job creation was not well targeted and there was a lack of active management when it was apparent that the targets set would not be met.

EXECUTIVE SUMMARY

VIII.

The Court therefore recommends that:

- In their rural development programmes (RDPs), Member States should clearly identify how and why public intervention for investments in non-agricultural activities will help to redress for example market failures related to barriers to employment and growth. The Member States should then set specific and measurable objectives in relation to these needs. The Commission should approve only those RDPs that present substantiated and comprehensive strategies with a clear rationale that show how policy intervention will contribute to strategic aims of creating growth conditions and employment opportunities.
- Member States should establish and consistently apply criteria to ensure the selection of the most effective, sustainable projects with respect to the Member States' specific objectives. The Commission should ensure that these criteria are correctly and continuously applied, not only in cases of budgetary shortage.
- The Commission and Member States should promote the adoption of best practices in respect of mitigating the risks of deadweight and displacement. The Commission should encourage Member States to adopt the practice whereby expenditure for investments would be eligible only as of the date of grant approval.
- The Commission should ensure that Member States have effective systems to carry out checks on reasonableness of costs.
- The Commission and Member States should ensure that for the forthcoming programming period, relevant and reliable information is obtained to facilitate management and monitoring of the measure and to demonstrate the extent to which the aid given is contributing to the achievement of EU priorities. The targets for job creation should be realistic and the numbers of jobs created accurately monitored, the measures should be better managed throughout the programming period and particularly if it becomes apparent that targets set will not be achieved.
- The Commission and Member States should increase their efforts in reducing the administrative burden and ensuring that payments are made in a reasonable timeframe.

INTRODUCTION

1. The EU rural development policy intends to address rural problems such as depopulation, scarcity of economic opportunities and unemployment. It provides funding in order to support growth, employment and sustainable development in rural areas.
2. EU rural development policy for 2007 to 2013 is focused on three themes (known as 'thematic axes'). These are:
 - o Axis 1 — improving the competitiveness of the agricultural and forestry sector;
 - o Axis 2 — improving the environment and the countryside;
 - o Axis 3 — improving the quality of life in rural areas and encouraging the diversification of the rural economy¹.
3. The eight measures under axis 3 are defined as having the following objectives²:

‘To diversify farming activities towards non-agricultural activities, develop non-agricultural activities and promote employment, to improve basic services, including local access to information and communication technologies and carry out investment making rural areas attractive in order to reverse trends towards economic and social decline and depopulation of the countryside [...]’.
4. Part of axis 3, the EU objective of diversifying the rural economy is supported through three specific measures:
 - (i) diversification into non-agricultural activities (**measure 311**);
 - (ii) support for the creation and development of microenterprises with a view to promoting entrepreneurship and developing the economic fabric (**measure 312**); and
 - (iii) encouragement of tourism activities (**measure 313**).

¹ Article 4(c) of Council Regulation (EC) No 1698/2005 of 20 September 2005 on support for rural development by the European Agricultural Fund for Rural Development (EAFRD) (OJ L 277, 21.10.2005, p. 1), which lays down the following overall objective: ‘To improve quality of life in rural areas and encourage the diversification of economic activities’.

² Recital 46 of Regulation (EC) No 1698/2005.

5. The Community strategic guidelines adopted by the Council³ identify the European Union's priorities under the European Agricultural Fund for Rural Development (EAFRD). These guidelines set out what axis 3 spending aims to achieve as follows:

'The resources under axis 3 should contribute to the overarching priority of the creation of employment opportunities and conditions for growth [...]'.

The guidelines set out the strategic approach to be followed by Member States for the preparation of their National Strategy Plan (NSP) and subsequent rural development programmes (RDP) for the period 2007–13. The expected contribution to growth and jobs in rural areas, in line with the Lisbon Strategy, was also reflected in the results indicators of the implementing rules⁴.

6. Diversification measures, as part of the rural development policy, are subject to the shared management system of the Commission and the Member States. RDPs are proposed by the Member States and are approved by the Commission. The Member States then select the projects to which funding is allocated based upon the programmes submitted. **Figure 1** shows how the regulatory framework allocates funding to diversification projects.

³ As required by Article 9 of Regulation (EC) No 1698/2005, the Council Decision 2006/144/EC of 20 February 2006 on Community strategic guidelines for rural development (programming period 2007 to 2013) (OJ L 55, 25.2.2006, p. 20) sets out the priorities for rural development, paragraph 3.3 of the Annex.

⁴ Annex VIII, point III of Commission Regulation (EC) No 1974/2006 of 15 December 2006 laying down detailed rules for the application of Council Regulation (EC) No 1698/2005 on support for rural development by the European Agricultural Fund for Rural Development (EAFRD) (OJ L 368, 23.12.2006, p. 15).

FIGURE 1



- 7.** Planned EU expenditure for these measures was 5 billion euro for the 2007–13 period and 2 billion euro were also earmarked from the Member States' national funds. As the level of demand for certain measures was lower than expected the programmed funding for the measures in some Member States has been reduced by a total of 0,3 billion euro during the course of the programming period (see **Annex I**).
- 8.** The funding is provided in the form of grants to support projects submitted and is therefore in addition to the funding that the beneficiaries themselves contribute. Typical types of projects financed under the axis 3 measures include:
- Under measure 311: service activities (bed and breakfast, agritourism, education and social activities on farm ...), craft activities (pottery, production of local products ...) and trade activities (creation of shops attached to the farm where products⁵ are sold directly to the customer ...).
 - Under measure 312: support for development of existing micro-enterprises or to individuals that will set up a new micro-enterprise (less than 10 workers and less than 2 million euro of turnover) in a non-agricultural business.
 - Under measure 313: construction or renovation of tourism infrastructure, facilities and/or attractions for visitors, facilities for leisure, development and marketing of tourism products, development of tourism marketing strategies, information materials.
- 9.** **Box 1** shows examples of the types of project financed under the three diversification measures that were audited by the Court.
- 10.** The audited projects ranged in total cost from 10 000 euro to 3 million euro, with public aid ranging from 2 500 euro to 1,1 million euro. For these measures, Regulation (EC) No 1698/2005 did not set the maximum eligible amount nor the maximum aid intensity rate allowed. Member States determine the aid rate and the maximum eligible amount in their RDPs in compliance with EU general state aid rules.

⁵ To be eligible under Measure 311, the shop must not sell only its own agricultural produce.

BOX 1

EXAMPLES OF THE TYPES OF INVESTMENT FINANCED BY DIVERSIFICATION MEASURES



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A farm diversified into providing accommodation in Italy (measure 311)



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A flower shop in Sweden (measure 312)



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A wildlife park and cafe in the United Kingdom (measure 313)

AUDIT SCOPE AND APPROACH

11. The Court sought to assess whether the measures audited were designed and implemented in a way that provided value for money, and whether the projects audited which were financed achieved the objectives of the measures. The Court also assessed whether the results of the measures were monitored and evaluated in a way that allowed the Member States and the Commission to identify and react to any problems which may have arisen, and to provide objective information on the outcomes of the measures.

12. The audit focused on answering the following question:

Have the Member States and the Commission achieved value for money with the measures for diversifying the rural economy?

The main sub-questions were:

- Are diversification measures designed and implemented in such a way to make an effective contribution to growth and jobs?
- Were the risks to efficiency and economy sufficiently mitigated?
- Were effective and efficient projects actually funded?

13. The audit covered both the Commission and visits to six Member States (the Czech Republic, France — Aquitaine, Italy — Campania, Poland, Sweden (Västra Götaland) and the United Kingdom — England (Yorkshire and Humber))⁶ and included the design and implementation of the measures, the results obtained by completed projects and the monitoring of the financial support under the diversification measures. This involved the examination of a sample of 129 project files covering the three diversification measures. Site visits were made to 57 of the projects, including an analysis of the underlying documentation and interviews with the aid beneficiaries. 72 project files were checked through a documentary review.

⁶ These Member States were selected to ensure a good geographical coverage and because they had implemented all three diversification measures with a sufficient number of completed projects.

OBSERVATIONS

PART ONE — ARE DIVERSIFICATION MEASURES DESIGNED AND IMPLEMENTED IN SUCH A WAY AS TO MAKE AN EFFECTIVE CONTRIBUTION TO GROWTH AND JOBS?

- 14.** ‘The measures under axis 3 should contribute to the overarching priority of the creation of employment opportunities in rural areas in non-agricultural activities and services. This is a response to the trends in many parts of Europe towards economic and social decline as well as depopulation of the countryside. Diversification is necessary for growth, employment and sustainable development in rural areas, and thereby contributes to a better territorial balance, both in economic and social terms ...’⁷
- 15.** The Member States are required to express their structural and territorial needs in terms of clear and specific objectives⁸ in their RDPs in line with their national strategy plans. They must then implement measures that focus on achieving these objectives.
- 16.** In order for its policies to be both effective and targeted, the Member States need to have an understanding of both the drivers of employment and growth in rural areas and the barriers against them. They must also ensure that the rationale for intervention is clearly justified in terms of how public funding can help for example by redressing market failures. Member States should also specify the outcomes that they plan to achieve (how diversification can/will contribute towards sustainable growth and what changes are to be achieved), thus providing a clear framework and clear guidance for the ongoing management of the programme (e.g. identifying improvements to be made when necessary).
- 17.** The Court reviewed EU legislation and Member State systems, procedures and documents to obtain evidence as to whether the design and implementation of diversification measures was likely to lead to the efficient funding of effective projects that addressed the priority of growth and jobs creation. Specifically, the audit examined whether Member States have a rationale that demonstrates for the measures the need for public intervention, the setting of clear objectives and relevant eligibility criteria together with the establishment of effective selection procedures. Furthermore, the audit assessed the extent to which the Commission and Member States managed the measures taking into account the performance achieved.

⁷ *Handbook on Common Monitoring and Evaluation Framework — Guidance note E — Measure fiches — setting out the rationale of the measures; DG Agriculture 2006.*

⁸ Article 43 of Regulation (EC) No 1974/2006: ‘For investment measures, Member States shall ensure that support is targeted on clearly defined objectives reflecting identified structural and territorial needs and structural disadvantage.’

OBJECTIVES SET WERE BROAD AND WERE NOT ALWAYS RELATED TO CREATING CONDITIONS FOR GROWTH AND EMPLOYMENT OPPORTUNITIES

- 18.** As required by Article 16 of Regulation (EC) No 1698/2005⁹, the audited national/regional RDPs had indeed identified a number of strengths and weaknesses in their rural economies. However, the RDPs and other programming documents did not further analyse the underlying causes of these problems in order to establish how the intervention should be targeted¹⁰ (see **Box 2**).
- 19.** While the RDPs examined had identified some potential benefits that could be achieved by Measures 311, 312 and 313, none of them set out a clear intervention logic along the lines of: *identified needs — specific objectives — activity needed to achieve these objectives*. For example, in Sweden, the RDP listed a number of areas where public intervention may be needed to achieve the diversification of the rural economy and support growth (eliminating obstacles to women's participation, creating credit guarantee associations, etc.) but it did not set specific objectives nor did it identify specific types of activities to be financed to meet those needs.

⁹ 'Each rural development programme shall include: (a) an analysis of the situation in terms of strengths and weaknesses, the strategy chosen to meet them and the *ex ante* evaluation referred to in Article 85'.

¹⁰ Annex II, point A.5.2 to Regulation (EC) No 1974/2006 requires that 'evidence for investment measures support is targeted on clearly defined objectives reflecting identified territorial needs and structural disadvantages'.

BOX 2

EXAMPLE OF A RDP WHERE THE NEED FOR FUNDING DIVERSIFICATION MEASURES IS NOT CLEARLY DEMONSTRATED

United Kingdom — England: According to the RDP, each region should have particular regard to economic underperformance and disadvantages when implementing the measures. The Yorkshire and Humber Regional Implementation Plan gives the justification that the region has a lower proportion of diversified farms than the national average, but it does not show that there is a need for more diversification of the rural economy, whether in terms of farm incomes, farm viability, volatility of revenues, or other factors, nor does it identify why there is less diversification in this region and how public intervention could help.

- 20.** In all the national/regional RDPs audited, with the exception of a particular example in Italy (see paragraph 21) the objectives provided were so general and open-ended that the national/regional authorities were not able to develop measurable targets (see **Box 3**). Therefore, each measure's contribution towards the operational objectives was only quantified in terms of targets for the monitoring indicators set out in the EU's common monitoring and evaluation framework¹¹. However, these 'targets' were established by calculating the expected results based on the volume of planned expenditure rather than first identifying the desired results required to fulfil a need or achieve an objective and subsequently identifying how much of a given target could be met with the available funding.
- 21.** Measure 311 in Italy — Campania was an exception insofar as it established a specific objective 'promoting the full employment of members of the farm household', to which it associated an additional quantified indicator (i.e with a target): 'number of members of the farm household who find employment in the supported activities'.

¹¹ The implementing regulation establishes the following result indicators within the Common Monitoring and Evaluation Framework (CMEF):

- increase in non-agricultural gross value added in supported business (measures: 311, 312, 313);
- gross number of jobs created (division according to on-farm/off-farm jobs, gender and age category) (measures: 311, 312, 313);
- additional number of tourist visits (division according to the number of overnight stays and the number of day visitors) (measure: 313).

BOX 3

EXAMPLE OF TOO BROAD OBJECTIVES SET FOR DIVERSIFICATION MEASURES

In the **Czech Republic**, identical objectives were set for all three measures: 'the diversification of agricultural activities into non-agricultural production, the development of non-agricultural production and support for job creation', 'diversity in the rural economy', 'the improvement of the quality of life in rural areas and economic diversification'. These objectives are taken from recital 46 of the preamble to Regulation (EC) No 1698/2005 without any further specification being added and are general and open-ended. For example, the objective 'diversity of rural economy' does not specify the extent of improvement of the current situation which the measure aims to achieve and can therefore not be translated into a qualitative or quantitative indicator.

In the RDP for **Poland**, the objectives of Measure 313 (tourism) were only broadly stated in the framework of an integrated measure¹² as follows 'The measure will improve the living conditions of rural areas'; 'This will contribute to the development of rural population identity'; 'This will contribute to the (...) preservation of (...) specificity of rural areas ...'. This general formulation does not specify how this measure will contribute towards encouragement of tourism activities.

¹² Measures 313 'Encouragement of tourism activities', 322 'Village renewal and development' and 323 'Conservation and upgrading of the rural heritage' were merged into one measure.

- 22.** The fact that the audited Member States and regions have not specified clearly what they wish to achieve indicates a strategy that is demand led rather than objective driven. As a consequence, many different activities and sectors remain eligible, with the risk that the aid will not be sufficiently targeted to the identified needs and structural disadvantages (the rationale for intervention) which inter alia represent the obstacles to growth and job creation.

THE COMMISSION APPROVED RDPs DESPITE WEAKNESSES

- 23.** Regulation (EC) No 1974/2006 specifies that Member States must identify the rationale for intervention, the objectives, the scope and the actions of the measures. Furthermore the RDPs should provide 'evidence that, for investment measures, support is targeted on clearly defined objectives reflecting identified territorial needs and structural disadvantages'. Therefore, prior to approving the Member States' RDPs, the Commission is required to check the consistency of the RDP objectives with EU and national strategies and with the identified needs and weaknesses.

- 24.** However, as the RDPs which were audited defined objectives in such general terms, the consistency checks that were made could only be of limited usefulness. Nevertheless, the Commission approved RDPs despite these weaknesses and it did not make a critical assessment of the arguments in favour of intervention. It also gave no consideration as to how effectively or efficiently the proposed measures could generate growth and sustainable jobs.

THE ELIGIBILITY CONDITIONS/CRITERIA SET BY THE AUDITED MEMBER STATES DO NOT RESTRICT THE SCOPE OF THE AID FOR DIVERSIFICATION

- 25.** Once the Member States have established their objectives, they must set out the conditions for eligibility — (e.g. the types of investment, the categories of beneficiary and the nature of the support) — so as to ensure that aid is targeted towards achieving the objectives set.

26. These eligibility conditions are intended to restrict the scope of the aid. The Court found that the Member States' eligibility criteria were also very broad so funds were allocated to projects that did not actually address the aims of the specific measures even though they may provide some benefit to the local population (see **Box 4**). The Court even found projects that were not eligible under EU regulations in the Czech Republic and Sweden (see **Annex II**).

¹³ Article 71(2) of Regulation (EC) No 1698/2005 states that: 'Expenditure shall be eligible for EAFRD contribution only where incurred for operations decided on by the Managing Authority of the programme in question or under its responsibility, in accordance with the selection criteria fixed by the competent body.'

SELECTION PROCEDURES DID NOT DIRECT FUNDING TOWARDS THE BEST PROJECTS

27. After establishing their objectives and eligibility criteria, the Member States must set out procedures for the selection of operations and projects from the population of eligible projects. The selection criteria should allow the Member States to identify and spend the available budget on those operations and projects that will contribute most to the objectives. Effectively applying selection criteria is a requirement of the relevant EU legislation¹³.

BOX 4

BROAD ELIGIBILITY CRITERIA LED TO THE FUNDING OF CERTAIN PROJECTS WHICH DID NOT ADDRESS THE OBJECTIVES OF THE MEASURES

Poland: Although measure 311 aims to diversify holdings towards non-agricultural activities and to promote employment outside agriculture in rural areas, in the Malopolska region, 42 % of the beneficiaries purchased equipment (such as tractors, etc.) so as to be able to provide basic agricultural services like those carried out on their own farms to third parties, without making any contribution to diversification in the rural economy.

Also in Poland, 68 % of the projects financed under measure 313 (tourism) at the time of the audit related to the construction of municipal sports facilities or investments in playing fields for children. For example, a football field located beside a school was modernised under measure 313. This project aimed to improve the quality of life for the rural community by creating a modern sport and leisure infrastructure and providing primary school children with sports facilities. However, this type of project is not likely to diversify the economy by attracting tourists, which is the aim of the measure¹⁴.

¹⁴ Article 55 of Regulation (EC) No 1698/2005 set the type of investment eligible under measure 313 — *Encouragement of tourism activities* — 'The support referred to in Article 52(a)(iii) shall cover the following: (a) small-scale infrastructure such as information centres and the signposting of tourist sites; (b) recreational infrastructure such as that offering access to natural areas, and small-capacity accommodation; (c) the development and/or marketing of tourism services relating to rural tourism'.

- 28.** Selection criteria should allow the relative merits of project proposals to be evaluated on an objective and transparent basis; they should also ensure that any projects that do not represent value for money are rejected. Indeed, even where projects do fulfil the conditions, some are better than others at addressing the objectives which have been set to satisfy the needs of the rural areas. For instance, as available funds are limited, all else being equal, if one investment project creates more jobs in rural areas than another project, it should be preferred.
- 29.** Two of the Member States audited did not set out any selection criteria and relied only on their broad eligibility criteria to draw up a list of projects to which funding was to be given. This was the case for France (Aquitaine) and Poland during the first years of the programming period (2007–10). In fact, during this period, Poland chose projects either on the basis of a ‘first-come, first-served’ principle or randomly¹⁵. In a further Member State, Sweden (‘Västra Götaland’), the selection procedure used did not result in any scoring or ranking of projects to enable an objective comparison between projects over time so as to ensure that the highest priority projects were selected consistently.
- 30.** The remaining three Member States (Italy — Campania, the Czech Republic and United Kingdom — England) applied selection criteria and a number of different scoring systems, although the Czech Republic suspended the application of their selection criteria in 2009. However, these became meaningless in Italy — Campania and the Czech Republic, since none of these two Member States/regions set an effective minimum threshold score which a project had to reach in order to be selected. This means that, whilst funding was available, projects could be selected even if they were assessed as not being particularly relevant to the national/regional priorities (see **Box 5**).
- 31.** Four of the audited Member States (France (Aquitaine), Italy — Campania, Sweden (Västra Götaland) and the Czech Republic), selected as many eligible projects as possible with the resources available regardless of their potential contribution towards the measures objectives. However, the audit found that, later on, if the budget was insufficient to cover all eligible applications, Member States selected the projects in a stricter manner. As a consequence, better projects were rejected later in the process solely as a result of budgetary reasons (see **Box 6**).

¹⁵ In Poland, selection criteria were only applied in 2011 call for proposal for M311, in 2010, 2011 calls for proposal for M312 and in 2009, 2010 calls for proposals for M313.

BOX 5

EXAMPLES OF SELECTION SYSTEMS FAILING TO SELECT RELEVANT PROJECTS

Italy — Campania: The design of the system appeared to represent good practice as eligible investment projects were evaluated on the basis of a selection criteria grid which provided for an overall minimum score (threshold) to be achieved by eligible projects, including a 'project quality' threshold. However, the system awarded points not only where a project met the criteria but also when they were not met.

Under the category 'quality of the projects', a project that does not satisfy any criteria will obtain 20 points (that is the 'minimum threshold' to be achieved) and will therefore still be financed. This effectively renders project quality selection meaningless since all projects automatically qualify if enough funding is available.

France (Aquitaine): In the absence of selection criteria, the mere fact that a project was eligible and funds were available meant that it would be selected. As a result, a project for the creation of a new wine tasting room was funded even though such facilities existed already. The project did not further diversify/broaden the farm's activity and therefore did not contribute to the objectives of the measure under which it was funded.

BOX 6

EXAMPLES OF INEFFECTIVE SELECTION PROCESSES

Czech Republic: During the first two years (2007 and 2008), without a minimum threshold and with a sufficient budget to finance all eligible applications, the projects submitted were not actually ranked according to the preferential criteria. As a consequence, projects with 0 points out of a maximum of 35 and 1 point out of a maximum available score of 106 were still financed. Since 2010, eligible projects have needed a much higher score to be funded: minimum 25 out of 40 and 54 out of 101 points respectively.

Italy — Campania: For measure 312, during the first application period (July/August 2009), all 163 eligible applications were financed. In the second period, (September/October 2009), 322 applications were admissible, but only 70 were financed because the entire budget for the measure had already been used up. This meant that projects from the second period were excluded even where they scored much better than others that had been financed during the first period. For example, of the projects excluded due to a lack of funds during the second period the best ranked had a score higher than 85 % of those financed during the first period.

Sweden: Until 2011, there were no cases where applications for eligible projects were rejected on the grounds of being low priority. A result of this failure to prioritise is that the measures were partially closed in 2011 due to budget shortages and projects were rejected on the grounds that 'money for projects is limited and we must prioritise'. While this resulted in a stringent targeting of the remaining budget, most of it had actually already been spent.

JOB CREATION WAS PART OF THE OVERARCHING PRIORITY FOR THE MEASURES, BUT THIS WAS NOT ALWAYS REFLECTED IN HOW FUNDS WERE CHANNELLED

- 32.** As mentioned above (see paragraph 14) creating jobs is part of the overarching priority of axis 3. Therefore, while prioritising projects that meet RDP objectives, Member States should try to select projects with the highest potential for creating jobs. They should seek not only to create more jobs but also to have due regard for the financial effectiveness and efficiency of the aid, for example by taking into account the cost per job and job quality.
- 33.** The audit revealed that, with the exception of France, all the Member States audited considered the job creation potential in their assessment of project proposals. However, the weaknesses in the selection systems described above meant that, in practice, in some Member States this was not effective in prioritising projects that created employment (see paragraphs 30, 31). As an example, although the Italian (Campania) measure 311 selection system did allow for the prioritisation of projects that promoted the full employment of a member of the farm household (see paragraph 21), there were weaknesses in the application of this criterion (see **Box 7**).

BOX 7

A GOOD SYSTEM ON PAPER BUT NOT IN PRACTICE

In **Italy — Campania**, the criterion linked to the objective to promote the full employment of the member of the household is described as the ratio Investment Cost/Number of employees. However, the assessment involved calculating the percentage of members of the farm household that find full employment and translating that percentage into points.

The call for proposals did not provide any instructions on how to calculate this percentage. Consequently, the calculations were not made and points were awarded on the basis of unsubstantiated claims in the technical report.

For example, for an agritourism project, the beneficiary included 'an increase in working hours for the members of the family' as an expected result and, on this basis, the project was given the maximum number of points. Compliance with this criterion was not checked during the on-the-spot checks carried out by the authorities before final payment and the beneficiary could not provide the auditors with any evidence to support this claim.

- 34.** For projects with the objective of creating jobs, the cost per job created is an indicator of their financial efficiency. The Court calculated this indicator¹⁶ for the 26 projects audited that managed to create jobs (see **Annex II**). This calculation showed that the cost per job created varied widely between projects, ranging from 3 000 euro to 215 000 euro. Whilst the Court recognises that projects may have other objectives that should also be considered during the selection process, the significant differences in the cost per job created within/for similar activities indicate the need for greater attention to this aspect.
- 35.** Three of the Member States audited considered financial efficiency of the projects proposals submitted in terms of cost per job. In their projects' appraisal, the UK authorities assessed and scored the skills level of the planned jobs relating to the project and their value for money (cost per job and cost per skill level in terms of the grant).
- 36.** In Poland, the amount granted varies according to the number of jobs that the beneficiary commits himself to creating, while in Italy the cost per job is only assessed under measure 312 and all expenditure (i.e. the entire investment cost) is taken into account compared to an average value determined by the authorities. Extra points are awarded on the basis of the calculation of the cost per job.
- 37.** Only Poland, the Czech Republic and the United Kingdom made the grant conditional upon achieving job creation where the latter was foreseen by the project. In Poland and the United Kingdom evidence had to be submitted together with the payment claim (although the UK also accepted expected results), while in the Czech Republic, project promoters were subject to targeted checks after the implementation of the projects. Clear rules on the commitment period for maintaining the created jobs were set out in Poland and the Czech Republic — respectively two years after the final payment and up to the end of the five-year commitment period.¹⁷
- 38.** Conversely, the authorities in Italy — Campania only relied on the estimate of jobs to be created as stated by the beneficiary in his/her application. The creation of these jobs was not a condition of payment and was not checked at final payment nor during later monitoring activities. The audit revealed that only four of the nine projects audited sought to create jobs and for two of those job creation was well below the expected realisation.

¹⁶ Calculated as the total public support paid to the beneficiary, divided by the number of jobs created (in full-time equivalents).

¹⁷ Article 72 of Regulation (EC) No 1698/2005.

NO PROACTIVE MANAGEMENT OF THE MEASURES

- 39.** Even when the monitoring and evaluation information showed that measures' targets were not met, the Member States authorities did not redesign the interventions in order to maximise their impact, supporting more effective and efficient projects that could deliver real results vis-à-vis the targets set.
- 40.** This was particularly visible in the Czech Republic, where despite the significant underachievement of the job creation target, partly due to the unrealistic/ambitious targets set by the authorities, no action was taken to increase the preference for projects that created jobs. In Sweden, re-allocation of part of the axis 3 budgets between counties took account of the level of expenditure but not the progress in achieving results. In Italy, a high aid rate was offered to increase take-up, but without any link to the achievement of results (see **Box 8**).

BOX 8

EXAMPLES OF LACK OF PROACTIVE MANAGEMENT

Czech Republic: The mid-term evaluation, issued in 2010, highlighted the limited effect of the three measures audited. The evaluator found that measure 311 only achieved 0,8 % of the indicator for gross jobs to be created. Measure 312 achieved only 1,4 % of the job creation target initially set and measure 313 only achieved 1 % after three years of programme implementation. Despite this lack of success, the Czech Republic had not adapted the measures. Instead, the Czech authorities, whilst maintaining the same level of programmed expenditure per measure, have reduced their targets for the result indicator 'Gross number of jobs created' by over 90 %, from 29 000 to 2 700.

Italy — Campania: In order to boost the financial implementation of the measures, in 2010, the authorities increased the maximum public aid rate to 100 % for project amounts up to 50 000 euro for measures 311 and 312. This removal of the obligation of a beneficiary to contribute to the project was not linked to an increased value for money of the projects in terms of results to be achieved.

Sweden: Despite the fact that the CMEF result indicator for jobs created only reached 6,6 % of the target in 2010, the measures or selection criteria were not adapted to make them more effective so as to ensure that the target would be met. Furthermore the counties were informed that if they had not committed at least 50 % by October 2011, their budgets would be reallocated to other counties that were able to spend faster.

THE COMMISSION HAS NOT SUFFICIENTLY USED PERFORMANCE INFORMATION TO IMPROVE THE EFFICIENCY AND EFFECTIVENESS OF DIVERSIFICATION MEASURES

- 41.** The Commission monitors and supervises the implementation of the programmes, notably through participation in monitoring committee meetings¹⁸, the examination of annual progress reports and audit visits to Member States. In addition, the Commission's responsibility for sound financial management also requires it to improve the implementation of the programme accordingly. Article 77(2) of Regulation (EC) No 1698/2005 provides the Commission the opportunity to participate in meetings of the Monitoring Committee 'in an advisory capacity'.
- 42.** The Commission has insisted, throughout the programming period, on the need for greater selectivity and targeting in the implementation of the measure, regardless of 'budgetary sufficiency'. However, the audit revealed that the Commission did not always ensure that Member States defined adequate selection criteria and/or applied them consistently. Indeed, the Commission did not take effective action despite the fact that France, Poland, and the Czech Republic (in 2009) did not apply any selection criteria. However, in respect of other rural development measures, the Commission has taken action for similar weaknesses by proposing financial corrections.
- 43.** Furthermore, the Commission did not take adequate steps during the Monitoring Committee or the annual examination of programmes' progress¹⁹ to ensure that Member States were effective in selecting and approving projects that contributed towards achieving the objectives set. With reference to the case shown in **Box 8**, the Commission has not required an improvement in the effectiveness of diversification measures in the Czech Republic, but rather it has accepted a simple reduction in the targets for gross number of jobs to be created.

¹⁸ Article 78 of Regulation (EC) No 1698/2005 states 'The Monitoring Committee shall satisfy itself as to the effectiveness of the implementation of the rural development programme'. This is done by considering and revising selection criteria, monitoring progress toward objectives, achievement of targets, etc.

¹⁹ Article 83 of Regulation (EC) No 1698/2005 states 'Each year, on presentation of the annual progress report, the Commission and the Managing Authority shall examine the main results of the previous year, in accordance with procedures to be determined in agreement with the Member State and Managing Authority concerned'.

PART TWO — WERE THE RISKS TO EFFICIENCY AND ECONOMY SUFFICIENTLY MITIGATED?

- 44.** Achieving value for money is about the optimal use of resources to realise the intended outcomes. In addition to effectiveness, the general risks to sound financial management are the risks to efficiency and economy.
- 45.** The risk to efficiency is the possibility that an activity:
- does not maximise output for a given input or that it does so without paying due regard to appropriate quality; or
 - does not minimise input for a given output, or that it does so without paying due regard to appropriate quality.
- 46.** The risk to economy is the possibility that an activity:
- does not minimise the cost of resources, or that it does so without having regard to appropriate quality.
- 47.** The risks to efficiency and economy can already be significantly mitigated by good programming. However, this does not relieve the authorities of the responsibility for performing the relevant checks on implementation.
- 48.** For this reason, and in accordance with the principles of efficiency and economy set out in Article 30(2) of Regulation (EU, Euratom) No 966/2012²⁰ the Court considers that Member States should:
- ensure, prior to granting funding, that applicants have been able to show that their projects are financially viable and sustainable;
 - apply procedures to mitigate the risk of deadweight and displacement²¹;
 - ensure that the projects have reasonable costs;
 - ensure that the projects can be implemented within a reasonable time frame and without unjustified ‘red tape’ and costs.

²⁰ Regulation (EU, Euratom) No 966/2012 of the European Parliament and of the Council of 25 October 2012 on the financial rules applicable to the general budget of the Union and repealing Council Regulation (EC, Euratom) No 1605/2002 (OJ L 298, 26.10.2012, p. 1).

²¹ For definitions, see paragraphs 51 and 58.

EFFICIENCY

MEMBER STATES CHECKS GIVE LIMITED ASSURANCE OF THE FINANCIAL SUSTAINABILITY OF PROJECTS

49. In order to avoid that public funding is not wasted on projects that fail prematurely, Member States should, through proportionate viability checks, analyse the soundness of the applicant's financial situation and business planning and document their appraisal.
50. The current legislation does not explicitly require such viability checks²², and only three of the Member States audited (Poland, Sweden and the UK) systematically performed checks on the applicants' financial standing. However, particularly in Poland and Sweden, the audit found a number of shortcomings, mainly in relation to superficial and unreliable assessments, and weak documentation. The other Member States audited did not perform any systematic viability check (France (Aquitaine) and Italy — Campania) or had suspended them (Czech Republic) (see **Box 9**).

²² However, Article 72 of Regulation (EC) No 1698/2005 requires that all supported projects need to be sustainable in the sense that Member States shall ensure that an investment operation does not, within five years of the funding decision, undergo a substantial modification, including the cessation or relocation of a productive activity. In addition, the Commission recognised that such criteria should be part of project appraisal in the EU Rural Review No 1: 'Care is being taken to ensure maximum value for money from the significant sums of axis 3 funding and economic sustainability forms a key criterion during assessment of all EAFRD project proposals' (page 31) (see: http://enrd.ec.europa.eu/publications-and-media/eu-rural-review/en/eu-rural-review_en.cfm).

BOX 9

VIABILITY CHECKS: EXAMPLES OF GOOD PRACTICE AND WEAKNESSES

United Kingdom — England: The authorities apply several procedures, depending on the size of the grant, that can be seen as good practice: financial ratios are calculated on the basis of accounting information and projections of cash flow, an independent opinion is provided by an accountant and a business plan with sales projections and a market analysis must be supplied. The underlying assumptions are critically reviewed by the appraiser and management and delivery risks taken into account.

Poland: In one case, the beneficiary's initial business plan showed a negative net present value (NPV), which would have rendered the project ineligible. When the Polish authorities asked the beneficiary to explain the negative NPV, he merely presented a new plan increasing the sales projections significantly. The NPV shifted from negative to positive and the project was accepted. The Court found that the project results had fallen significantly short of both the initial and revised projections.

France (Aquitaine): Financial analyses and feasibility studies are requested for certain projects, although no formal check on viability is made on the basis of these documents. In one case, a project was approved and funded despite a feasibility study highlighting that the enterprise was experiencing financial difficulties as its overall solvency was weak, with significant short-term risks and very limited financial autonomy. The Court's audit visit revealed that the supported business was in bankruptcy.

Czech Republic: Checks on the applicant's creditworthiness were initially carried out for projects over 2 million CZK (approximately 78 000 euro) in eligible costs. In view of the economic crisis and to avoid reducing the number of eligible applicants during the crisis, the Czech authorities decided to stop assessing the creditworthiness of beneficiaries from mid-2009 onwards.

MEMBER STATES' PROGRAMMING AND IMPLEMENTATION OF THE MEASURE DO NOT EFFECTIVELY MITIGATE RISKS OF DEADWEIGHT ...

51. Deadweight refers to the extent to which a beneficiary would have undertaken the investment even without grant funding. Giving grants in such cases reduces the efficiency of EU and national budget funds, as public expenditure is not needed to achieve the desired effect.
52. The primary means of reducing the risk of deadweight is to design and programme measures 311–313 in such a way that public funding is directed where there is an identified need (e.g. market failures) or to encourage the provision of positive externalities and public goods (e.g. through assistance with the costs of introducing environmentally sustainable technologies or projects providing wider public benefits). However, even when the system was designed to encourage the delivery of public goods through support for private beneficiaries, the potential positive impact was, in some cases, nullified in practice (see **Box 10**).
53. Member States can also mitigate the risk of deadweight through the project selection process. The Member States could have asked the applicants to demonstrate that they need a grant with reference to the financial, marketing and management information obtained for the viability check. If an applicant had sufficient capital or access to capital to finance the entire project or if the project's prospects for success were high, the investment would normally be made anyway with or without the aid. This would represent an inefficient use of scarce public funds.

BOX 10

AN EXAMPLE OF POTENTIAL POSITIVE IMPACT NULLIFIED IN PRACTICE

Italy — Campania: The system of project assessment provided for the calculation of a score related to environmental criteria. However, the audit found that 10 points could be attributed for the criterion 'water saving' or five points for 'going beyond normal waste treatment' by only promising to make the most basic investments like dual flush toilets or a low-cost compost bin (cost of a compost bin: 350 euro as against total project cost of 247 000 euro in one example). No overall water saving needed to be promised, nor was it assessed. 15 points (a decisive number in many cases) could thus be obtained with no meaningful water saving or environmental impact being envisaged by the project.

- 54.** The rural development programmes of two out of the six Member States audited (Sweden and the UK — England) highlight the fact that deadweight implies a serious risk to sound financial management. However, only in the United Kingdom did the authorities require beneficiaries to demonstrate the need for the grant, rejecting projects where the need for public funding was not proven. The following elements were taken into account by the United Kingdom authorities during the projects appraisal: how convincing the application was in justifying why a grant is needed, the market failures the project addresses, the existence of a funding gap (for example comparing alternative cash flow projections between a 'borrowing scenario' and a 'public intervention scenario'), and value of the project outputs to the region by estimating the proportion of the outputs that would have been delivered without the grant.
- 55.** The Court has already noted (e.g. in its reports on the Leader approach, measure 121 and measure 123²³) that cases where investments have already started or even been completed before a decision is taken to award a grant are a strong indication of the deadweight effect. In these situations, the beneficiary's initial investment decision already shows that he/she would have been willing and able to carry out the investment even without the aid. Consequently, it is considered good practice for Member States only to deem projects eligible for funding as from the date of grant approval.
- 56.** The United Kingdom (England) applied this good practice. In the other Member States that were audited, investments were generally eligible as from the date on which the application was submitted. The auditors found that 25 of the 57 projects visited (i.e. 44 %) had started before the grant decision was made (see the **Table**).
- 57.** The risk of deadweight was further assessed on the basis of interviews with the beneficiaries and documentary evidence regarding the sources of financing used to complete the project, the profitability of the investment and the timing of the investment in relation to the grant decision. The analysis shows that 35 out of the 57 projects (61 % of the sample) would have been implemented anyway, albeit in some cases on a smaller scale or over a longer period of time (see **Annex II**). This was particularly the case where the grant amount was very small, such as in Sweden where over one third of the grants awarded were around 10 000 euro or less. Moreover, in Sweden, the Court even found a case where a project was approved after its completion (see **Box 11**).

²³ Special Report No 5/2010 on the implementation of the Leader approach for rural development; Special Report No 8/2012 on targeting of aid for the modernisation of agricultural holdings and Special Report No 1/2013 Has the EU support to the food-processing industry been effective and efficient in adding value to agricultural products? (<http://eca.europa.eu>).

TABLE

PROJECTS THAT HAD BEEN STARTED BEFORE GRANT APPROVAL

Member State	Total number of projects subject to audit visits	Audited projects started before approval
Czech Republic	11	4
France (Aquitaine)	10	8
Italy — Campania	9	3
Poland	8	3
Sweden (Västra Götaland)	10	7
United Kingdom — England (Yorkshire and Humber)	9	0
Total	57	25

BOX 11

A STRONG INDICATION OF DEADWEIGHT: GRANTING EU FUNDING FOR A PROJECT WHICH HAS ALREADY BEEN COMPLETED

In **Sweden**, a grant of 240 000 SEK (22 000 euro) was given for an extension to the workshop premises of an existing business servicing and repairing forestry machinery. The beneficiary submitted an incomplete grant application in May 2008, with a one line description of the project and no business plan. Subsequently, he completed his grant application at the beginning of May 2009 with information requested by the County Board. The decision to award the grant was taken one week later and, in the same month, the beneficiary forwarded a payment claim. The project had already been completed in April 2009 before the complete application was submitted.

During the Court's audit visit, the beneficiary stated that he had already decided to undertake the project before he learned of the possibility of a grant. He had a bank loan agreement in place for up to 1,2 million SEK (approximately 110 000 euro), which he would have used to finance the entire project if the grant had not been awarded.

... AND DISPLACEMENT

- 58.** Displacement is the degree to which the benefits resulting from an activity supported using public funds are offset by reduced activity elsewhere. A subsidy that enables one beneficiary to increase its market share at the expense of a competitor may have no net effect on policy objectives such as creating employment. Such subsidies are therefore a priori not an efficient use of EU funds and can lead to market distortion at local level. A degree of displacement may, however, be justified where there is a sufficient net effect in terms of policy objectives.
- 59.** As with deadweight, the primary means of mitigating the risk of unjustified displacement lies in the design of the measures. The RDP should establish the need for expenditure (e.g. by analysing expected demand and excluding sectors where the market appears saturated), identify needs that are sufficiently strong to justify any displacement that may occur and set objectives and eligibility conditions that are specific to those needs. As shown in the first part of this report, this was not done in the Member States audited. The rural development programmes of Sweden and the UK do however recognise displacement as a potential risk to sound financial management.
- 60.** Member State authorities should assess project proposals for the risk of displacement during the project approval stage. Where displacement is likely to occur, they should ensure that the contribution that the project would make to the measures' objectives is sufficiently high to justify the grant.
- 61.** Only the United Kingdom²⁴ had taken appropriate steps to assess and mitigate displacement; specifically their implementing rules exclude proposals 'in sectors of the economy that have reached saturation point, leading to an oversupply, damaging productivity and lead to the displacement of similar businesses'. Furthermore, the Court identified the following elements of good practice in the UK appraisal system: a requirement for the beneficiary to prove market demand and describe the impact on competitors, the assessment of displacement risk as part of project appraisal and selection, and projects rejected where displacement was likely.

²⁴ France (Aquitaine) had also, for a specific type of investment in camping facilities, provided for an assessment of displacement risks.

- 62.** The Court assessed the 57 projects visited for the risk of displacement, basing its review on an examination of documentation and on discussions with beneficiaries about their companies' products, markets and competitors, and about the effects of the investment on these factors. Indications of displacement risk were identified for 19 projects (see **Annex II**). Examples of indications of displacement are described in **Box 12**. For three projects, the risk of displacement was considered not applicable and for four projects the Court did not have enough evidence to assess it.

ECONOMY

- 63.** The principle of economy requires that the financial resources must be made available in due time, in an appropriate quantity and quality and at the best price. There is a risk that beneficiaries may not seek to implement the projects at the lowest costs consistent with the necessary quality. In this event, the cost to the EU and national budgets may be unnecessarily inflated. This is uneconomical and inefficient and reduces the available funding for other projects. The Commission and the Member States should ensure that the project costs proposed by the applicants of measures 311–313 are reasonable, and that administrative procedures should be as simple as possible to allow an effective and efficient implementation of projects for the benefit of rural areas.

BOX 12

EXAMPLE DEMONSTRATING THE RISK OF DISPLACEMENT

Sweden: Measure 313 supported the construction of conference rooms for a visitor centre. The beneficiary provides two-day conferences during which around 15 participants are lodged at a nearby hotel. A new investment project promoted by the visitor centre and supported with EU funds includes the construction of guest accommodation for up to 20 people. The Swedish authorities did not consider the risk of displacement when approving the grant, despite the fact that the project is likely to result in a loss of business for the nearby hotel, where the participants currently stay overnight.

However, the audit did find examples of good practice

United Kingdom — England: In the case of a farm shop, the regional development agency assessed as part of the project appraisal how close the nearest farm shop competitors were and if it was likely to affect their businesses. The low level of displacement was considered justified given the positive assessment of the regional tourism authorities.

POOR CHECKS ON THE REASONABLENESS OF COSTS

- 64.** Article 24(2)(d) of Regulation (EC) No 65/2011²⁵ specifies that Member States should verify the reasonableness of project costs submitted as part of the administrative checks on applications for support. This evaluation must be performed using a suitable system, such as reference costs, the comparison of a number of offers or an evaluation committee.
- 65.** The Court found that France did not apply any such procedures. This was all the more serious because the Commission had already (in 2008) asked the French authorities to introduce a system to verify the reasonableness of costs as part of their administrative checks and has applied, in the past, a financial correction for this type of weakness concerning other investment measures.
- 66.** The other Member States that were audited applied relevant systems, consisting of specific procurement rules, checks against standard costs or a combination of both. However, these checks varied in quality. The Court identified cases of non-compliance with EU rules in Sweden and significant weaknesses in the Czech Republic, Italy — Campania and Poland, involving incomplete, superficial and poorly documented checks (see **Box 13**). Following the Court's visit, the Italian authorities issued a revocation order for the aid granted to a local municipality (46 780 euro) partly due to problems relating to the selected bid and the price accepted for the services funded.

²⁵ Commission Regulation (EU) No 65/2011 of 27 January 2011 laying down detailed rules for the implementation of Council Regulation (EC) No 1698/2005, as regards the implementation of control procedures as well as cross-compliance in respect of rural development support measures (OJ L 25, 28.1.2011, p. 8).

EXAMPLES OF WEAK AND 'GOOD PRACTICE' RULES AND CHECKS IDENTIFIED IN THE MEMBER STATES

Sweden: The usual method used for establishing the reasonableness of costs is to require applicants to provide two quotes for costs that represent at least 25 % of the total. This means that a project promoter does not have to show, for up to 75 % of the proposed total, that the costs are reasonable.

Eligible expenditure is not limited to the amounts quoted and beneficiaries can therefore claim for costs in excess of the amounts (accepted as being 'reasonable') and still get the full grant as long as they obtain lower prices on other items (for which 'reasonableness' was not checked), or by not purchasing other items included in the application. This does not result in savings to the EU budget as the beneficiary may use the 'savings' to purchase additional items up to the ceiling of the approved total project cost.

In one of the audited projects, no quotes were provided for 2,5 million SEK or 290 000 euro involving the building and fitting of a new restaurant and a separate guest house (grant: 900 000 SEK or 94 000 euro, grant rate: 30 %). There was no mention in the project file of any measures to check that the costs were reasonable.

Italy — Campania: In Italy, the only check carried out by the provincial authorities on the reasonableness of costs for general expenses was that their value should not exceed the ceilings mentioned in the call for proposals without considering the detailed nature and scope of the services (usually consultancy services) provided. For example, for a simple project involving the purchase of a new bus, the consultant charged a fee of 15 000 euro (5,1 % of the price of the bus); this fee was eligible for public support.

Furthermore, for some projects, machinery and/or equipment were provided by different companies from those selected by the independent expert and authorised by the expert evaluator. In one case the beneficiary stated that he had granted the contract for the creation of a website to a friend who was able to do the work at the same price as the company selected by the expert. However, the auditors found that the website was not fully functional at the time of the audit (March 2012) despite the invoice having been paid on 9 August 2010. The incomplete website was not noted during the visit made as part of the pre-payment checks.

The Court identified the following good practices: in **England**, the inspections made in accordance with Articles 27 and 30 of Regulation (EC) No 1975/2006 (5 % at payment and 1 % *ex post*) included checks for credit notes or discounts. In **Italy — Campania**, the region included in the 2011 call for proposals the requirement to enclose the vendor's published price-list to the offer and to indicate any discounts offered.

THE ADMINISTRATIVE BURDEN IMPEDES THE EFFECTIVE AND EFFICIENT IMPLEMENTATION OF PROGRAMMES

- 67.** As stated in paragraph 63, the Member States' procedures must not be excessively long and burdensome so as not to dissuade applicants from submitting project proposals. This risk is particularly evident for potential beneficiaries who cannot afford to take the risk of their grant application's being rejected, leaving them to finance the project entirely by themselves — or otherwise delay the investment and potentially miss a business opportunity.
- 68.** The administrative burden and associated bureaucratic costs and delays stand out as factors that hamper the achievement of programme objectives, particularly where they are not justified by the selection of more effective projects (see **Box 14**).

BOX 14

A SYSTEM THAT REDUCES THE BURDEN ON THE APPLICANT AND ONE THAT DID NOT

United Kingdom — England: The UK authorities reviewed short Expression of Interest forms weekly and gave feedback to applicants on their project's likely eligibility and the extent to which it matched the region's priorities. This procedure spared applicants the expense of preparing a full application that was likely to be rejected while decreasing the administrative burden for appraisal, etc. Rural business facilitators were appointed for each project to support the applicant in making the application.

Once the promoter submitted an application, the selection process was completed within around nine weeks. The appraisal covered strategic fit with regional priorities, innovation, the multiplier effect, demand for the product/service, financial viability, the reasonableness of costs; outputs and outcomes of the proposal, dead-weight and the value for money of the public funding.

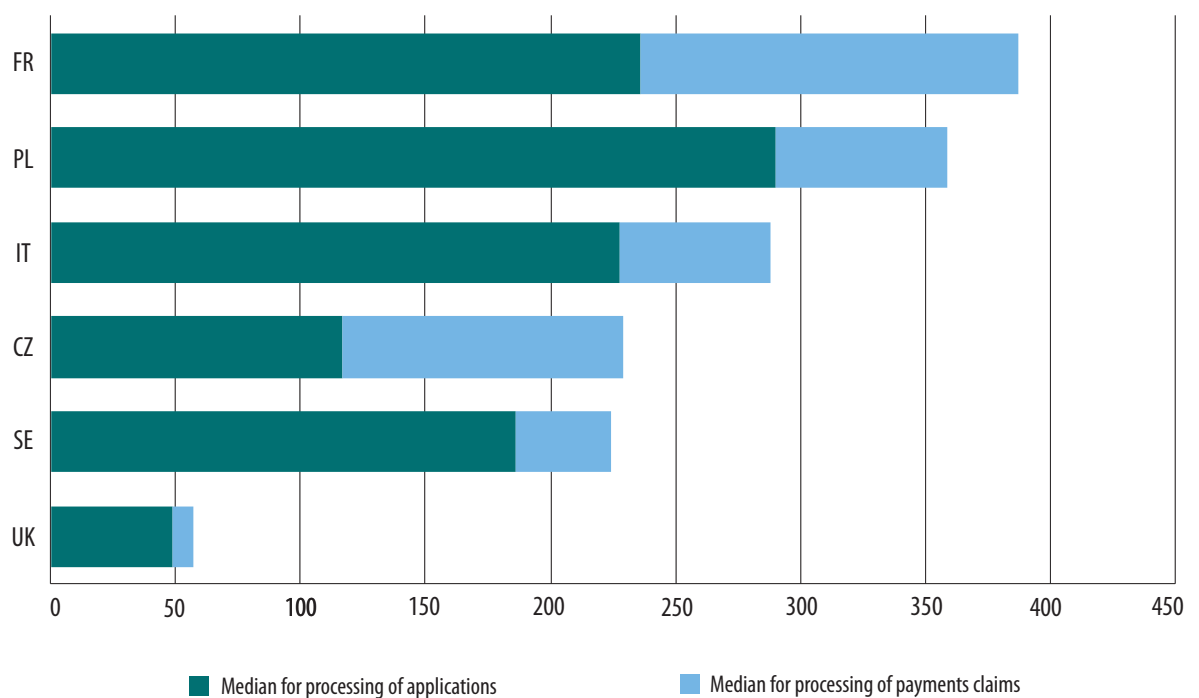
Poland: In Poland, the approval procedure for the majority of applications took longer than 6 months — and more than one year for 55 % of measure 312 applications. The main reasons for this were the low quality/incompleteness of applications and the flexible rules that allowed beneficiaries to amend their application twice during each stage of the assessment. The selection criteria set out by the Polish authorities did not assess the 'quality of the individual projects' as they referred to quantifiable indicators relating to characteristics of the holding (e.g. size, no previous use of EU funds) or the area where they were located. There was no appraisal of the relative merits of the project proposals.

69. In France, Italy — Campania, Poland and Sweden, it took seven to eight months²⁶ to process grant applications (see **Graph 1**). Furthermore, the French authorities needed around five months to process payment claims and make final payments, with extreme cases of more than 1 year. The Court considers this to be disproportionately long, given the low value and low level of complexity of most of the projects supported under measures 311–313.

²⁶ Median value (in calendar days).

GRAPH 1

PROCESSING OF APPLICATIONS AND PAYMENT CLAIMS (IN CALENDAR DAYS)



- 70.** Delays in project approval and payments can have negative impacts on timely project implementation and the scope of projects financed, and ultimately on the economic situation of an applicant (see **Box 15**).
- 71.** In Italy — Campania, France (Aquitaine) and the Czech Republic, the project owners interviewed considered the procedures in their own countries to be too burdensome. Moreover, it should be noted that the Court only audited projects that had been completed successfully, thus not considering applicants that had been dissuaded by the administrative burden or delays. Furthermore, most beneficiaries used consultants to prepare their applications, sometimes at significant cost, partly because they did not feel able to do so themselves.

BOX 15
PAYMENT SYSTEMS CAN HELP OR HINDER BENEFICIARIES

United Kingdom — England: In the UK, the system provided relative certainty to beneficiaries about project approval and payment dates, allowing short-term finance to be arranged and encouraging grants to be taken up by companies that might not otherwise have been able to cope with the cost of the projects. Moreover, applicants were informed in advance of the selection panel's meeting dates and applications were timed to be submitted at a specific meeting. For payment claims, project promoters were informed that they could plan for their grants to be paid in the month after their claim had been submitted. The Court considered these to be examples of good practice.

Italy — Campania: In order to receive an advance payment, beneficiaries are required to present an insurance policy guaranteeing the amount requested. The Italian Paying Agency's (AGEA) procedure for processing guarantees was only fully functional from May 2010 although the call for proposals had already been published in 2008. This led to serious delays in the advance payments, with consequent impact on the implementation of the programme: out of 430 projects approved in the 2008–11 period, only 27 projects were at the final payment stage (6 %) in 2012. Beneficiaries faced further problems with the release of the guarantees which led to cases where, at the time of the audit in March 2012, some beneficiaries still incurred significant guarantee-related costs despite having received their final payments in 2011.

PART THREE — WERE EFFECTIVE AND EFFICIENT PROJECTS ACTUALLY FUNDED?

- 72.** Performance information on the effectiveness and efficiency of rural development spending is needed to demonstrate what has been achieved with the EU budget and that it has been spent well (accountability); to be used to improve the efficiency and effectiveness of the EU budget through informing ongoing management (calls for proposals or grant decisions), identifying improvements to be made in the current programming period, and informing decision-making on future policy.
- 73.** In order to show what has been achieved with EU budget spent on diversification measures, Member States should collect data on the results achieved by projects. Under the Common Monitoring and Evaluation Framework (CMEF), Member States must collect information for at least the common output and result indicators (see footnote 11). The two common result indicators set out for measures 311–313 should provide information on how projects performed in terms of increase in non-agricultural gross value added (GVA)²⁷ and gross number of jobs created.
- 74.** The Court examined the data collection and monitoring systems in the six Member States and found, as in previous reports²⁸, that there was an absence of relevant and reliable information to conclude on the effectiveness of these measures. Therefore, the auditors measured project results (in terms of the two CMEF indicators mentioned above) and achievements of the specific project objectives, where possible, on the basis of evidence obtained from project visits.

MONITORING INFORMATION IS LACKING AND PROJECT RESULTS SHOW A MIXED PICTURE IN TERMS OF EFFICIENCY AND EFFECTIVENESS

- 75.** Given the element of co-financing and irrespective of the monitoring and evaluation work required by the CMEF, Member States' authorities have their own interest in project monitoring as an important tool to keep track of the projects' progress and to be informed as to whether they are achieving the expected results and the RDP objectives. This could be done by Member States using the administrative and control information available and by collecting periodically relevant information from the beneficiaries, at least until the expiry of the 5-year period for retaining the assets determined by Article 72 of Regulation (EC) No 1698/2005.

²⁷ To measure the GVA of the supported businesses, Guidance Note I of the CMEF guidelines suggests using the following proxy: 'Total Output — Total Intermediate Consumption'. The guidance note acknowledges that a change in GVA over the years can also be explained by factors other than the support received.

²⁸ See Special Reports No 8/2012 and No 1/2013 (<http://eca.europa.eu>).

- 76.** The audit found that the Member States did not monitor the short- to medium-term success of the projects either in terms of their achievements in addressing RDP objectives, or in terms of the objectives set for the project itself. This was hampered by the lack of clear, specific and realistic objectives and targets set out in the application and/or grant decision (see **Box 16**). France (Aquitaine) had not submitted even the mandatory monitoring information required by the CMEF at the date of the audit.
- 77.** The auditors found that the monitoring information provided by the Member States audited was not reliable. Data collected by Member States was largely based on estimates either at the time of the application (Italy, Sweden and the Czech Republic) or at the time of the final payment claim (the United Kingdom). In addition, data from beneficiary monitoring surveys was not verified by the authorities (Poland and the Czech Republic). The auditors identified several inconsistencies and errors in the data reported, particularly differences between forecasts and the actual figures (see examples in **Box 17**).
- 78.** Although reliable data concerning the achievement of the projects' objectives and results could have been obtained by Member State authorities during on-the-spot checks and *ex post* inspections, the audit revealed that this check was not part of the procedures. For example, even though one project in Italy had undergone several checks on the existence of the purchases and works after its implementation, none of these highlighted the fact that the actual revenue was well below the forecast contained in the application.
- 79.** Given that reliable monitoring information was not available, and that, at programming level, there was little assurance that support for the axis 3 measures is directed to the projects that best fulfil the measures' objectives, the Court's auditors assessed the efficiency and effectiveness of the 57 projects audited on the basis of information provided during the audit visits. The analysis shows that most projects achieved their objectives in terms of physical output and positive effects on GVA, but those with the objective to create jobs were only moderately successful in generating employment (see **Annex II**).

BOX 16

GENERIC OBJECTIVES LEAD TO A SITUATION WHERE 'ENHANCING BIODIVERSITY' IS ACCEPTED AS AN OBJECTIVE FOR A CAKE SHOP

For a project from [Italy — Campania](#), concerning the renovation of a cake shop (measure 312), the following seemingly unrelated objectives were stated in the application: '... balancing high-risk situations such as the depopulation of the countryside, reducing the gap with more developed areas [...], enhancing biodiversity as well as traditional farming knowledge'. These objectives cannot be quantified or measured for such a project.

BOX 17

EXAMPLES OF INCONSISTENCIES IN THE MONITORING DATA COLLECTED BY THE MEMBER STATES

Sweden: Data for the CMEF indicators were compiled from project information collected from the beneficiaries at the grant application stage (the business plan and financial forecasts), and were not updated on the basis of what was actually achieved. For a restaurant and guest house project, evidence obtained during the visit showed CMEF data for gross value added was overestimated at 1 800 000 SEK (202 000 euro), compared to the actual result of 238 000 SEK (27 000 euro) and three full-time equivalent jobs were reported in the CMEF database as compared to the actual result of one full-time equivalent job created with the supported investment.

United Kingdom — England: Evidence obtained in the project visits shows that the results recorded in the CMEF database were not accurate. In five cases out of nine audited, the data on jobs created and jobs safeguarded were overestimated, in the other cases they were underestimated.

Poland: The non-agricultural GVA figure declared by a beneficiary in the monitoring survey could not be reconciled with income data collected during the audit visit. The declared GVA was higher than the total output for the supported business, which is not possible according to the definition of gross value added.

- 80.** Whilst projects could be seen to achieve the expected physical output (e.g. construction of a building, purchase of a vehicle) the objectives of the measures to diversify the rural economy were not necessarily achieved. This was the case where the purpose of the investment was not in line (or was only partially in line) with the objectives of the measure (11 projects in total: three in France and Poland, two in Sweden and Italy, and one in the Czech Republic) or/and where there were strong indications that it was not sustainable (two cases in the Czech Republic) or the business had gone bankrupt (one project in France).
- 81.** The Court found cases where there was indication that EU funds to develop the tourist sector or to support micro-enterprises were spent on investments which were at least partially used for private purposes (see **Box 18** for some examples).

BOX 18

INVESTMENTS THAT DID NOT EFFECTIVELY CONTRIBUTE TOWARDS DEVELOPING THE TOURIST SECTOR AND SUPPORTING ENTREPRENEURIAL INITIATIVES

Italy — Campania: At the time of the on the-spot visit at an agritourism project, a flat refurbished with measure 311 funds was being used by a member of the beneficiary's family, meaning that it did not fully contribute towards the measure's objective to increase the non-agricultural GVA through diversified activities.

Poland: Indications of private use were identified for a project for the purchase of office equipment that received measure 312 aid. A leather sofa for receiving clients was funded at the beneficiary's home (which also served as the premises for the business) and used in a living room. No pre-payment visit to this project was made which could have raised doubts by the inspectors as to the potential private use of the goods funded.

DIVERSIFICATION PROJECTS CAN HELP BOOST FARMERS' FINANCIAL PERFORMANCE ...

- 82.** 33 of the supported businesses (58 %) managed to increase their non-agricultural GVA; however, for eight of these cases, there was a weak link between this and the grant-aided investment. The GVA could not be calculated for five projects audited in Poland and the Czech Republic because they were subject to simplified accounting rules. Despite this situation, the authorities had not introduced a system to collect reliable data. GVA increase could not be assessed in six further projects (in Poland and Italy) because either it was too soon to assess their financial impact, or the beneficiary had not supplied the relevant financial data. Six projects did not generate an increase in non-agricultural GVA.

... BUT WHEN THEY AIM TO CREATE JOBS THEY ARE ONLY PARTIALLY EFFECTIVE ...

- 83.** Of the 27 projects that were intended to create jobs, only 13 projects achieved the targets set (although the Court has doubts in two cases about the sustainability of jobs created) while nine projects only partly created the foreseen number of jobs intended and five did not create any jobs. The audit revealed that jobs were largely created as envisaged in those Member States where the grant was made conditional upon job creation, and targeted checks were carried out to ensure compliance with this condition. This was the case in Poland, the Czech Republic (for certain sub-measures) and the United Kingdom (see paragraph 37). Conversely, the auditors noted that the impact on job creation was minor for projects audited in France, Italy and Sweden, where this type of condition did not apply and targeted checks were not carried out (see *Annex II*).

... AND THERE IS AN UNKNOWN EFFECT ON MAINTAINING JOBS

- 84.** Although projects may not all be intended to create jobs, the investments may maintain or safeguard jobs. However, Member States are not required by the monitoring and evaluation framework to collect these data. Only the United Kingdom — England defined an additional indicator in its CMEF database measuring 'jobs safeguarded' as jobs that would be lost if the grant-aided investment was not undertaken, although the application of this definition was inconsistent. In one project which reported two jobs as being safeguarded, the Court found that the number should have been reported as zero. In Poland, the audit revealed that data on jobs maintained were reported but mixed with data on job creation. As a result, the auditors were not able to conclude on the impact of the projects on jobs safeguarded or maintained, as no evidence was available to assess this at the Member State and beneficiary levels.

CONCLUSIONS AND RECOMMENDATIONS

- 85.** As part of the rural development policy Member States may use the EU budget to finance projects that seek to diversify the rural economy in order to support growth, employment and sustainable development in rural areas. This is done through the EU and Member States co-financing of projects in the areas of diversification into non-agricultural activities, creation of micro-enterprises and the encouragement of tourism activities.
- 86.** This audit examined the question ‘Have the Member States and the Commission achieved value for money with measures for diversifying the rural economy?’ The Court concludes overall that the Commission and the Member States have, only to a limited extent, achieved value for money through the measures for diversifying the rural economy, as the aid was not systematically directed to the projects that were most likely to achieve the purpose of the measures. This was due to a lack of clear needs for intervention or specific objectives being set in the RDPs, broad eligibility criteria adopted that did not limit the projects to those most likely to achieve diversification and selection criteria that did not choose the most effective projects or were not applied at all.
- 87.** Too often, and particularly at the start of the programming period, the selection of projects was driven more by a need to spend the allocated budget than by the quality of the projects themselves. In some Member States audited, all eligible projects were funded where sufficient budget was available regardless of how the project was assessed by their selection systems. The overarching priority of job creation was not properly targeted, the monitoring did not allow the true picture of jobs created to be ascertained and there was a lack of active management particularly when it was apparent that the targets set would not be met.
- 88.** Member States did not sufficiently mitigate the risks of deadweight and displacement, and therefore they did not ensure the most efficient use of resources. Member States checks on reasonableness of costs did not sufficiently reduce the risk of overspend and there were examples of excessive administrative burden and payment delays.
- 89.** These weaknesses and the related Court’s recommendations are further developed below.

- 90.** Better targeting of rural development support is a key issue in improving efficiency at measure level. Since targeting is based on the identification of priority areas, beneficiaries or types of activity or achievements, its effectiveness depends primarily on the quality of the strategy that the programme is based on. Therefore, improved targeting will follow from improved strategy making and above all a clear framework on how diversification can/will contribute towards sustainable growth (i.e. the rationale for intervention). However, the majority of RDPs which were audited did not set down the outcome that they plan to achieve and did not explain how providing funding under diversification measures would improve the economic sustainability of the rural area. Nevertheless, the Commission approved these RDPs.

RECOMMENDATION 1

In their RDPs, Member States should clearly identify why and how public intervention for investments in non-agricultural activities can help to redress for example market failures related to barriers to employment and growth.

The RDPs should set specific and measurable objectives in relation to these needs.

The Commission should approve only those RDPs that present substantiated and comprehensive strategies with a clear rationale that show how policy intervention will contribute to strategic aims of creating growth conditions and employment opportunities.

- 91.** Eligibility conditions established by some Member States did not restrict the aid to activities supporting diversification of rural economy towards non-agricultural activities. Furthermore, EU legislation requires Member States to establish selection criteria; these should allow the most effective and efficient eligible projects to be prioritised, and provide a basis for rejecting those that do not represent value for money. Only four of the six audited Member States/regions established selection criteria, and even these were not always applied in practice.

- 92.** Where the audited Member States still had funds available from the amount which was budgeted, they financed all eligible projects, regardless of their effectiveness and efficiency. Later in the period when funding was tight 'better' projects were rejected.

RECOMMENDATION 2

Member States should establish and consistently apply criteria to ensure the selection of the most effective, sustainable projects with respect to the Member States' specific objectives in order to develop non-agricultural activities and promote employment. The potential of the projects to produce positive effects on employment and incomes should be taken into account in the design of future policy and be more prominently considered by the Member States in their project selection systems. These selection systems should systematically set a minimum threshold taking into account the 'quality of project'. Targeted controls should be carried out to ensure the respect of such criteria for example during the on the spot and *ex post* checks.

The Commission should ensure that these criteria are correctly and continuously applied, not only in cases of budgetary shortage.

- 93.** The Court found that Member States did not systematically channel the funding to projects for which there was a demonstrable need for public support. As a consequence, the likelihood of deadweight is high and the results achieved by the projects cannot necessarily be attributed to the grant. Furthermore such subsidies may constitute a waste of scarce public money when they lead to market distortion at local level (i.e displacement effect). Only one Member State took these risks into account in projects' appraisal.

RECOMMENDATION 3

The Commission and Member States should promote the adoption of best practices in respect of mitigating the risks of deadweight and displacement. This requires Member States to select projects for which there is a demonstrable need for public support (and which deliver added value). Member States should consider deadweight and displacement risks both when drawing up their RDP and when selecting projects. The Commission should encourage Member States to adopt the practice whereby expenditure for investments would be eligible only as of the date of grant approval.

- 94.** The Court identified weaknesses in the systems put in place by the Member States to assess the reasonableness of project costs. These weaknesses increase the risk that public funds are spent without due regard to the principle of economy.

RECOMMENDATION 4

Member States should mitigate the risk to economy by a systematic assessment of costs that should not be limited only to questions of eligibility and the results of this assessment should be adequately documented. Where feasible, benchmarks should be developed for common cost items in order to facilitate the assessment of costs in project proposals.

The Commission should ensure that Member States have effective systems to carry out checks on reasonableness of the costs.

- 95.** The CMEF has been set up as a monitoring and evaluation tool for the Member States and the Commission. The Court found that it does not generate reliable data which can be used to monitor the effectiveness of the measures implementation and identify problems and solutions in a timely manner. Moreover the Commission and the Member States have not used the monitoring information to actively manage these measures in order to improve their effectiveness.
- 96.** In terms of job creation, part of the overarching priority of axis 3, the Member States audited could not provide accurate information on the jobs created or maintained nor, where targets were not being met, did they adapt spending to take this into account.

RECOMMENDATION 5

The Commission and the Member States should ensure that for the forthcoming programming period, relevant and reliable information is obtained to facilitate management and monitoring of the measure and to demonstrate the extent to which the aid given is contributing to the achievement of EU priorities. Furthermore, Member States should ensure that clear specific objectives are set for the projects to which funds are committed. Objectives should be quantified where possible to facilitate the execution and monitoring of the projects and to provide useful feedback for the managing authority.

The targets for job creation should be realistic and the numbers of jobs created accurately monitored, the measures should be better managed throughout the programming period and particularly if it becomes apparent that targets set will not be achieved.

Member States should be encouraged to develop tailor-made indicators that reflect their own specific context and need, for their own management and evaluation purposes.

- 97.** The administrative burden should be reduced as far as possible, especially in respect of smaller projects; excessive payment delays can discourage beneficiaries.

RECOMMENDATION 6

The Commission and Member States should increase their efforts in reducing the administrative burden and ensuring that payments are made in a reasonable timeframe. Consideration could be given to a procedure for 'fast tracking' small scale investments (shorter periods for processing applications) and payments.

This Report was adopted by Chamber I, headed by Mr Ioannis SARMAS, Member of the Court of Auditors, in Luxembourg at its meeting of 5 June 2013.

For the Court of Auditors

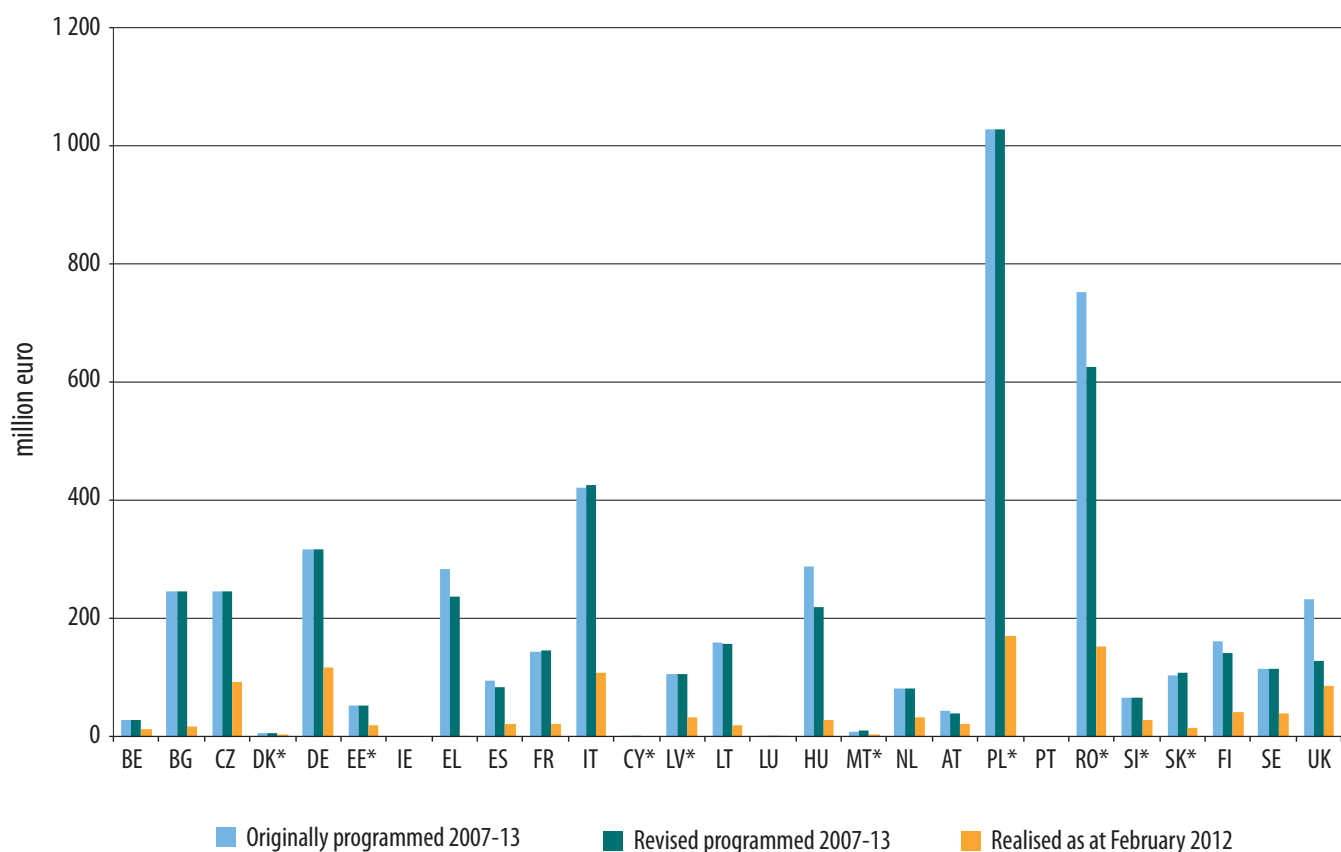


Vítor Manuel da SILVA CALDEIRA
President

ANNEX I

EU FUNDS FOR AXIS 3 DIVERSIFICATION MEASURES PROGRAMMED AND SPENT (AS AT FEBRUARY 2012)

- Originally programmed expenditure (2007–13): 4 922 400 000 euro
- Revised programmed expenditure (2007–13): 4 619 133 731 euro¹
- Implemented expenditure (2007–February 2012): 1 090 970 738 euro



¹ By 31 December 2011.

Source: European Court of Auditors' compilation on the basis of data provided on the website of the European Network for Rural Development: Financial and physical indicators (http://enrd.ec.europa.eu/policy-in-action/rural-development-policy-in-figures/rdp-monitoring-indicator-tables/financial-and-physical-indicators/en/financial-and-physical-indicators_en.cfm). Ireland and Portugal have not programmed measures 311, 312 and 313. The symbol "*" indicates the Member States (Denmark, Estonia, Cyprus, Latvia, Malta, Poland, Romania, Slovenia and Slovakia) that have not programmed all three measures. As at February 2012, no expenditure had been declared by Cyprus.

COURT'S ASSESSMENT OF THE PROJECTS AUDITED

Member State	Measure	Project description	Eligible costs (rounded, euro)	Public aid as % of eligible costs	Project output delivered in line with the general objectives of the measure	Project results		Indications of dead-weight	Indications of displacement
						Non-agricultural GVA increase	Number of jobs created/foreseen (in FTE)		
Czech Republic	312	Construction of a printing hall	200 000	60 %			0 / 0	strong	some
	312	Purchase of production line for book binding	95 000	49 %			1 / 1	strong	some
	313	Installation of information panels and resting areas on a wine path	20 000	90 %			0 / 0	few	none
	313	Construction of tourist accommodation by extending an existing wine cellar	75 000	60 %			0 / 0	some	some
	312	Purchase of a saw machine and auxiliary equipment	45 000	50 %			2 / 2 **	few	few***
	311	Construction of biogas plant (500 kW)	1 600 000	35 %			0 / 0	few	insufficient evidence
	311	Extension of biogas plant (by 250 kW) and other construction works	550 000	30 %			0 / 0	some	insufficient evidence
	312	Reconstruction of a production hall and purchase of a metal processing equipment	190 000	50 %	*		6 / 6 **	strong	strong
	311	Construction of biogas plant (537 kW)	2 380 000	45 %			0 / 0	few	insufficient evidence
	311	Purchase of drying wood facilities and site preparation works	155 000	60 %			0 / 0	few	few
	311	Construction of biogas plant (526 kW)	1 890 000	46 %			0 / 0	few	insufficient evidence

 positive assessment

 negative assessment

 n.a. not applicable

 mainly positive assessment

 no jobs created/no jobs foreseen

 mainly negative assessment

 insufficient evidence/too early to assess

ANNEX II

Member State	Measure	Project description	Eligible costs (rounded, euro)	Public aid as % of eligible costs	Project output delivered in line with the general objectives of the measure	Project results		Indications of dead-weight	Indications of displacement
						Non-agricultural GVA increase	Number of jobs created/foreseen (in FTE)		
France (Aquitaine)	311	Creation of a shop for local sales	135 000	29 %			0,8/0	strong	few
	311	Creation of a wine tasting room	130 000	21 %			0/0	strong	some
	311	Creation of a farm shop selling own-produce (cheese)	60 000	38 %			0/0	some	some
	311	Creation of a farm shop selling own-produce (cheese)	55 000	50 %			0/0	few	some
	312	Relocation of a shop in a new commercial area	35 000	25 %			0/0	strong	some
	312	Creation of an electrical appliances shop	35 000	25 %			0/0	strong	few
	312	Purchase of an electric bread oven	35 000	25 %			-3,3/0	some	few
	313	Construction and upgrading of an eco-hostel	3 000 000	10 %			0/1	some	few
	313	Creation of an eco-campsite	625 000	16 %			2,58/2	few	some
	313	Construction of a reception hall/shop as part of renovation works in a public castle	200 000	50 %			1,2/0	strong	n.a.

 positive assessment

 negative assessment

 n.a. not applicable

 mainly positive assessment

 no jobs created/no jobs foreseen

 mainly negative assessment

 insufficient evidence/too early to assess

ANNEX II

Member State	Measure	Project description	Eligible costs (rounded, euro)	Public aid as % of eligible costs	Project output delivered in line with the general objectives of the measure	Project results		Indications of dead-weight	Indications of displacement
						Non-agricultural GVA increase	Number of jobs created/foreseen (in FTE)		
Italy (Campania)	311	Renovation of an agri-tourism resort and purchase of gardening equipment	400 000	50 %			0/0	strong	few
	311	Reconstruction of house for rural tourism	245 000	50 %			0,75/0	few	some
	311	Paving of the outside area of a holding and purchase of teaching room furniture for an educational farm	125 000	50 %			0/0	strong	few
	313	Organisation of rural events and festivals and creation of a website	45 000	100 %	****	n.a.	n.a.	few	n.a.
	312	Purchase of bus with facilities for disabled people to allow visits to tourist attractions	305 000	50 %			1,2/3	strong	few
	312	Renovation of a cake shop and purchase of solar panels and other cake-mining equipment	205 000	40 %			1/1	some	few
	312	Renovation of a trattoria and creation of a pizzeria including a wood-fired oven	50 000	50 %			1/3	some	some
	311	Restoration of small houses for rural tourism	190 000	50 %			0/0	some	few
	311	Restoration of farm building for rural tourism	400 000	50 %			0,92/1	few	some

 positive assessment

 negative assessment

 n.a. not applicable

 mainly positive assessment

 no jobs created/no jobs foreseen

 mainly negative assessment

 insufficient evidence/too early to assess

ANNEX II

Member State	Measure	Project description	Eligible costs (rounded, euro)	Public aid as % of eligible costs	Project output delivered in line with the general objectives of the measure	Project results		Indications of dead-weight	Indications of displacement
						Non-agricultural GVA increase	Number of jobs created/foreseen (in FTE)		
Poland	311	Purchase of a tractor to carry out agricultural services in the neighbouring area	25 000	50 %			0/0	few	few
	311	Purchase of a digger-loader to create an alternative source of non-agricultural income	55 000	43 %			0/0	some	few
	312	Purchase of office equipment and a car	15 000	50 %			1/1	strong	few
	312	Purchase of a digger to extend the scope of construction services rendered	175 000	37 %			4/3	some	few
	313	Construction of sport and beach ball fields	90 000	100 %		n.a.	n.a.	few	few
	311	Renovation and equipment for an agritourism holding	40 000	56 %			0/0	some	few
	312	Purchase of a truck and reconstruction of a building used by a wholesaler	30 000	50 %			1/1	strong	some
	313	Reconstruction of an amphitheatre	140 000	100 %		n.a.	n.a.	few	n.a.

 positive assessment

 negative assessment

 not applicable

 mainly positive assessment

 no jobs created/no jobs foreseen

 mainly negative assessment

 insufficient evidence/too early to assess

ANNEX II

Member State	Measure	Project description	Eligible costs (rounded, euro)	Public aid as % of eligible costs	Project output delivered in line with the general objectives of the measure	Project results		Indications of dead-weight	Indications of displacement
						Non-agricultural GVA increase	Number of jobs created/foreseen (in FTE)		
Sweden	312	Staff and overhead costs for the association aiming to build a network of rural businesses	120 000	62 %	*	n.a.	0/4	few	few
	312	Creation of a cooperative for handicraft sales and cleaning services	65 000	98 %		n.a.	1/0	few	few
	312	Construction of a hall for indoor horse riding	170 000	30 %			0/2	some	some
	312	Conversion of a barn into a new flower/plant shop business	10 000	30 %			1/1	some	few
	312	Extension of the flower shop business to allow flower-arranging courses	10 000	25 %			0/0	strong	few
	313	Construction of an entrance hall with gift shop, art gallery/conference rooms	160 000	30 %			4/1,5	some	some
	313	Extension of café at tourist site to increase capacity	190 000	25 %		n.a.	0/0	few	few
	311	Extension of workshop premises with lifting equipment	90 000	25 %	*		0/0,25	strong	few
	311	Business advice and marketing material for a travel agency specialising in agritourism	10 000	30 %			0/1	strong	few
	311	Construction of a new restaurant and a separate bed and breakfast guest house	315 000	30 %			1/4	strong	some

 positive assessment

 negative assessment

 not applicable

 mainly positive assessment

 no jobs created/no jobs foreseen

 mainly negative assessment

 insufficient evidence/too early to assess

ANNEX II

Member State	Measure	Project description	Eligible costs (rounded, euro)	Public aid as % of eligible costs	Project output delivered in line with the general objectives of the measure	Project results		Indications of dead-weight	Indications of displacement
						Non-agricultural GVA increase	Number of jobs created/foreseen (in FTE)		
United Kingdom (England)	312	Renovation of barn for use as business premises plus some IT equipment	105 000	40 %			2/3	some	few
	312	Completion of renovation of building and equipping as dental surgery	140 000	40 %			4,8/5,3	strong	some
	311	Construction and equipment to extend existing farm shop/café; website	320 000	40 %			5,9/5,5	few	some
	313	Café, courtyard and walkway construction within a new start-up visitor attraction	315 000	40 %			3,5+/4	few	few
	313	Construction and equipment to create a café, plus a secure storage area	205 000	40 %			1,25/6	strong	few
	311	Purchase and erection of wind turbines on farm	75 000	50 %			0/0	few	none
	313	Construction and equipment to create a new entrance to the gardens with shop	155 000	50 %		n.a.	1,5/2,5	few	few
	311	Renovation of barn and equipping as café and premises for existing farm shop	220 000	50 %			2,5/4	few	few
	312	Equipment for a start-up offering laundry services to tourist accommodation	30 000	40 %			4,5/2,5	strong	some

 positive assessment

 negative assessment

 not applicable

 mainly positive assessment

 no jobs created/no jobs foreseen

 mainly negative assessment

 insufficient evidence/too early to assess

- * The Court found that three projects were not eligible. Two projects in Sweden were not eligible because in one case the beneficiary was not a microenterprise (according to Article 54 of Regulation (EC) No 1698/2005) and in the other case the beneficiary was not a member of the farm household (Article 53 of Regulation (EC) No 1698/2005). In the Czech Republic the Court's audit found that a metal processing company given aid under M. 312 was not a microenterprise: a recovery order for nearly 97 000 euro is to be issued.
- ** The Court has doubts on the sustainability of jobs.
- *** Project aimed at capturing previously outsourced activities from the production chain but this had not been achieved at the date of the audit.
- **** Following the Court audit, the Italian authorities issued a recovery order because the beneficiary (the Commune) did not provide access to documents to the Court auditors.

Assessment criteria	
Project output delivered in line with the objectives of the measure¹	<p>The outputs delivered by the project in terms of:</p> <ul style="list-style-type: none"> — contribution to the objectives of the measure set out in the main EU regulation ((EC) No 1698/2005); indications of private use are taken into consideration — sustainability of the financed activity as of the date of the audit (as a pre-condition of achieving objectives)
Non-agricultural GVA increase	<p>The results of the project in terms of increase in non-agricultural GVA (gross value-added), where $GVA = Total\ Output - Total\ Intermediate\ Consumption$ $Total\ Output = Value\ of\ sales + Balance\ of\ stocks + Own\ use\ or\ consumption$ $Total\ Intermediate\ Consumption = Direct\ Inputs + Overheads$ (i.e. linked to production activities, but not to specific lines of production) such as maintenance of buildings and machinery, energy, water, insurance for buildings, other overheads)</p> <p><i>Note:</i> a change in GVA can also be due to other factors than the support received. Low causality with the supported project is indicated in yellow</p>
Job creation	<p>The results of the project in terms of:</p> <ul style="list-style-type: none"> — number of jobs created (expressed in FTE — full-time equivalents) compared to the number envisaged at the moment of the application for support — type of jobs created (permanent jobs, seasonal jobs, temporary jobs, etc.)
Indications of deadweight	<ul style="list-style-type: none"> — beneficiary's own assessment of whether the investment would have taken place without the grant — investment project started or even completed before grant application/before grant decision — project pre-financed mostly or entirely from own resources — the company's financial situation at the date of application shows a very good financial position — investment appraisal shows high rate of return (or short payback) and there are no indications that the beneficiary had difficulties in acquiring capital
Indications of displacement	<ul style="list-style-type: none"> — beneficiary's own assessment of displacement — the beneficiary is in a stable or decreasing market or one with little product differentiation and the project's primary aim was to increase capacity/market share or increase efficiency/reduce costs

¹ Article 4(c) of Regulation (EC) No 1698/2005 states that 'Support for rural development shall contribute to achieving the following objectives ... encouraging diversification of economic activity' and Article 52(a): 'Support shall involve

(a) measures to diversify the rural economy, comprising:

- (i) diversification into non-agricultural activities,
- (ii) support for the creation and development of micro-enterprises (...),
- (iii) encouragement of tourism activities.'

REPLY OF THE COMMISSION

EXECUTIVE SUMMARY

IV.

The Commission would like to remark that the concept of the measures subject to Court's audit is broad.

The objectives of the diversification measures are not strictly and solely linked to growth and jobs. Other objectives as defined by MS in their RDPs could also be addressed by these measures.¹

The Commission would like to point out that the third core objective of the rural development policy is the improvement of the quality of life in rural areas and encouragement of diversification of economic activities.

V.

The legal framework, which is currently in place, provides for a broad scope and purpose of the measures, which provides for a large flexibility in the implementation.

The principles of subsidiarity and shared management hands considerable discretion to Member States and regions. According to these principles, project selection including the setting up of project selection criteria lies within the responsibility of Member States.

Nevertheless, in its supervisory role, the Commission has insisted on several occasions on the need for greater selectivity² and targeting in the implementation of the measure.

¹ Council decision of 20 February 2006 on Community strategic guidelines for rural development (programming period 2007 to 2013), 2006/144/EC, section 3.3.

² For example, during annual meetings, notably, at the beginning of the programming period a letter was sent from the Commission to the managing authorities of all programmes inviting them to take into account the importance of well-defined selection criteria for an effective implementation throughout the whole period. Furthermore, in 2009, another letter asked all Member States to make sure that adequate selection criteria are specified and used for the allocation of funds.

The Commission takes the view that needs and opportunities were described with sufficient clarity to make programming of the audited measures appropriate and possible even if the analyses in question could have been improved in some cases. The Commission considers that the purpose of the eligibility criteria defined by the MS is not, per se, to exclude a specific company of an economic sector from EU support. Instead eligibility criteria should aim, at the level of supported operation, at better targeting the support to the actual needs of the territory concerned, on the basis of the strategic programming and the SWOT analysis. The legislation itself already favours micro-enterprises, rural tourism activities and farm diversification activities. As concerns targeting, the Commission agrees with the Court that improvements in better targeting the support are needed at the level of MS.

Targeting can also take the form of detailed eligibility rules, regional and sectorial differentiation, differentiation of aid intensities as well as aid ceilings by which Member States can make a pre-selection among potential beneficiaries.

While noting that the measures subject to audit have wider objectives than barriers to employment and growth, the Commission agrees that the RDPs should present measurable objectives contributing to the policy aims.

The Commission, being aware of some weaknesses in this field, has proposed, for the EAFRD for the next programming period 2014–20, to strengthen the legal framework so that *ex ante* quantified targets are set for each of the focus areas of the Union priorities. The content of the programme shall contain a description of the strategy, and that the selected measures in relation to the Union priorities are based on sound intervention logic supported by an *ex ante* evaluation.

REPLY OF THE COMMISSION

VI.

The targeting requirement of investment support (Article 43 of Commission Regulation (EC) No 1974/2006) was first explicitly introduced in this programming period, among other aspects, to counter deadweight and displacement effects.

Support to projects should be granted on the basis of the assessment whether the project contributes to the objectives of the RDP.

The Commission agrees that the current framework could be improved. However, taking account of the beneficiaries' financial capacity in isolation to assess deadweight may entail the risk of supporting non-viable projects and increased administrative costs for the authorities and increased administrative burden for the beneficiaries.

The risk of overspending is to be considered. The aid-intensity rates should contribute to reduce such risks.

On the subject of administrative burden, the Commission has proposed for the next programming period 2014–20 that the three measures audited by the Court be merged into one single measure with a better beneficiary focus, improved eligibility conditions and better rules for payments reducing the administrative burden that could be associated with these measures. The Commission is foreseeing further reduction of the administrative burden in the form of introducing simplified costs.

The Commission is encouraging MS (e.g. in monitoring committees and in annual review meetings) to shorten the delay for project approval and payment to beneficiaries, and is informed that the situation is improving. However, it is Member State's responsibility to ensure efficient delivery mechanisms and well-functioning administrative procedures at national/regional level.

VII.

The Commission considers that, as a matter of principle, the CMEF³ is a valid instrument to monitor and evaluate progress towards achieving the EU's rural development policy objectives and has turned out to have much strength, although some difficulties have also been encountered.

To remedy the weaknesses in methodologies developed by Member States (MS) to assess some indicators, the Commission established, distributed and explained methodological guidelines in 2010 to those in charge of the evaluation within the MS. More reliable figures are now expected.

The strategic approach in rural development and for each MS is defined in the respective National Strategy Plan (NSP).

RDPs should comply with the strategic approach identified in the NSPs and should aim at developing support options in line with the EU legislation that can contribute to the achievement of the EU and MS strategic priorities, including the one on creation of employment in rural areas.

For the next programming period the Commission is developing a new version of the CMEF, together with the Member States, which will allow the assessment, for each RDP, of progress in implementation against commonly defined target indicators for the priorities and focus areas selected for the programme. At the basis is an indicator plan which for each focus area sets the target and the planned outputs and expenditure for the measures that will be used to achieve the targets and objectives of the programme. The indicator plan represents more accurately the quantified intervention logic for each individual programme than does the current rigid axis structure.

³ CMEF — Common Monitoring and Evaluation Framework.

REPLY OF THE COMMISSION

VIII.

The Commission notes that many of the following recommendations are addressed to the Member States and that the principle of subsidiarity and shared management hands considerable discretion to Member States and regions.

— When approving the RDPs, the Commission carries out an analysis to assess that programmes and measures are consistent with the Community strategic guidelines, the relevant national strategy plans and that they comply with the relevant legal provisions⁴.

While noting that the measures subject to audit have wider objectives than just redressing market failures related to barriers to employment and growth, the Commission agrees that the RDPs should present measurable objectives contributing to the policy aims.

The Commission, being aware of some weaknesses in this field, has proposed, for the EAFRD for the next programming period 2014–20, to strengthen the legal framework so that *ex ante* quantified targets are set for each of the focus areas of the Union priorities. The content of the programme shall contain a description of the strategy, and that the selected measures in relation to the Union priorities are based on sound intervention logic supported by an *ex ante* evaluation. Where a proposed programme does not contain such a strategy and adequate targets, the Commission will not approve it.

⁴ Council Regulation (EC) No 1698/2005 and Commission Regulation (EC) No 1974/2006 (Article 18 of Council Regulation (EC) No 1698/2005).

— The broad scope of the audited measures should be recognised, as they not only bring impact on employment and income but also contribute to the sustainability of rural areas.

The Commission has insisted on several occasions during the current programming period on the need for greater selectivity and is prepared to further encourage Member States to do so.

The application of selection criteria or equivalent targeting mechanism is examined by the Commission in its audit missions and several observations in this regard have been made to the Member States. If needed, the Commission proposes financial corrections.

The Commission agrees with the recommendation and has, in the proposal⁵ on the EU rural development policy for programming period 2014–20 foreseen that the selection criteria shall be defined for all measures and shall aim to ensure equal treatment of applicants, better use of financial resources and targeting of measures in accordance with the Union priorities for rural development. The use of selection criteria is proposed to be generally compulsory even in the case where available funds are sufficient, except in case of some compensatory area and animal-related measures.

The Commission also agrees that the project selection system of the Member States should take into account the quality of the projects and use a minimum scoring system. The Commission will present guidelines to the Member States on the use of eligibility and selection criteria for the next programming period.

⁵ The legal basis is the proposal for the Rural Development Regulation and its Article 49, as well as the related implementing/delegated acts. See COM(2011) 627 Final/2 dated 19.10.2011.

REPLY OF THE COMMISSION

— The Commission agrees with the recommendation and is prepared to organise exchange of best practices on the mitigation of deadweight and displacement risks with the Member States.

The legislation provided that the general state aid rules apply for support under Article 52(a) of Regulation (EC) No 1698/2005. These rules require that expenditure is eligible from the submission of the aid application. This requirement is stated in the state aid rules to establish the necessary incentive element to prevent the deadweight.⁶ The same rules should apply to co-financed measures as for separate aid schemes notified under state aid regime.

Taking account of the beneficiaries' financial capacity in isolation to assess deadweight may entail the risk of supporting non-viable projects and increased administrative costs for the authorities and increased administrative burden for the beneficiaries.

— The Commission covers the issue of evaluation of the reasonableness of costs during its audit missions on investment measures. It verifies that the Member State has established an effective system to evaluate the reasonableness of costs. Given the complexity of the subject, the Commission will continue to examine the issue during its audit missions. It will also continue the discussions with the Member States outside the Clearance of Accounts framework.

The number of audit missions is limited due to the number of available staff. Therefore, the number and scope of these missions are decided on the basis of a risk analysis.

— Objectives and their targets at programme level are set up by the managing authority as part of the programme strategy. At the project level estimated/predicted results/outcomes by which the project in question will contribute to the programme objectives are set *ex ante* by potential beneficiaries in their applications. However, there are always uncertainties and external factors in the achievement of the targets set, so the targets should also be able to be adjusted accordingly, if need be.

⁶ Article 8 of Commission Regulation (EC) No 800/2008. Its paragraph 2 states: Aid granted to SMEs, covered by this regulation, shall be considered to have an incentive effect if, before work on the project or activity has started, the beneficiary has submitted an application for the aid to the Member State concerned.

The Commission agrees with the recommendation and is taking care that in the preparation of the Common Monitoring and Evaluation Framework for the future period, which is currently being elaborated⁷, weaknesses observed during this period are taken into account. Therefore, for the next programming period, result indicators will rather be assessed as part of the RDP evaluation. It will also be done by developing more precise explanatory documents (fiches) for each indicator to avoid potential inconsistencies in data collection through misinterpretation.

For the next programming period 2014–20 the Commission is developing a CMEF, together with the Member States, which will allow the assessment, for each RDP, of progress in implementation against commonly defined target indicators for the priorities and focus areas selected for the programme. At the basis is an indicator plan which for each focus area sets the target and the planned outputs and expenditure for the measures that will be used to achieve the targets and objectives of the programme. The indicator plan represents more accurately the quantified intervention logic for each individual programme than does the current rigid axis structure.

— The Commission is encouraging MS in different contexts (e.g. in monitoring committees and annual review meetings) to shorten the delay for project approval procedures and payments to beneficiaries, and is informed that the situation is improving during the current programming period.

For the next programming period 2014–20 the Commission is foreseeing further reduction of the administrative burden in the form of introducing simplified costs. As a result, the processes of claiming, administering and auditing reimbursement for payments made will be easier for both the beneficiaries and the administration itself.

⁷ The legal basis is the proposal for the Horizontal Legislation art.110, the proposal for the RD Regulation title VII, as well as the related implementing/delegated acts. See COM(2011) 628 Final/2 dated 19.10.2011 and COM(2011) 627 Final/2 dated 19.10.2011.

REPLY OF THE COMMISSION

INTRODUCTION

3.

Recital 47 from Council Regulation (EC) No 1698/2005, also applies to axis 3.

The Commission would like to point out that Recital 11 and Article 4 of Regulation (EC) No 1698/2005 define the third core objective of the rural development policy to be the improvement of the quality of life in rural areas and encouragement of diversification of economic activities.

5.

The Community Strategic guidelines state in addition that: 'In promoting training, information and entrepreneurship, the particular needs of women, young people and older workers should also be considered'.

8 — third indent

Typical projects such as recreational infrastructure and small-scale infrastructure (information centres and sign posting of tourist sites) as described by Article 55 of Council Regulation (EC) No 1698/2005, are also important for the assessment of axis 3.

OBSERVATIONS

16.

The objectives of the diversification measures are not strictly and solely linked to growth and jobs. Other objectives as defined by MS in their RDPs could also be addressed by these measures.⁸ Therefore the analysis of the situation in terms of strengths and weaknesses is a general one covering the whole programming area and goes beyond the mere drivers of employment and growth (Annex II, point 3.1 of Commission Regulation (EC) No 1974/2006).

⁸ See section 3.3 of the Community strategic guidelines for rural development (programming period 2007 to 2013).

18.

When approving the RDPs, the Commission carries out an analysis to assess that programmes and measures are consistent with the Community strategic guidelines, the relevant national strategy plans and that they comply with the relevant legal provisions. Its observations have been communicated to the Member States, resulting in improvements of the programmes. The intervention logic that characterises each RDP covers the whole architecture of a programme and its delivery mechanism, and thus each RDP contained the necessary information that allowed its approval according to the legal framework.

The Commission considers that in general needs and opportunities were described with sufficient clarity to make programming of audited measures appropriate and possible in each case.

The study on the 'Synthesis of *ex ante* evaluations of 2007–13 RDPs'⁹ which was finalised in 2008 concluded that that 'substantial efforts have been made in the MS to identify needs, and that these have been carefully considered in the programming phase. MS devoted considerable efforts in the development of their strategies which are based on a thorough assessment of needs'.

Most of the RDP-level *ex ante* reports found an appropriate and strategic choice of measures.

Box 2

The RDP for UK (England) explains that the regional/local authorities 'will have particular regard to rural economic underperformance and disadvantage ... when deciding, with their regional and local partner, which areas resources will be allocated to' (section 5.3.1.3, paragraph 553).

19.

See reply to point 18.

⁹ Study on 'Synthesis of *ex ante* evaluations of rural development programmes 2007–13'; available at: http://ec.europa.eu/agriculture/eval/reports/rurdev/index_en.htm.

REPLY OF THE COMMISSION

20.

The principles of subsidiarity and shared management hands considerable discretion to Member States and regions. Under these principles, the setting up of objectives at national or regional level lies within the responsibility of Member States.

The legal framework does not prevent a programme from having different objectives in terms of scope and measurability. Member States can always set additional indicators than those identified in the CMEF, if this proves necessary.

The Commission has proposed, for the next programming period, that appropriate targets should be set for each of the focus areas of the Union priorities, on the basis of common indicators, and that the selected measures in relation to the Union priorities should be based on sound intervention logic supported by an *ex ante* evaluation.

Box 3 — Czech Republic

All three measures belong to the same priority within axis 3 (job creation and support of using renewable energy sources) and as such have identical global objectives. Nevertheless, with regards to the specificity of each measure, the three measure fiches, under heading 'profile of the measure' (characteristics of the measure), illustrate the nature of the projects to be funded.

22.

The legislation allows for a wide interpretation of the eligibility of activities and sectors under axis 3.

Targeting can be achieved not only via limitation on the eligibility of activities or economic sectors, but also through regional and sectorial differentiation, selection criteria, differentiation of aid intensities as well as aid ceilings by which Member States can make a pre-selection among potential beneficiaries.

24.

See replies to paragraphs 18, 20 and 22.

As regards the efficiency and effectiveness of the measures proposed by Member States contributing to growth and jobs, the Commission considers that it cannot be fully established *ex ante* (e.g. the impacts of the ongoing financial and economic crisis on rural businesses).

Growth and jobs are not the only objectives of axis 3 of the EU rural development policy, and are not the only territorial or structural needs that can be potentially identified by Member States in their RDPs.

25.

See reply to paragraph 22.

26.

See reply to paragraph 16.

The measures under axis 3 are delivered within the limitations of the general EU state aid rules. The legislation has not imposed on Member States a legal requirement for setting of restrictive eligibility rules, unless the SWOT analysis and assessment of needs require such actions at national or regional level.

The Commission will provide additional guidance on eligibility and selection criteria for the next programming period 2014–20.

As regards the observations of the Court that projects are ineligible, the following should be taken into consideration:

Czech Republic: According to information provided by the national authorities, the project is currently under review.

Sweden: Article 54 of Regulation 1698/2005 only stipulates that support shall relate to micro-enterprises, and not that micro-enterprises should be the sole beneficiaries under the measure.¹⁰

¹⁰ The Community strategic guidelines for rural development 2007–13 further define the strategic intentions behind the support provided under Article 52(a)(ii) of Council Regulation No 1698/2005. Key action (iv) from section 3.3: 'developing micro-business and crafts, which can build on traditional skills or introduce new competences, particularly when combined with purchase of equipment, training and coaching, thus helping to promote entrepreneurship and develop economic fabric.'

REPLY OF THE COMMISSION

Box 4

See reply to paragraph 26.

Poland implements measure 313 in an integrated way with village renewal and development (measure 322) and conservation and upgrading of the rural heritage (measure 323). The integrated measure aims also at the setting up of basic services, including cultural and leisure activities, concerning a village or group of villages, including related small-scale infrastructure as defined in Article 56 of Council Regulation (EC) No 1698/2005.

29.

See reply to paragraph 20.

According to the principles of subsidiarity and shared management, setting up a selection criteria and actual project selection lies within the responsibility of Member States.

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

For the next programming period, the Commission proposals¹¹ foresee that the selection criteria shall be defined for all measures. The use of selection criteria shall generally be compulsory even in the case where available funds are sufficient.¹²

Sweden: Sweden adopted selection criteria for the programme in the Monitoring Committee on 9 October 2007.

¹¹ The legal basis is the proposal for the RD Regulation, Article 49, as well as the related implementing/delegated acts.

¹² Only in case of certain annual or multiannual measures, for example agri-environment-climate measure, where the measures are implemented through standard operations which should provide equal environmental or animal welfare effects, will the use of the selection criteria be optional in case of sufficient funds.

30.

See the reply to paragraph 29.

Italy (Campania): See reply in Box 5.

Box 5 — Italy (Campania)

Following the Court's audit the managing authority has recognised the weakness detected in the attribution of points to individual projects and it has acted immediately in order to remedy the mistakes in awarding the projects presented for support. The action undertaken consisted in issuing clear instruction to the staff responsible to scrutinise the projects proposed for support. In particular it was made clear to them that no points (0 points) should be attributed if the selection criteria are not met.

Box 5 — France (Aquitaine)

According to the regional authorities investments made in order to meet the criteria set out, amongst others, in the framework of the regional programme 'Destination Vignobles' are eligible under measure 311. This is in line with the overall strategy of the region which aims at improving the standards of the touristic facilities in the vineyards by encouraging the managers to make the necessary investments in order to respect a quality charter.

According to the rules under Council Regulation (EC) No 1698/2005, the development of existing rural businesses could be supported if eligibility conditions are met.

Box 5 — Italy (Campania)

The Commission has reminded the Italian authorities about the importance of the selection procedures in ensuring that the measures and programme objectives are achieved (see also reply to Box 5).

REPLY OF THE COMMISSION

Box 6 — Czech Republic

The Commission has challenged this practice and addressed this issue with the managing authority during meetings and in writing at the beginning of 2010.¹³

Box 6 — Italy (Campania)

See replies in Box 5 and paragraph 31.

Box 6 — Sweden

According to the explanations of the Swedish Board of Agriculture the County board accepted applications on a running basis and only the projects that contributed to the objectives of the programme and the priorities set by the county were accepted. The quality of the projects and their capacity to satisfy these priorities was assessed on the basis of the business and project plans. This assessment shall in future be justified.

32.

The audited measures contribute also to the sustainable development of rural areas and their economic environment, to safeguarding existing jobs, and to development of the conditions for economic growth. Furthermore, 'skill level' should also be taken into account.

It should be noted that costs per job differ between regions, MS and economic sectors, and is not the only criterion for assessment of applications.

Cost per job may be an inappropriate indicator, for example, in the cases when investments cover highly technological activities that require little human resources for their management, when safeguarding jobs, when improving existing jobs' quality, or when temporary employment linked to the investment is created.

¹³ 1. By letter of 19 March 2010 (Ref. Ares(2010)148269) the Commission wrote to the CZ authorities indicating that it had been informed in the preparatory meeting held on 11/11/2009 before the Monitoring Committee meeting of 12/11/2009 that in 2009 the selection criteria had not been applied. This issue was also discussed with the CZ authorities at the Annual Review meeting held in February 2010 and at the preparatory meeting held on 24/03/2010 before the Monitoring Committee meeting of 25/03/2010. In its letter the Commission made reference to Article 43 of Regulation 1974/2006 and Article 71 (2) of Regulation 1698/2005.

2. The CZ authorities replied by letter of 7/04/2010 Ref. Cj.10039/10-11200 (registered at the Commission on 13/04/2010 with Ref. Ares(2010)189115).

3. The Commission has indeed replied to this letter on 17/05/2010 (Ref. Ares(2010)261022). In this letter the Commission indicated 'In the Monitoring Committee meeting itself [held on 25/03/2010], we have also understood that you would ensure that in the future the financial envelopes would be definitely fixed prior to the opening of the calls for applications and that the latter would be selected in accordance with the established criteria. Therefore, I (i.e. the undersigned person for the Commission) consider that, even though it is not clearly mentioned in your letter, you are committed by your statement in the abovementioned Monitoring Committee meeting.'

34.

The range of costs per job given by the Court (3 000–215 000 euro) does not relate to similar or same activities, thus recognition of the different types of investments should also be made.

37.

The Commission notes that the principles of subsidiarity and shared management hands considerable discretion to Member States and regions given that the CMEF does not specify what additional indicators are to be used by Member States when evaluating and monitoring projects. The selection of projects and their implementation monitoring lies within the responsibility of Member States.

The Commission makes the necessary effort in the course of its audit missions to detect inadequate practices and propose relevant measures related to it, including their correction.

40.

Italy (Campania) and Sweden: See reply given to Box 8.

Box 8 — Czech Republic

It is correct that the Czech authorities have set initially rather ambitious targets related to job creation. At the same time, the economic/financial crisis has significantly hindered creation of employment. Therefore, following the mid-term evaluation and following the Court's visit, a revision of these targets has been proposed on 27/09/2012 under the 8th RDP modification, accepted by the Commission on 13/03/2013.

Box 8 — Italy (Campania)

According to the general state aid rules, which apply to axis 3 of the EAFRD, subsidies of less than 200 000 euro granted to an undertaking over a period of 3 years do not constitute 'State Aid' (so-called 'de minimis' rule). However, the Commission is encouraging Member States not to apply a 100 % aid intensity for private profit-generating projects within this rule.

REPLY OF THE COMMISSION

Box 8 — Sweden

The CMEF result indicators are set at national level. Sweden has, however, 21 counties each of which face different challenges, needs and administrative problems.

The final result indicators' achievements will be collected on the basis of the finalised projects, which mean that these targets are often reached quite slowly, as the realisation of a project may take several years. By the end of 2012 axis 3 was committed at about 76 %, thus significant progress has been made between 2010 and 2012.

42.

See reply to paragraph 29.

The application of selection criteria or equivalent targeting mechanism is examined by the Commission in its audit missions. Several observations in this regard have been made to the Member States concerning rural development measures. If needed, the Commission proposes financial corrections.

Czech Republic: See replies to paragraph 30 and 31.

43.

See reply to paragraph 42.

Czech Republic: The Commission, in the light of its competences and responsibility, has undertaken the necessary steps for ensuring that the targets set by the CZ are now more appropriate.

In the Annual Review meetings¹⁴ in 2011 and 2012, the 'Commission pointed to the unbalance between the fulfilment of the targets for output indicators and the amounts committed and reiterated that adaptation of indicators can be done only if no other action is possible to ensure that the targets are achieved. The Commission emphasised that priority should be given to projects which create jobs.'

The Commission has accepted a reduction in the targets for gross number of jobs because it became clear that the initial targets were more ambitious than realistic, and that due to the economic and financial crisis such targets would not be achieved.

¹⁴ In relation to measure 311 (code in CZ RDP: III.1.1 'Diversification into non-agricultural activities') and measure 313 (code in CZ RDP: III.1.3 'Encouragement of tourism activities').

50.

Demonstration of economic viability of the enterprises supported for an investment is not a requirement under Council Regulation (EC) No 1698/2005. Furthermore, the administrative checks on applications mentioned in Article 24(2) of Regulation (EC) No 65/2011 do not require MS to establish the economic viability of projects.

The requirement is to identify needs in the RDP in relation to the SWOT analysis of the area concerned, hence to target support according to identified territorial needs and structural weaknesses.

Box 9 — France (Aquitaine)

The Commission will follow up this case.

52.

The requirement to target investment support (Article 43 of Commission Regulation (EC) No 1974/2006) was introduced explicitly in this programming period, among other aspects, to counter deadweight and displacement effects.

Box 10 — Italy (Campania)

It is the responsibility of the managing authority to ensure an adequate proportionality between the investments (which would contribute to deliver environmental benefits) to be supported and the score attributed according to the selection criteria.

53.

The legislation did not foresee an a priori assessment of whether or not the applicants would be in need of a subsidy. The requirement is to identify needs in the RDP in relation to the SWOT analysis of the area concerned, hence to target support according to identified territorial needs and structural weaknesses.

The assessment of deadweight is complex and should be part of the evaluation of programmes.

REPLY OF THE COMMISSION

55.

In the context of the axis 3 measures of the EAFRD, the legislation provided that the general state aid rules apply for support under Article 52 of Regulation (EC) No 1698/2005 and for Leader when delivering on axis 3. These rules require that expenditure is eligible from the submission of the aid application. This requirement is stated in the state aid rules to establish the necessary incentive element.¹⁵ The same rules should apply to co-financed measures as for separate aid schemes notified under the state aid regime.

Furthermore, the support to projects should be granted on the basis of the assessment of whether the project contributes to the objectives of the RDP.

Taking account of the beneficiaries' financial capacity in isolation to assess deadweight may entail the risk of supporting non-viable projects and increased administrative costs for the authorities and increased administrative burden for the beneficiaries.

The Commission, however, encourages Member States to apply systems that reduce the risk of deadweight.

57.

See reply to paragraph 53 and 83.

58.

The Commission considers that if the investment support is well targeted (using among others eligibility and selection criteria, differentiation in aid rates) and based on clearly identified gaps/needs¹⁶, the risk of deadweight and displacement is minimised. The targeting of investment support (Article 43) was introduced in this programming period exactly to limit deadweight and displacement effects coming out of earlier evaluations.

The Commission does not consider that in case a subsidy leads to increase of the marketing share at the expense of a competitor a priori is economically inefficient. The support e.g. may have led to more efficient (economically and/or environmentally) businesses which may contribute to the overall development of the rural economy.

¹⁵ Article 8 of Commission Regulation (EC) No 800/2008. Its paragraph 2 states: Aid granted to SMEs, covered by this regulation, shall be considered to have an incentive effect if, before work on the project or activity has started, the beneficiary has submitted an application for the aid to the Member State concerned.

¹⁶ Article 43 of Commission Regulation (EC) No 1974/2006.

59.

The Commission considers that axis 3 measures have been designed in order to ensure an adequate support for the diversity of rural areas as identified in the RDPs according to the NSPs (please see reply to point 18). The *ex ante* analysis of the sectors suitable for farm diversification could help potential beneficiaries in developing niche products and services. The support granted by axis 3 measures is meant to spur the local development with the aim to overcome the rather negative economic conditions existing in many rural areas. The support to be given to disadvantaged rural areas is conceived for ensuring better living conditions by satisfying identified needs in relation to local development and improving the existing socioeconomic situation.

See also reply to paragraph 58.

The measurement of displacement should cover many factors and it is more appropriate to be done at project level.

61.

Some of the MS are in a stage of development of their rural areas such that consideration of saturation points, oversupply and displacement are not relevant because economic activities are generally missing or strongly insufficient. Therefore, in these cases, it seems to be more appropriate to evaluate the displacement at the time of *ex post* evaluation.

The fact that the selection of projects in some of the audited cases takes place at local level should normally contribute to limit the displacement effects, as displacement is most appropriately measured at project level.

REPLY OF THE COMMISSION

62.

See reply to paragraph 83.

Any analysis on displacement should be thorough and detailed. Its results should not lead automatically to defending national/regional/local monopolistic situations and it should rather be oriented towards the stimulation of the healthy competition between businesses with similar activities for offering high quality products/services/activities to potential consumers. In this context, attention should be paid to quality of the services or products provided by competitors, prices, development strategies that have been or are followed, recent investments by competitors, type of structures and organisational and management matters, etc., before concluding that there have been any displacement effects.

Box 12

See reply to paragraph 83.

Box 12 — Sweden

See reply to paragraph 62.

Business development and investments linked to physical development are often done in stages. Entrepreneurship and healthy competition should not be penalised nor customers should remain without a choice when making decisions, thus businesses should be allowed to introduce innovative ideas related to their medium to long-term sustainability and competitiveness, including their expansion. Often, such expansion is done in stages and not in one go.

63.

According to the principles of subsidiarity and shared management, the selection of projects falls under the responsibility of the Member States and the Commission cannot assess the reasonableness of costs of individual projects *ex ante*.

65.

The Commission confirms that it has decided a financial correction for France because of weaknesses in the verification of the reasonableness of costs for which have been found evidence in one region in France in which concerned measures were 121 and 323. Furthermore, the Commission services found during a mission in 2013 similar weaknesses in another region in France which are currently being discussed with the French authorities in the clearance of accounts procedure.

66.

Following the Court's audit, the regional authorities took action in order to improve the verification of the reasonableness of the costs during the on-the-spot checks (new check lists).

As answered by the Czech authorities, there are a number of positive elements (price catalogues for building and construction, cost limits for the renewable energy projects).

Box 13 — Sweden

The estimation of the reasonability of costs is not necessarily made on the basis of comparison of offers but can be made by other means like reference costs (Article 24.2d of Regulation 65/2011). The Commission will analyse this aspect.

Box 13 — Italy (Campania)

In the case mentioned by the Court, the professional fees that have been considered excessive compared to the given professional advice are in line with the indications given by the professional corporation and the national provisions on the admissibility of general costs. The regional authority has specified that a number of different consultancy services have been provided against that payment. The Commission will follow up this case.

REPLY OF THE COMMISSION

67.

The Commission is encouraging MS (e.g. in monitoring committees and in annual review meetings) to shorten the delay for project approval and payment to beneficiaries, and is informed that the situation is improving. However, it is Member States' responsibility to ensure efficient delivery mechanisms and well-functioning administrative procedures at national/regional level.

68.

See reply to paragraph 67.

Box 14 — Poland

Difficulties encountered in implementing measure 312 in Poland have in the past been discussed both during monitoring committee sessions and annual review meetings with the Commission services.

69.

See reply to paragraph 67.

The Commission has been informed that action has since been taken to reduce the processing time in the MS mentioned by the Court.

Sweden: The implementation of axis 3 measures was regularly discussed in the monitoring committees' meetings and the annual review meetings. In the autumn of 2012 the managing authority has fixed maximum delays for the handling of the applications (4 months) and also for the processing of the payments (90 days).

Box 15 — Italy (Campania)

As underlined by the regional authorities, the procedure for granting the advance payment to the beneficiaries and for releasing the insurance policy guaranteeing the amount requested by the beneficiaries as an advanced payment has been revised by the paying agency (AGEA).

71.

For the next programming period 2014–20 the Commission is foreseeing further reduction of the administrative burden in the form of introducing simplified costs. As a result, the processes of claiming, administering and auditing reimbursement for payments made will be easier for both the beneficiaries and the administration itself.

72.

For the purpose of measuring the effectiveness and efficiency of rural development spending, the Common Monitoring and Evaluation Framework has been developed in 2006 and Member States were requested to set relevant targets and expected output indicators to each measure programmed under the EAFRD for the programming period 2007–13.

74.

The Commission has addressed the question of reliability of indicators in several cases; in the context of examination of the annual reports, annual review meetings and at the meetings of monitoring committees.

To compile result indicators such as 'increase of gross value added (GVA)', MS have been invited¹⁷ to capture relevant information on GVA from the supported enterprises when the application is approved and 2 years after the investment completion in order to integrate as much as possible the long-term effect of the investments.

In the preparation of the monitoring and evaluation system for the next programming period 2014–20, account is being taken of weaknesses observed during this period. Therefore, indicators will rather be assessed as part of the RDP evaluation. It will also be done by developing more precise explanatory documents (fiches) for each indicator to avoid potential inconsistencies in data collection through misinterpretation.

¹⁷ Working document providing guidance to MS for the result indicator 'increase of GVA': http://enrd.ec.europa.eu/app_templates/filedownload.cfm?id=84053593-C697-FF89-ED5C-51797D9754FD.

REPLY OF THE COMMISSION

76.

See reply to paragraph 74.

Box 16

The Commission will address the regional authority for further clarification on this point.

77.

See reply to paragraph 74.

In respect of the principles of subsidiarity and shared management, the CMEF handbook describes globally the monitoring and evaluation tasks but also offers some flexibility to MS on how they implement their monitoring and evaluation. MS should identify the right balance to ensure good quality data at an acceptable cost in terms of monitoring procedures.

Box 17

See reply to paragraph 74.

79.

See reply to paragraph 74 and 83.

80.

Italy (Campania): The regional authorities consider that the audited projects are pertinent with the objectives of the measures and contribute to reach the overall objectives set down for axis 3 in terms of diversification of rural activities into non-agricultural activities. This is also the case for projects number 2 and 3 cited by the Court. In the case of project number 3 the regional authorities maintained the position that the refurbishment of the external court yard is linked to the diversification projects '*fattoria didattica*' because it is essential for ensuring a proper access to the farm.

The Commission will analyse this case.

82.

Estimation of GVA increases is a complex issue, because beneficiaries may need time to stabilise their new or expanded economic activity. Short delays between project realisation and time for assessment may result in underestimation of the GVA increase. Furthermore, attention should be paid to the type of investment as some investments may not lead to immediate or a direct GVA increase (e.g. signposting, information centres, marketing studies, etc.).

83.

The assessment of deadweight and displacement can be better established at evaluation stage.

As regards deadweight, and in relation to the 20 projects marked by the Court with a 'strong' label for indications of deadweight in Annex II, the EU legislation provides that the general state aid rules for the support provided under Article 52 of Council Regulation (EC) No 1698/2005 and for Leader when delivering on axis 3. These rules stipulate that that expenditure is eligible from the submission of the aid application. This requirement is stated in the state aid rules to establish necessary incentive element.¹⁸ The same rules should apply to co-financed measures as for separate aid schemes notified under the general state aid regime.

See also replies to paragraph 52, 53 and 55.

As regards displacement see replies to paragraph 58, 59, 61, 62 and Box 12.

Economic situation changes over time, especially with the entry of the economic and financial crisis in 2008–09. It is therefore possible that *ex ante*-made assumptions do not fully realise within the course of the projects' implementation. Moreover, for projects aiming at medium to long-term sustainability, these indicators could be reached at a later stage (than immediately after the investment is finalised).

¹⁸ Article 8 of Commission Regulation (EC) No 800/2008. Its paragraph 2 states: Aid granted to SMEs, covered by this regulation, shall be considered to have an incentive effect if, before work on the project or activity has started, the beneficiary has submitted an application for the aid to the Member State concerned..

REPLY OF THE COMMISSION

84.

The Commission considers that safeguarding of existing jobs through support to existing businesses is one of the major value-added aspects of the EAFRD alongside the temporary job creation linked to the implementation of investment projects in certain fields (e.g. construction activities). The 5-year durability period also ensures that a certain safeguarding element exists for every supported project.

Indeed, there is no common indicator such as 'Number of jobs maintained', but managing authorities are invited to define additional indicators relevant for their RDP. It should be considered that the current set of common indicators is already numerous and many MS have requested a simplification and reduction of the CMEF indicators for the next programming period.

CONCLUSIONS AND RECOMMENDATIONS

86.

The EU legal framework, which is currently in place, provides for a broad scope and purpose of the measures, which provides for a large flexibility in implementation.

When approving the RDPs, the Commission carries out an analysis to assess that programmes and measures are consistent with the Community strategic guidelines, relevant national strategy plans and comply with the relevant legal provisions¹⁹.

The Commission takes the view that needs and opportunities were described with sufficient clarity to make programming of the audited measures appropriate and possible even if the analyses in question could have been improved in some cases.

According to the principles of subsidiarity and shared management, setting up the selection criteria and project selection lies within the responsibility of Member States. The Commission has no role in the ongoing selection of projects.

However, lessons have been learned which will be applied for the next programming period 2014–20 especially through guidance within the programming process.

¹⁹ Council Regulation (EC) No 1698/2005 and Commission Regulation (EC) No 1974/2006 (Article 18 of Council Regulation (EC) No 1698/2005.

For the next programming period 2014–20, the Commission has also proposed the merger of these three measures into one single measure, better beneficiary focus, improved eligibility conditions and better rules for payments reducing the administrative burden that could be associated with these measures. The co-legislators will define the final scope of the proposed new single measure.

87.

Axis 3 measures play a role in safeguarding businesses and work places, and for the creation of conditions for sustainable growth in rural areas.

In its supervisory role, the Commission has insisted throughout the programming period on the need for greater selectivity²⁰ and targeting in the implementation of the measure.

The application of selection criteria or equivalent targeting mechanism is examined by the Commission in its audit missions. Several observations in this regard have been made to the Member States concerning several RD measures. If needed, the Commission proposes financial corrections.

88.

The targeting of investment support (Article 43 of Commission Regulation (EC) No 1974/2006) was explicitly introduced in this programming period, among other aspects, to counter deadweight and displacement effects.

Support to projects should be granted on the basis of the assessment whether the project contributes to the objectives of the RDP.

See reply to paragraph 55.

The risk of overspending is to be considered. The aid-intensity rates should contribute to reduce such risks.

The Commission is encouraging MS (e.g. in monitoring committees and in annual review meetings) to shorten the delay for project approval and payment to beneficiaries, and is informed that the situation is improving. However, it is Member State's responsibility to ensure efficient delivery mechanisms and well-functioning administrative procedures at national/regional level.

²⁰ For example, during annual meetings, notably at the beginning of the programming period a letter was sent from the Commission to the managing authorities of all programmes inviting them to take into account the importance of well-defined selection criteria for an effective implementation throughout the whole period. Furthermore, in 2009, another letter asked all Member States to make sure that adequate selection criteria are specified and used for the allocation of funds.

REPLY OF THE COMMISSION

The Commission has proposed for the next programming period 2014–20 that the three measures audited by the Court be merged into one single measure with a better beneficiary focus, improved eligibility conditions and better rules for payments reducing the administrative burden that could be associated with these measures. The Commission is foreseeing further reduction of the administrative burden in the form of introducing simplified costs. As a result, the process of claiming, administering and auditing reimbursements for payments made will be easier for both the beneficiaries and the administration itself.

90.

As regards objectives in the current period, Member States must identify the rationale for intervention, the objectives, the scope and actions. Furthermore, there has to be evidence that for investment measures support is targeted on clearly defined objectives reflecting identified territorial needs and structural disadvantages (Article 43 and Annex II of Regulation (EC) No 1974).

When approving the RDPs, the Commission carries out an analysis to assess that programmes and measures are consistent with the Community strategic guidelines²¹, the relevant national strategy plans and that they comply with the relevant legal provisions²².

The Commission, being aware of some weaknesses in the measurability, has proposed, for the next programming period, that appropriate targets should be set for each of the focus areas of the Union priorities, on the basis of common indicators, and that the selected measures in relation to the Union priorities should be based on sound intervention logic supported by an *ex ante* evaluation.

Recommendation 1

The principles of subsidiarity and shared management hands considerable discretion to Member States and regions.

When approving the RDPs, the Commission carries out an analysis to assess that programmes and measures are consistent with the Community strategic guidelines, the relevant national strategy plans and that they comply with the relevant legal provisions.²³

²¹ Council decision of 20 February 2006 on Community strategic guidelines for rural development (programming period 2007 to 2013), 2006/144/EC.

²² Council Regulation (EC) No 1698/2005 and Commission Regulation (EC) No 1974/2006 (Article 18 of Council Regulation (EC) No 1698/2005).

²³ Council Regulation (EC) No 1698/2005 and Commission Regulation (EC) No 1974/2006 (Article 18 of Council Regulation (EC) No 1698/2005).

While noting that the measures subject to audit have wider objectives than just redressing market failures related to barriers to employment and growth, the Commission agrees that the RDPs should present measurable objectives contributing to the policy aims.

The Commission, being aware of some weaknesses in this field, has proposed, for the EAFRD for the next programming period 2014–20, to strengthen the legal framework so that *ex ante* quantified targets are set for each of the focus areas of the Union priorities. The content of the programme shall contain a description of the strategy, and that the selected measures in relation to the Union priorities are based on sound intervention logic supported by an *ex ante* evaluation. Where a proposed programme does not contain such a strategy and adequate targets, the Commission will not approve it.

91.

The principle of subsidiarity and shared management hands considerable discretion to Member States and regions. The adopted EU legal framework is broad and flexible, and the restriction of aid to certain activities only, as well as the selection and approval of projects, lies within the responsibility of the Member States.

The Commission believes it should continue to define basic eligibility conditions at EU level, but that more precise eligibility conditions and selection criteria should be set within individual RDPs. It believes that its proposals for a rural development policy for after 2013 follow this approach. However, the Commission will provide additional guidance in this matter.

92.

The Commission considers there was an improvement in the implementation of the programmes alongside the progress of programming period.

The Commission, being aware of certain problems in this area, has introduced in its proposal for the new EU rural development policy for the next programming period 2014–20 a specific compulsory requirement in relation to the setting up and use of selection criteria (with the exception of some areas of animal-related measures for which such compulsory use may not be appropriate).

REPLY OF THE COMMISSION

Recommendation 2

The broad scope of the audited measures should be recognised, as they not only bring impact on employment and income but also contribute to the sustainability of rural areas.

The Commission has insisted on several occasions during the current programming period on the need for greater selectivity and is prepared to further encourage Member States to apply such an approach.

The application of selection criteria or equivalent targeting mechanism is examined by the Commission in its audit missions and several observations in this regard have been made to the Member States. If needed, the Commission proposes financial corrections.

The Commission agrees with the recommendation and has, in the proposal on the EU rural development policy for programming period 2014–20 foreseen that the selection criteria shall be defined for all measures and shall aim to ensure equal treatment of applicants, better use of financial resources and targeting of measures in accordance with the Union priorities for rural development. The use of selection criteria is proposed to be generally compulsory even in the case where available funds are sufficient, except in the case of some compensatory area and animal-related measures.²⁴

The Commission also agrees that the project selection system of the Member States should take into account the quality of the projects and use a minimum scoring system. The Commission will present guidelines to the Member States on the use of eligibility and selection criteria for the next programming period.

93.

The legislation did not foresee an a priori assessment of whether or not the applicants would be in need of a subsidy. The requirement is to identify needs in the RDP in relation to the SWOT analysis of the area concerned, hence to target support according to identified territorial needs and structural weaknesses.

Therefore, the Commission does not consider the question to the beneficiary of whether he needs the grant as an appropriate tool to assess deadweight. The assessment of deadweight is more complex and should be part of the evaluation of programmes.

The Commission considers that if the investment support is well targeted (using among others eligibility and selection criteria, differentiation in aid rates) and based on clearly identified gaps/needs, the risk of deadweight and displacement is minimised. The targeting of investment support (Article 43 of Regulation 1974/2006) was introduced in this programming period exactly to limit deadweight and displacement effects coming out of earlier evaluations.

As regards the displacement, the Commission does not consider that in case a subsidy leads to increase of the marketing share at the expense of a competitor a priori is economically inefficient. The support e.g. may have led to more efficient (economically and/or environmentally) businesses which may contribute to the overall development of the rural economy.

The Commission has included in the legal proposal for the next programming period requirement that specific needs linked with specific conditions at regional or sub-regional level are taken into account and concretely addressed through adequately designed combinations of measures or thematic subprogrammes.

The Commission has also proposed that appropriate targets are set for each of the focus areas of the Union priorities, on the basis of common result indicators, and that the selected measures in relation to the Union priorities are based on sound intervention logic supported by an *ex ante* evaluation.

²⁴ The legal basis is the proposal for the Rural Development Regulation and its Article 49, as well as the related implementing/delegated acts. See COM(2011) 627 Final/2 dated 19.10.2011.

REPLY OF THE COMMISSION

Recommendation 3

The Commission agrees with the recommendation and is prepared to organise exchange of best practices on the mitigation of deadweight and displacement risks with the Member States.

The legislation provided that the general state aid rules apply for support under Article 52(a) of Regulation (EC) No 1698/2005. These rules require that expenditure is eligible from the submission of the aid application. This requirement is stated in the state aid rules to establish the necessary incentive element to prevent the deadweight.²⁵ The same rules should apply to co-financed measures as for separate aid schemes notified under the state aid regime.

Taking account of the beneficiaries' financial capacity in isolation to assess deadweight may entail the risk of supporting non-viable projects and increased administrative costs for the authorities and increased administrative burden for the beneficiaries.

94.

The risk of overspending is to be considered. The aid-intensity rates should contribute to reduce such risks.

Recommendation 4

The Commission notes that this recommendation is for the Member States and that the principles of subsidiarity and shared management hands considerable discretion to Member States and regions.

The Commission covers the issue of evaluation of the reasonableness of costs during its audit missions on investment measures. It verifies that the Member State has established an effective system to evaluate the reasonableness of costs. Given the complexity of the subject, the Commission will continue to examine the issue during its audit missions. It will also continue the discussions with the Member States outside the Clearance of Accounts framework.

The number of audit missions is limited due to the number of available staff. Therefore, the number and scope of these missions are decided on the basis of a risk analysis.

²⁵ Article 8 of Commission Regulation (EC) No 800/2008. Its paragraph 2 states: Aid granted to SMEs, covered by this regulation, shall be considered to have an incentive effect if, before work on the project or activity has started, the beneficiary has submitted an application for the aid to the Member State concerned.

95.

In the preparation of the monitoring and evaluation system for the future period, account is being taken of weaknesses observed during this period. In practice, it has been difficult for MAs to compile the necessary data and conduct the analysis required to establish values for these types of result indicators (GVA ...) as part of their regular annual monitoring activities. Therefore, for the next programming period, result indicators will rather be assessed as part of the RDP evaluation. It will also be done by developing more precise explanatory document (fiches) for each indicator to avoid potential inconsistencies in data collection through misinterpretation.

The collection of information and the monitoring of projects' implementation lies within the responsibilities of the Member States and the Commission cannot be requested to actively manage this process as it goes against the subsidiarity and shared management principle.

Recommendation 5

Objectives and their targets at programme level are set up by the managing authority as part of the programme strategy. At the project level estimated/predicted results/outcomes by which the project in question will contribute to the programme objectives are set *ex ante* by potential beneficiaries in their applications. However, there are always uncertainties and external factors in the achievement of the targets set, so the targets should also be able to be adjusted accordingly, if need to be.

The Commission agrees with the recommendation and is taking care that in the preparation of the Common Monitoring and Evaluation Framework for the future period, which is currently being elaborated²⁶, weaknesses observed during this period are taken into account. Therefore, for the next programming period, result indicators will rather be assessed as part of the RDP evaluation. It will also be done by developing more precise explanatory documents (fiches) for each indicator to avoid potential inconsistencies in data collection through misinterpretation.

²⁶ The legal basis is the proposal for the Horizontal Legislation art. 110, the proposal for the RD Regulation title VII, as well as the related implementing/delegated acts. See COM(2011) 628 Final/2 dated 19.10.2011 and COM(2011) 627 Final/2 dated 19.10.2011.

REPLY OF THE COMMISSION

For the next programming period 2014–20 the Commission is developing a CMEF, together with the Member States, which will allow the assessment, for each RDP, of progress in implementation against commonly defined target indicators for the priorities and focus areas selected for the programme. At the basis is an indicator plan which for each focus area sets the target and the planned outputs and expenditure for the measures that will be used to achieve the targets and objectives of the programme. The indicator plan represents more accurately the quantified intervention logic for each individual programme than does the current rigid axis structure.

Recommendation 6

According to the principles of subsidiarity and shared management it is for the Member States to ensure efficient delivery mechanisms and well-functioning administrative procedures at national/regional level.

The Commission is encouraging MS in different contexts (e.g. in monitoring committees and annual review meetings) to shorten the delay for project approval procedures and payments to beneficiaries, and is informed that the situation is improving during the current programming period.

For the next programming period 2014–20 the Commission is foreseeing further reduction of the administrative burden in the form of introducing simplified costs. As a result, the processes of claiming, administering and auditing reimbursement for payments made will be easier for both the beneficiaries and the administration itself.

European Court of Auditors

Special Report No 6/2013

Have the Member States and the Commission achieved value for money with the measures for diversifying the rural economy?

Luxembourg: Publications Office of the European Union

2013 — 74 pp. — 21 × 29.7 cm

ISBN 978-92-9241-292-0

doi:10.2865/88553

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DIVERSIFYING THE RURAL ECONOMY IS ESSENTIAL FOR ECONOMIC GROWTH, EMPLOYMENT AND SUSTAINABLE DEVELOPMENT IN RURAL AREAS. THIS REPORT CONCLUDES THAT THE COMMISSION AND THE MEMBER STATES HAVE, ONLY TO A LIMITED EXTENT, OBTAINED VALUE FOR MONEY THROUGH THE FUNDING OF THE MEASURES AIMED AT DIVERSIFYING THE RURAL ECONOMY. THIS WAS DUE TO A LACK OF A CLEAR DEMONSTRATION OF THE NEED FOR SUPPORT, THE ABSENCE OF SPECIFIC OBJECTIVES, AND EXCESSIVELY BROAD ELIGIBILITY AND SELECTION CRITERIA. MEMBER STATES DID NOT TAKE ADEQUATE STEPS TO MITIGATE THE RISKS OF DEADWEIGHT, DISPLACEMENT AND OVERSPENDING RESULTING IN AN INEFFICIENT USE OF RESOURCES. THE ECA MAKES RECOMMENDATIONS TO HELP THE COMMISSION AND MEMBER STATES REMEDY THESE WEAKNESSES.



EUROPEAN COURT OF AUDITORS



Publications Office



ISBN 978-92-9241-292-0



9 789292 412920