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HAS THE EU SUPPORT TO THE FOOD-PROCESSING INDUSTRY BEEN EFFECTIVE AND EFFICIENT IN ADDING VALUE TO AGRICULTURAL PRODUCTS?

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

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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).

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

CMEF: Common Monitoring and Evaluation Framework.

Community strategic guidelines: With these strategic guidelines the Council identifies the European Union's priorities under the European Agricultural Fund for Rural Development (EAFRD). 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.

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

MTE: Mid-term evaluation report.

Multi-annual supply contract: Type of contract that establishes the terms of business between an agricultural producer and a processor or distributor over a period of several years.

Measure 123: The measure for 'adding value to agricultural and forestry products'.

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.

As part of the EU's rural development policy grants are made available to enterprises that process and market agricultural products through a measure called 'Adding value to agricultural and forestry products' that aims to improve the competitiveness of agriculture and forestry. For the current programming period, 2007–13, the EU budget for this measure is some 5,6 billion euro. This financing is complemented by national spending, which brings the total public funding to 9 billion euro.

II.

The Court's audit examined whether the EU support had been effective and efficient in adding value to agricultural products. In particular, the Court questioned whether the measure was designed and implemented in a way that provides for the efficient funding of projects addressing clearly identified needs and whether the measure is monitored and evaluated in a way that allows its results to be demonstrated.

III.

As is to be expected, the projects mostly improved the financial performance of the companies concerned and a number of the projects audited may result in some added value. This, however, could not be attributed to the design of the measure or the selection procedures used by the Member States. There was a lack of evidence to demonstrate that the companies aided needed a subsidy, or the specific policy objectives that the subsidy was expected to achieve. The Court concludes that the support has not been systematically directed to projects that effectively and efficiently add value to agricultural products.

EXECUTIVE SUMMARY

IV.
Member States must draw up Rural Development Programmes (RDPs) tailoring the aid to their needs through national or regional objectives and setting the scope of the measure to ensure that efficient use is made of the funding available. However, the Court found that only general objectives were set, which did not demonstrate how the funding was intended to add value to agricultural products or improve the competitiveness of agriculture. Despite this lack of specificity, the Commission approved the programmes.

V.
Member States should set eligibility criteria to limit the type of investment or beneficiary eligible for funding and then selection criteria to identify the most effective and efficient projects to be supported. The audit found that eligibility criteria were set that allowed almost any food-processing company to be eligible. Furthermore, selection systems were poor or non-existent and while there were sufficient resources — which is often the case at the beginning of a programming period — were not applied at all.

VI.
The Court found that Member States do not direct the funding to projects for which there is a demonstrable need for public support. Without this, the measure risks becoming a handout — a general support to enterprises investing in the food-processing sector — with the attendant risks of distortion of competition and waste of scarce public money.

VII.
Almost a fifth of the EU budget for improving the competitiveness of agriculture is paid to food-processing companies but the effects on the competitiveness of agriculture can only be indirect and there is no clear intervention logic. However, the monitoring and evaluation arrangements do not collect information on added value or on the effects on competitiveness of agriculture. Consequently, the current arrangements are unlikely to provide the information necessary to demonstrate the success or otherwise of the funding allocated to the measure or to provide a basis to assess the effectiveness of the measure when programming rural development measures for the 2014–20 period.

VIII.
The Court therefore recommends that:

(a) Member States' programmes clearly identify the need for funding and set objectives that are meaningful and measurable; the Commission should only approve programmes that do so.

(b) Selection criteria should be defined that enable the most effective projects to be identified. To ensure that the EU funds are used efficiently, these criteria should be rigorously applied, even when there is sufficient budget available to finance all eligible projects.

(c) The Commission and Member States should promote the adoption of best practices in respect of the mitigation of deadweight and displacement risks.

(d) The monitoring and evaluation framework applicable to the projects financed should be improved for the forthcoming programming period to ensure that the effectiveness of the funds spent can be properly measured.

INTRODUCTION

1. As part of the aid given for rural development under pillar 2 of the common agricultural policy (CAP), provision is made for a specific measure 'Adding value to agricultural and forestry products' (hereafter 'measure 123'). Measure 123 contributes to the axis 1 objective of improving the competitiveness of agriculture and forestry as introduced by Regulation (EC) No 1698/2005 (see ***Box 1***)[1].

2. Through measure 123, public money is made available to enterprises with fewer than 750 employees or less than 200 million euro turnover that process and market agricultural and forestry products. Support is given to fund investments that should add value to those products. This should ultimately benefit the competitiveness of agriculture, for example by developing new market opportunities for agricultural products[2]. Secondary benefits may include creating jobs in rural areas and environmental improvements.

3. Having regard to the requirements of the relevant regulations set at EU level, Member States draw up Rural Development Programmes (RDPs), at national or regional level, in which they define a strategy and propose the measures they wish to use to address their identified needs. The RDPs only become operational after the Commission has approved them. EU and national funds should then be channelled to investment projects through measure 123 by using eligibility and selection criteria. The following figure describes the different stages of the decision-making process leading to the financing of an investment project with measure 123 funds.

[1] Axis 1: improving the competitiveness of the agricultural and forestry sector; axis 2: improving the environment and the countryside; axis 3: improving the quality of life in rural areas. 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) and 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).

[2] For enterprises that are not small or medium-sized (i.e. with fewer than 250 employees and less than 50 million euro turnover) the maximum rate of support is halved.

BOX 1

EXTRACT FROM REGULATION (EC) NO 1698/2005

Axis 1

Improving the competitiveness of the agricultural and forestry sector

Article 20

Measures

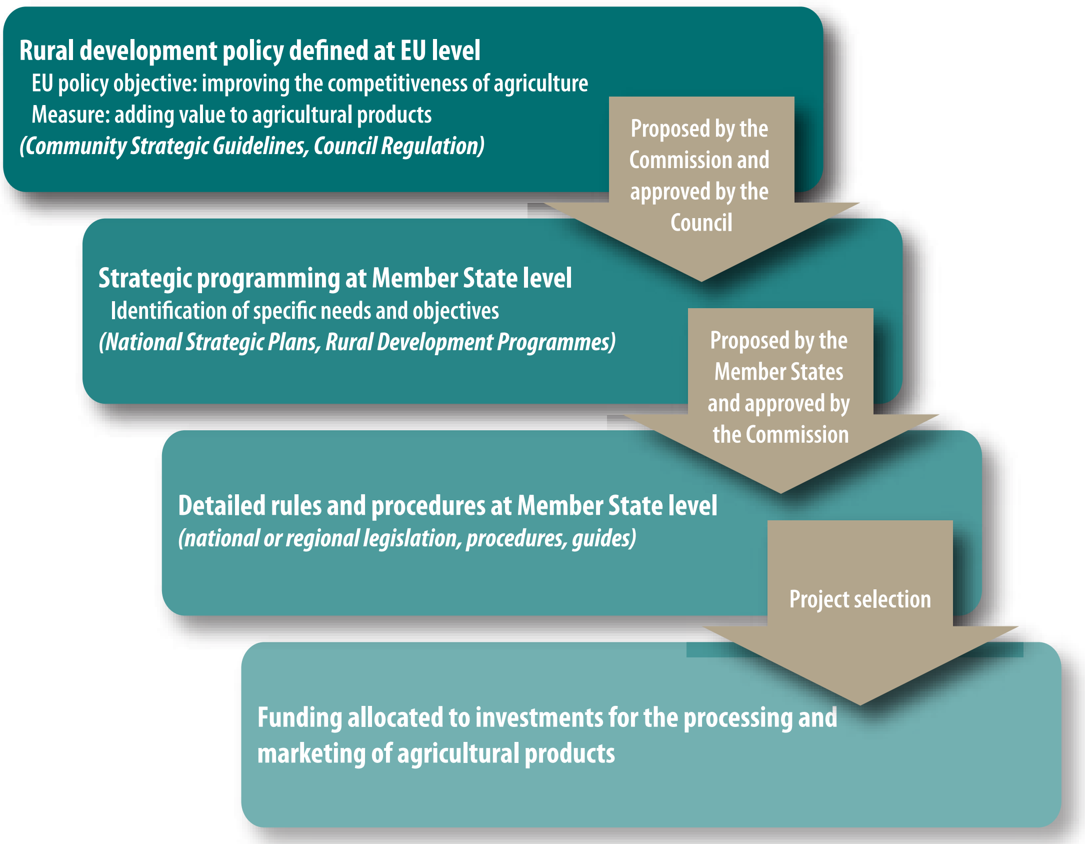
Support targeting the competitiveness of the agricultural and forestry sector shall concern: ... (b) measures aimed at restructuring and developing physical potential and promoting innovation through: ... (iii) adding value to agricultural and forestry products.

4. EU aid is co-financed with national public money and the total public expenditure on the measure will be some 9 billion euro. The measure is used principally to give grants towards the beneficiaries' investment costs. Member States may determine the aid rate, within limits. Most grants are for between 20 % and 50 % of the companies' total eligible investments.

5. The EU budget for the period 2007–13, for measure 123, totals 5,6 billion euro. This represents 5,9 % of the planned EU expenditure on rural development and 18 % of the total allocated for improving the competitiveness of agriculture and forestry (axis 1)[3]. The ***Figure*** in ***Annex I*** shows the programmed EU funds by Member State and the financial implementation as at the end of 2011. At that date, 35 % of the planned expenditure for the period had been spent.

[3] European Union, Directorate-General for Agriculture and Rural Development, 'Rural Development in the European Union — Statistical and Economic Information, Report 2011', section 4.3.4 ('Main Rural Development Instruments funded by EAFRD').

FIGURE



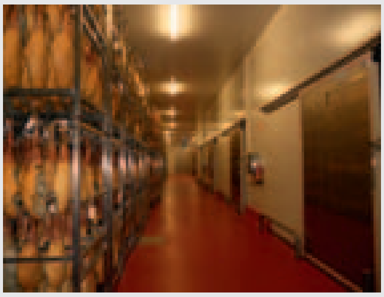
6. As only about 5 % of the approved expenditure for the measure relates to forestry projects, this audit focused on support granted for adding value to agricultural products. The investments financed are generally made by start-up or existing businesses for new or improved plant and machinery or for the construction of new facilities to process and market agricultural products (see ***Box 2***).

BOX 2

EXAMPLES OF THE TYPES OF INVESTMENTS FINANCED BY MEASURE 123

Investments financed included milling equipment for the production of olive oil …

… equipment for drying ham, and …



… systems for modernising milk processing.

AUDIT SCOPE AND APPROACH

7. The Court sought to assess whether the measure was designed and implemented in a way that provides value for money and whether the projects financed achieved the objectives of the measure. Furthermore, the Court assessed whether the results of the measure as a whole were appropriately monitored and evaluated to allow the Member States and the Commission to identify and react to any problems encountered and to provide objective information on the measure's achievements.

8. The overall audit question was:

Has the EU support to the food-processing industry been effective and efficient in adding value to agricultural products?

The main sub-questions were:

— Has the measure been designed in a way that provides for the efficient funding of projects addressing clearly identified needs?

— Have Member States implemented the measure with due regard to value for money?

— Have the Commission and the Member States appropriately monitored and evaluated the results of the measure?

9. In the context of this audit, projects were considered as effective, if they were sustainable and contributed to specific RDP objectives for the measure as well as adding value to agricultural products. The funding was considered to be efficient if deadweight was limited and any displacement was justified[4].

10. The Court's audit covered six national and regional rural development programmes (RDPs), selected mainly for their size: Spain (Castilla y León), France, Italy (Lazio), Lithuania, Poland and Romania. In France, the national RDP is implemented regionally and the Rhône-Alpes region was selected for this audit.

[4] Deadweight refers to the extent to which a beneficiary would have undertaken the investment even in the absence of public financial support. Displacement is the degree to which an activity promoted by public support is offset by reductions in activity elsewhere.

11. The audit work comprised a review of the RDPs, an examination of the Member States' management systems and separate audit visits to 24 completed food-processing projects in these Member States, including four projects nominated by the Member States as best practice examples. The remainder were selected by the Court to give a range of projects typical of those financed in the Member State concerned. A list of the projects audited is in ***Annex II***. The Court also reviewed the mid-term evaluation reports for 23 RDPs (see list in ***Annex III***).

OBSERVATIONS

PART ONE

HAS THE MEASURE BEEN DESIGNED IN A WAY THAT PROVIDES FOR THE EFFICIENT FUNDING OF PROJECTS ADDRESSING CLEARLY IDENTIFIED NEEDS?

12. Good design of the measure is essential for sound financial management. The measure grants public support to investments by private enterprises in the food-processing and marketing sector. These enterprises have their own motivations and objectives, which may coincide with the EU's policy objective of improving the competitiveness of agriculture (see paragraph 15), but this is not automatic. The sector is considered to be one of the world's most competitive and innovative[5]. Providing funding to such companies should therefore be in response to a clearly identified need. The need for public intervention has to be established and the logic for how this will improve the competitiveness of agriculture explained.

13. Clear and specific RDP objectives reflecting the particular needs of the Member State or the region are therefore a prerequisite for effective project selection and to provide a basis for accountability, to demonstrate what should be and later what has been achieved[6]. If specific needs for public intervention have not been identified and RDP objectives are too general, this may give rise to the selection of projects which provide little or no contribution towards improving the added value of agricultural produce and thereby improving the competitiveness of agriculture.

14. The Court reviewed EU legislation, RDPs and Member State systems, procedures and documents to obtain evidence as to whether the design of measure 123 at both EU and Member State level was likely to lead to the efficient funding of effective projects addressing clearly identified needs.

[5] Council Decision 2006/144/EC.

[6] Article 43 of Commission Regulation (EC) No 1974/2006 of 15 December 2006 laying down detailed rules for the application of Council Regulation (EC) No 1698/2005 on support for rural development by the European Agricultural Fund for Rural Development (EAFRD) stipulates, 'For investment measures, Member States shall ensure that support is targeted on clearly defined objectives reflecting identified structural and territorial needs and structural disadvantages' (OJ L 368, 23.12.2006, p. 15).

THE LEGISLATION PUTS THE ONUS ON MEMBER STATES TO ENSURE THAT THE MEASURE IS EFFECTIVE AND EFFICIENT ...

15. Objectives are defined in the EU legislation only at the level of the rural development policy axes, in this case axis 1, with the objective of improving the competitiveness of agriculture[7]. Measure 123 aims to contribute to this through adding value to agricultural products that are processed or marketed following the investments made. The legislation itself does not specify what the added value is intended to be (purely financial, from an environmental or a quality standpoint, etc.) nor to whom such added value should accrue.

16. A similar measure existed in the previous programming period 2000–06[8], which stipulated: 'Investment must contribute to improving the situation of the basic agricultural production sector in question. It must guarantee the producers of such basic products an adequate share in the resulting economic benefits.' Similar rules also existed under earlier support schemes[9].

17. There are no such requirements in the current programming period. The regulation[10] requires investments in processing and marketing to 'improve the overall performance of the [supported] enterprise', i.e. the legislation only specifies that there should be a benefit to the individual food-processing and marketing enterprises concerned.

18. The removal of the previous requirement that the aid should improve the situation for agricultural producers and the absence of prescription on how the measures are to add value are intended to simplify the legal texts and allow Member States to define the measure in a way that best meets their circumstances and needs. Consequently, the onus is on Member States to ensure that the measure results in improved added value and achieves benefits for the competitiveness of agriculture. The Commission, when approving the RDPs, should ensure that this is the case.

[7] Article 4 of Regulation (EC) No 1698/2005.

[8] Article 26 of Council Regulation (EC) No 1257/1999 of 17 May 1999 on support for rural development from the European Agricultural Guidance and Guarantee Fund (EAGGF) and amending and repealing certain Regulations (OJ L 160, 26.6.1999, p. 80).

[9] Article 9(1) of Council Regulation (EEC) No 355/77 of 15 February 1977 on common measures to improve the conditions under which agricultural products are processed and marketed (OJ L 51, 23.2.1977, p. 1); Article 12(1) of Council Regulation (EEC) No 866/90 of 29 March 1990 on improving the processing and marketing conditions for agricultural products (OJ L 91, 6.4.1990, p. 1); Article 12(1) of Council Regulation (EC) No 951/97 of 20 May 1997 on improving the processing and marketing conditions for agricultural products (OJ L 142, 2.6.1997, p. 22).

[10] Article 28(1)(a) of Regulation (EC) No 1698/2005.

… BUT MEMBER STATE RDPs DO NOT CLEARLY JUSTIFY THE NEED FOR THE MEASURE

19. Through the ongoing process of the simplification of EU law and the principle of subsidiarity, EU legislation has evolved to be quite general and non-prescriptive, as described above. However, Member States' RDPs at either national or regional level, are required by the legislation[11] to be more specific. RDPs have to be approved by the Commission, which has overall responsibility for the efficient and effective spending of the EU budget.

20. Specifically, RDPs are required to analyse the existing situation in terms of strengths and weaknesses and to develop a strategy in relation to them. The RDP must provide evidence to show that the support is targeted on clearly defined objectives reflecting identified territorial needs and structural disadvantages. Furthermore the RDPs should identify the rationale for the intervention and define the types of investments and beneficiaries that would be eligible for support. If done well, this should result in an effective and efficient programming of the measure.

21. However, the RDPs audited did not identify specific needs for intervention in the food-processing sector, such as instances where the possibilities to add value to agricultural products were hindered by inadequate processing capacity. Where needs were identified, they were of a very general nature. For example in Poland, the RDP stated 'Support of agricultural products processing is of crucial importance because the sector is one of the most important branches of Polish economy.' The RDPs did not show why public support was necessary and how it could achieve the desired change. The rationale for the measure was therefore missing and the objectives set were necessarily general and were not clearly linked to the regional strengths and weaknesses identified nor to a clearly identified need for intervention. They were often verbatim copies of the EU objectives, or slightly modified recitals of those objectives (see ***Box 3*** for some examples).

[11] Article 5 of Regulation (EC) No 1974/2006.

22. A final step in programming is to define the eligibility conditions — the types of investments, the categories of beneficiaries and the nature of the support — to ensure that the aid is directed to the specific objectives that have been set. Despite the lack of specific objectives, all RDPs set at least some eligibility conditions. In the case of France, the Rhône-Alpes programming document stated that the entire food-processing sector was eligible throughout the region's territory with the exception of sugar and milk substitutes. Other Member States, Spain (Castilla y León) and Lithuania in particular, went further in defining specific eligibility conditions. Lithuania excluded most new construction in sectors that had received support under previous programmes, such as new slaughterhouses or milk processing plants, as there was already sufficient capacity. In Spain (Castilla y León), wine-related projects were eligible only if they concerned wines with a geographical indication of origin, for example.

23. These eligibility conditions have the effect of restricting the scope of the aid to some extent. However, almost all major food sectors remain eligible, with the risk that the aid will not be sufficiently targeted.

BOX 3

EXAMPLES OF OBJECTIVES SET FOR MEASURE 123

The objective identified in the RDP of Castilla y León is 'to improve the processing and marketing of the products of the primary and forestry sectors through investments to improve the efficiency, renewable energies, new technologies and new market opportunities.' These elements are taken from recital 23 of Regulation (EC) No 1698/2005, without any further specification.

The national RDP of France sets the objective of the measure as 'to improve the competitiveness of the agri-food industry.' This general formulation allows specific objectives to be established at regional level. However, the region Rhône-Alpes, audited by the Court, did not do so.

THE COMMISSION APPROVED RDPs DESPITE WEAKNESSES

24. 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. However, as the RDPs audited defined objectives in such general terms, this check of consistency is not very meaningful.

25. The Commission's procedures to assess RDPs do not contain any verification that the Member State or region is strategically targeting measure 123 support to where public intervention is needed. No checks are made on the rationale for intervention. The Commission does not assess how effectively or efficiently the proposed measure will generate an added value for agricultural products and improve the competitiveness of agriculture.

26. Despite the weaknesses described in paragraphs 21 to 23 above, the Commission approved the RDPs in question. Once an RDP is approved by the Commission and EU funds are made available to the Member State, it is more difficult for the Commission to retroactively ensure that the measures will be effective and efficient[12].

27. The audit has shown that the design and the programming of the measure has not sufficiently addressed the risks that follow from paragraphs 12 and 13. This makes it more important — but also more difficult — for Member States to avoid the risks and ensure effectiveness and efficiency when selecting the individual projects for support. This issue is covered in the next part of this report.

28. A second consequence is that there is not a satisfactory basis for monitoring and evaluation and for accountability. This issue is covered in part III.

12 See paragraphs 33 to 37 of Special Report No 8/2012 (http://eca.europa.eu).

PART TWO

HAVE MEMBER STATES IMPLEMENTED THE MEASURE WITH DUE REGARD TO VALUE FOR MONEY?

29. To make best use of public money, when implementing the measure Member States should:

— ensure, prior to granting funding, that applicants demonstrate the financial sustainability of the project;

— ensure that support goes to projects that offer the best results in adding value to agricultural products;

— mitigate the risks of deadweight and displacement.

CHECKS GIVE LIMITED ASSURANCE ON THE FINANCIAL SUSTAINABILITY OF PROJECTS

30. Although the legislation no longer requires applicants to demonstrate the viability of their enterprises[13], all Member States audited still carry out viability checks on the applicants' financial accounts.

[13] This was formerly stated in Article 26(1) of Regulation (EC) No 1257/1999.

BOX 4

VIABILITY CHECKS: WEAKNESSES IN PRACTICE

Lithuania: The maximum attainable revenue from the investment project (grain drying and storage facilities) operating at full capacity could be calculated at LTL 4 million. The projection of LTL 29 million presented in the grant application was clearly unattainable.

Romania: A sample of 17 application files showed unrealistically high forecasts, with returns on investment of more than 90 % for half of these projects.

Italy (Lazio): As the methodology for assessing the financial projections was public, project promoters knew that if their business plan did not show financial data that met the required minimum values their application would be rejected. Unsurprisingly, no projects were submitted that did not reach the required score. The region's officials did not check the information submitted or evaluate whether the projections were realistic or not. The auditors found that in several cases, sales figures and other financial information had been overstated.

31. The current legislation requires Member States to check that the investment improves the overall performance of the enterprise receiving support. All the audited Member States obtained relevant projections from the applicants showing expected turnover, profits, cashflows, etc. With the exception of France (Rhône-Alpes), the Member States compared these projections to minimum values and rejected projects that did not meet the requirements. However, a common weakness was that Member States relied on the projections made by the applicants without checking that the figures and the underlying assumptions were well-founded and plausible. In particular, projections were not tested for different scenarios to ensure that project proposals were sufficiently robust to withstand foreseeable events, such as downturns in market conditions, for example.

32. The Court found unrealistic assumptions, calculation errors and other inconsistencies in the financial projections that had not been detected by the Member State authorities during the appraisal of the project (see examples in ***Box 4***).

MEMBER STATES DO NOT SELECT PROJECTS WITH THE HIGHEST POTENTIAL BENEFIT

33. As shown in part I, the Member States audited did not identify structural and territorial needs for public intervention and did not set specific objectives for the measure. As a consequence a wide range of potential projects in almost all food sectors was eligible for support.

34. Three main instruments are available to the Member States to ensure that support is nevertheless directed to the projects that best meet the national or regional needs: application of selection criteria, imposing specific conditions and varying the aid rates to give incentives.

SELECTION SYSTEMS

35. Member States are expected to make a selection from within the population of eligible investment projects, using selection criteria related to the objectives set. This is a requirement of the EU legislation. It allows the relative merits of project proposals to be evaluated on an objective basis and for those projects that do not represent value for money to be rejected.

36. Spain (Castilla y León) and Poland have not defined such selection criteria. The selection systems applied in the other four Member States audited are characterised by weaknesses, described below.

37. While most of the selection criteria were relevant to the (albeit general) national and regional objectives for the measure, few concerned the degree to which the projects added value to the agricultural products. Those that did were not highly weighted in the evaluation, with an exception in Italy (Lazio) (see ***Box 5***). In Lithuania and Romania priority was given to criteria unrelated to the effectiveness or efficiency of the project (see ***Box 6***).

BOX **5**

SELECTION CRITERIA RELATED TO ADDED VALUE

Lithuania	Poland	Romania	France (Rhône-Alpes)	Italy (Lazio)	Spain (Castilla y León)
Introduction of innovation (5th priority out of 6)	No selection criteria	Organic production (5 points/100) Traditional products (3 points/100)	None	Organic production (10 points/100) Product innovation (4 points/100) Quality improvements for wine (38 points/100)	No selection criteria

BOX **6**

CRITERIA UNRELATED TO THE EFFECTIVENESS OF THE PROJECT

In **Lithuania**, the first priority is automatically given to applicants that have not previously received a grant, regardless of the quality of the project.

Romania rejects projects that fail to achieve a minimum score of 20 points from the assessment of the selection criteria. One criterion concerns whether the project is in a 'priority sector'. However, all the major food sectors (dairy, meat, cereals, wine, fruit and vegetables) are classed as priority sectors, with scores of 32 to 36 points. Consequently, almost all projects automatically achieve the minimum score.

38. With the exception of Romania, at the time of the audit the EU and national budgets programmed for the measure by the Member States audited was more than sufficient to be able to support every eligible project application. Instead of limiting support to the most effective projects these Member States chose to spend the budget on projects that they had identified as low priority. The selection systems in these Member States have had little or no effect (see ***Box 7***).

SPECIFIC CONDITIONS

39. Member States may define specific conditions to be met by the investment projects to ensure that they will contribute to national and regional objectives. This facility was not widely used in the audited Member States but there were instances in Poland, and Italy (Lazio). In Poland beneficiaries are required as a condition of the grant to conclude multi-annual 'supply contracts' with agricultural producers covering at least 50 % of their supplies. This is intended to improve the situation of farmers by giving them some stability by fixing the quality and quantity of produce to be delivered. Supply contracts are also a condition of the grant in Italy (Lazio).

BOX 7

SELECTION SYSTEMS THAT HAVE LITTLE EFFECT

In **Italy (Lazio)** there is no minimum score so projects have been selected with as little as 15 points out of 100 in the project evaluation, indicating a poor contribution to the region's priorities and objectives.

In **France (Rhône-Alpes)** the national cofinancing is granted by the regional council and/or the local council. The regional council evaluates projects against its own, regional, objectives and rejects projects that do not achieve a minimum score. However, the rejected projects nevertheless received EU funding, as co-financing for these was provided by the local council, which does not operate a formal selection system.

In **Lithuania**, the selection system of prioritisation is only applied if the budget is insufficient to finance all eligible projects — which, at the time of the audit, had not been the case. Projects could therefore be selected even if they did not meet any of Lithuania's six priorities.

INCENTIVES

40. For projects co-financed by the regional council in France (Rhône-Alpes), supply contracts are not an obligation but project promoters may make a voluntary commitment. In return for this, and other commitments such as using local suppliers or creating new jobs, the beneficiary is given an additional 5 % or 10 % aid. How much additional effect this practice leads to is unclear: three of the four beneficiaries visited in this audit met the conditions for the additional aid without having to adapt their projects (for example, the cooperatives already had supply contracts with local suppliers, i.e. their members). The fourth beneficiary (a maker of traditional sausage products) declined the additional aid element as they did not want to be tied to regional suppliers of pork.

41. In Spain (Castilla y León), projects were assessed against evaluation criteria, which determined the aid rate applicable. Several criteria were related to priorities identified in the regional legislation, such as projects that conclude contracts with local farmers or that are related to innovation or organic production. However, only around 2 % of the projects corresponded to each of these criteria. The incentive effect of the evaluation criteria is reduced because of the predominance of criteria related to the size of the company and the food sector: small or medium-sized beneficiaries in sectors such as fruit and vegetables automatically received the maximum 40 % aid rate regardless of the other characteristics of the project. Aid rates for larger companies, which were as low as 3 % in the dairy sector or 7 % in the wine sector, for example, are unlikely to provide sufficient incentive to potential applicants that may have had proposals for effective projects.

ASSESSMENT OF AUDITED PROJECTS

42. The Member States audited[14] did not have information to show if the projects to which they had given financial support were financially sustainable and effective, i.e. that they had achieved specific RDP objectives for the measure and added value to agricultural products.

43. The Court assessed the financial sustainability and effectiveness for the 24 projects as illustrative case studies. The contribution to specific RDP objectives could not be assessed as the RDPs set only very general objectives (see part I). Consequently, projects were considered as 'effective' if they resulted in an added value for agricultural products. The results of this assessment are shown in ***Annex II*** and summarised below.

[14] Lithuania and Poland are exceptions in that the companies had to declare some information on their financial situation after the grant.

44. All of the 24 projects visited by the Court's auditors were financially sustainable at the time of the audit. In two cases, it was too soon to assess the impact of the project on the company's financial results but of the remaining 22 companies, 15 had improved their financial results since the investment. Seven of these had achieved or exceeded their financial targets, and in eight cases, although the targets were not achieved, some improvement in the companies' financial situation had occurred. In seven cases, the company's financial results had deteriorated, although only in one case was the future sustainability of the project at risk. The reasons given were complex but ultimately the projects were insufficiently robust in sometimes unfavourable market conditions.

45. It might be expected that most investments by food processing and marketing companies would result in adding value to agricultural produce as this is the nature of their business. The Court assessed the results of the projects in terms of the value added, including whether new products were created, new market opportunities developed or the quality of existing products improved.

46. The Court found that six of the projects had a clear effect in adding value and classified these as 'high added value' according to the criteria set out in paragraph 45 (although this result may be biased to an extent as the projects in France, Spain (Castilla y León) and Romania were best practice projects nominated by the Member State). These projects had as their main objective to increase added value and included wine producers that moved production to higher quality wines and an olive mill that introduced organic production. Further examples are given in ***Box 8***.

47. A further 12 projects were assessed as medium by the Court for their results in adding value. These were characterised by improvements to product quality that did not affect the sales price, or new products that were small-scale in relation to the investment or of low value. An example is a 1,5 million euro investment by a tomato processing plant in Romania that enabled it to meet hygiene standards and produce a high volume, low cost range of own-label products for supermarket chains.

BOX 8

PROJECTS THAT CLEARLY ADDED VALUE TO AGRICULTURAL PRODUCE

In **Spain (Castilla y León)**, a 1 million euro investment improved the ham drying process by expanding the storage and handling areas and providing new equipment. This allowed the drying times to be increased from 11 months to 18 months, thus improving the quality of the final products and enabling the company to gain certification for authentic 'jamón serrano' and 'jamón ibérico' products. The new equipment also enabled new types of products to be produced with a higher added value — vacuum-packed and boneless dried ham.

In **France**, in a 200 000 euro project a new company purchased equipment for producing vegetable crisps. The company developed new products with a high added value and created new market outlets for organic vegetables produced in the area.

In **Romania**, a 1,1 million euro project by one of the country's leading wine producers invested in modern equipment for wine production, conditioning, bottling and transport. As a result of the project, the company was able to increase the share of quality wines in the total sales. A new high quality brand was introduced, which helped the company expand to external markets.

48. The remaining six projects resulted in little or no adding of value to the agricultural products and were aimed primarily at increasing the capacity and/or efficiency of the processor. Displacement is an issue with these projects in particular (see paragraphs 62 onwards). Examples are given in ***Box 9***.

49. The Court further assessed whether there was a demonstrable benefit to the agricultural producers that supplied the processing and marketing companies concerned. Eight of the 24 projects could demonstrate that the added value at least partly accrued to the agricultural producers. Seven of these were cooperatives. A further seven beneficiaries in Italy (Lazio) and Poland were obliged to conclude supply contracts, which may have had some value for the producers. For the remaining nine projects, the companies could not demonstrate a benefit for their agricultural suppliers.

50. A common, horizontal objective of all the RDPs was to create new jobs in rural areas. While this is not the primary objective of measure 123, projects that create employment in addition to adding value enhance the effectiveness of the measure. Three of the projects had a strong impact on employment, each creating over 20 new jobs (but see paragraphs 62 to 66 for findings on displacement) and nine projects created at least one new job. A further 11 projects had no impact on employment and one project led to a reduction.

BOX 9

PROJECTS THAT ADDED LITTLE OR NO VALUE TO AGRICULTURAL PRODUCE

In **France**, the main element of a cheese company's investment project was a new cutting and packaging line. The company supplied whole cheeses to another processor for packaging. The new line enabled the company to instead sell pre-packaged cheese directly to retailers and thereby capture a higher share of the added value themselves at the expense of the other processor. The final product remained unchanged.

In **Spain (Castilla y León)**, a project that qualified for the maximum 40 % aid rate had no effect on the added value of the product: the investment was a simple increase in storage capacity at a fruit distributor, with the aim of allowing the distributor to capture a greater market share.

In **Romania**, the main element of a milling company's 1,8 million euro project was the purchase of a fleet of 12 lorries for collecting the wheat and distributing the flour products. With a 50 % grant for the purchase of the lorries, the company is able to operate its own fleet of vehicles at a lower cost than the haulage contractor that the company used previously. This, however, has had no impact on the value added to the agricultural produce.

51. Three of the projects also contributed to horizontal environmental objectives through energy and water savings resulting from improved processing equipment and techniques.

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

52. Deadweight refers to the extent to which a beneficiary would have undertaken the investment even in the absence of public financial support. To give a grant in such cases is an inefficient use of the EU and national budgets as it is not needed to achieve the desired effect (i.e. the investment).

53. The primary means of reducing the risk of deadweight is to design and programme the measure such that it is only used where there is an identified need for public intervention. Public support may be needed, for example, where investments are innovative, making it difficult for the investor to raise capital; or where the financial returns are insufficient to justify the full costs of the investment, such as in a project that has mainly environmental benefits. However, as shown in part I, the Member States audited did not identify such needs and did not set specific objectives so the measures were open to all investment projects whether public support was needed or not.

54. A second level at which Member States can mitigate the risk of deadweight is in the project selection process. The Member States audited all obtained detailed information about each beneficiary's financial situation and the costs and financial projections for the investment. This was used to check the requirement that the investment would improve the overall performance of the beneficiary company. In doing so, the Member States could also check whether the applicant needed a grant for the project to be viable and whether the applicant had sufficient capital or access to capital to finance the entire project. None of the Member States audited did so.

55. In Lithuania the opposite occurred: project applications that showed a high rate of return on the investment were given priority. Yet these were likely to be the projects with the least need for support. In Romania, many business plans showed very high rates of return. Although these projections appear unrealistic the Romanian authorities accepted them without questioning why a project with a 90 % return on investment needed public support. Similarly in Spain (Castilla y León), the projects' financial data evaluated by the authorities showed rates of return of over 30 % and payback of 3 or 4 years even without taking the grant into account.

56. A strong indication of the deadweight effect is where investments have already started or even been completed before a decision is taken to award a grant. In these situations, the beneficiary has demonstrated, by his initial investment decision that he was willing and able to carry out the investment without the aid. Consequently, it is considered good practice for Member States to exclude such cases from the measure, thereby increasing the likelihood that the aid will be directed to those that need it.

57. Romania applied this good practice and considers investment costs eligible for support only if incurred after the approval of the grant. In contrast, in Lithuania, the authorities accepted project costs retroactively up to two years before the submission of the support application. Support of around 115 million euro was retrospectively approved and paid for 37 large projects in Lithuania.

58. In the other Member States audited, investments were generally eligible from the date of submission of the application, with some exceptions in Spain (Castilla y León), France and Italy (Lazio) that allowed project costs to be financed even if incurred before applying for EU support (see example in ***Box 10***).

59. The audit found long delays for project approval and payments. In Spain (Castilla y Léon) and Italy (Lazio), the approval of projects took on average 14 and 17 months respectively and in France, Poland and Romania, approximately 8 months. Delays put the applicant in a position of having to decide whether to start the investment, with the risk that their grant application may be rejected and they would have to finance the project entirely themselves — or to delay the investment and potentially miss a business opportunity. Applicants that cannot afford to take this risk (for example, those with innovative projects that cannot raise sufficient capital) are effectively excluded from the aid scheme, yet these are the very projects with the greatest need for support. In contrast, where the applicants are able to pre-finance the investments from their own resources (which was the case for 7 of the 24 projects audited) or long-term loans, the aid becomes a mere reimbursement to beneficiaries rather than a source of complementary financing and is an indication of likely deadweight.

BOX 10

AN INDICATION OF DEADWEIGHT: GRANTING EU FUNDING FOR ALREADY COMPLETED PROJECTS

In **France**, a cooperative in the wine sector applied for a grant from a local council aid scheme unrelated to the EU rural development policy. It received the maximum grant of 50 000 euro for its investment project, which was completed in 2007. Measure 123 came into operation in France in May 2008 with a higher aid ceiling. The cooperative applied for and received an additional grant of 37 000 euro from measure 123 for the same project. Given that the cooperative had already completed the project with the 50 000 euro grant, the additional 37 000 euro was clearly deadweight.

60. The Court assessed the 24 projects visited for the risk of deadweight based on documentation and discussions with the beneficiary on the company's financial situation and access to capital; how the project was financed (in particular for the period before the grant was received); the timing of the investment in relation to the grant decision; the nature of the project and its importance in the company's strategy; and the project payback or rate of return (see ***Annex II***). Indications of deadweight were strong in eight of the 24 projects visited with indications of some deadweight in a further 11.

61. The Court has already identified and made recommendations on this issue in previous reports[15]. The weaknesses in programming and in the selection practices applied in the Member States audited combined with results from several mid-term evaluation reports[16] suggest that deadweight is of particular relevance for measure 123.

... AND DISPLACEMENT

62. Displacement is the degree to which an activity promoted by public support is offset by reductions in activity elsewhere. A subsidy that enables one company to increase its market share at the expense of a competitor may have no net effect on policy objectives such as creating employment or — in the case of measure 123 — adding value to agricultural produce, and is therefore *a priori* not an efficient use of the EU funds. Examples of this situation are shown in ***Box 9***. A degree of displacement may, however, be justified where there is a sufficient net effect in terms of the policy objectives.

63. Food processing and marketing is a competitive sector with many thousands of enterprises continually investing to improve their efficiency, to develop their products and to grow. Small and medium-sized enterprises are part of this competitive market: of the 24 companies visited in this audit only three traded predominantly in local markets, the others all competed nationally and 10 of the companies, internationally. Giving a grant of up to 50 % of a company's investment costs puts it at a competitive advantage in relation to unsubsidised companies and therefore carries a strong risk of displacement. Subsidies can also distort normal competitive forces and have negative effects, such as hindering the consolidation of fragmented production.

[15] Special Report No 5/2010 on implementation of the Leader approach for rural development; Special Report No 8/2012 on targeting of aid for the modernisation of agricultural holdings (http://eca.europa.eu).

[16] When replying to the horizontal evaluation question identified by the Commission in the Common Monitoring and Evaluation Framework, 'To what extent has the programme design been successful in avoiding deadweight and/or displacement?', the mid-term evaluations of the Czech Republic, Germany (Lower-Saxony/Bremen and Mecklenburg-Vorpommern), Lithuania, the United Kingdom (England and Wales) RDPs indicate a deadweight risk of approximately 50 % for measure 123.

64. As with deadweight, the primary means of mitigating the risk of unjustified displacement lies in programme design. This requires identifying needs that are sufficiently strong to justify any displacement that may occur, and setting objectives and eligibility conditions specific to those needs. As shown in part I, in the Member States audited this was not done. However, in Lithuania and Spain (Castilla y León) the RDPs limited eligibility in certain food sectors in which there was overcapacity and therefore a high likelihood of displacement.

65. Because of the displacement risks, particularly with an aid scheme such as measure 123 that supports private companies, Member States' authorities should assess project proposals for the likelihood of displacement risk during project approval. Where displacement is likely, they should ensure that the project makes a sufficiently high contribution to the measure's objectives to justify the grant. However, none of the Member States audited did so. None gave any consideration to the risk of displacement or to the efficiency of the measure in this respect.

66. The Court assessed the 24 projects visited for the risk of displacement based on documentation and discussions with the beneficiary on the company's products, markets and competitors and the effects of the investment on these (see ***Annex II***). In particular, where the investment resulted in increased capacity, the Court considered whether this was responding to an expanding market or was aimed at capturing market share from competitors. The analysis showed that displacement was likely in 13 of the projects, which was most evident where the project aimed at increasing market share by increasing capacity or reducing costs. The Court also found displacement effects within the food-processing chain, such as those noted in paragraph 48.

THESE WEAKNESSES LEAD TO MIXED RESULTS FOR THE EFFICIENCY AND EFFECTIVENESS OF THE GRANTS

67. This audit has shown that the design and programming of measure 123, and the systems implemented by the Member States audited, cannot be relied on to ensure that the measure will make an efficient and effective use of the EU and national budgets. The impact of this can already be seen in the projects that have received support. As explained in paragraph 9, the effectiveness and efficiency of the measure would be demonstrated if the projects selected are financially sustainable, result in an improvement in added value, are not affected by deadweight and do not cause unjustified displacement. Only two of the 24 projects met all four of these criteria (see ***Annex II***). Ten were classed as medium and represent satisfactory value for money. Effective projects should also contribute to specific RDP objectives — but this could not be assessed as the RDPs set only very general objectives (see part I).

68. It should be noted that the success of these projects cannot be attributed to the design of the measure or the selection systems implemented by the Member States: the remaining 12 projects selected by the same Member States with those same systems are classed as low or very low in the Court's analysis.

69. The 24 projects were not intended to constitute a statistical sample to be extrapolated to predict the incidence of such projects financed EU-wide. Nevertheless, these case studies illustrate the consequences of a lack of effective programming and selection: the failure in the first instance to identify needs, set specific objectives and design the measure in a way to best achieve those objectives; and in the second instance to have an effective selection process.

PART THREE

HAVE THE COMMISSION AND THE MEMBER STATES APPROPRIATELY MONITORED AND EVALUATED THE RESULTS OF THE MEASURE?

70. Monitoring and evaluation should provide relevant and timely information to the Commission and Member States for managing the 9 billion euro of EU and national money allocated to measure 123, allowing the design and implementation of the measure to be adapted to optimise its effectiveness and efficiency. Information on results and impacts is also important for accountability: to show what has been achieved with the public money. Member States should not only collect data from the applications for support and payments but also on the results achieved at beneficiary level, at least until the expiry of the five-year period for which the EU regulations require beneficiaries to maintain their investments.

71. Under the Common Monitoring and Evaluation Framework (CMEF), Member States must collect information for at least the common output and result indicators and provide mid-term and *ex post* evaluations of their rural development programmes in 2010 and 2015 respectively. The mid-term evaluation is intended to generate amendments to the current programmes when necessary but also contribute to the design of the subsequent (2014–20) programmes. As regards measure 123, the CMEF sets two common result indicators[17] and five common evaluation questions[18].

72. The Court examined the data collection and monitoring systems in the six Member States audited and reviewed a total of 23 mid-term evaluation reports.

[17] (1) Increase in gross value added in supported enterprises (this measures improvements in a company's financial performance).
(2) Number of enterprises introducing new products and/or new techniques.

[18] (1) To what extent have supported investments contributed to introducing new technologies and innovation?
(2) To what extent have supported investments contributed to improving the quality of agricultural and forestry products?
(3) To what extent have supported investments contributed to improving the efficiency in the processing and marketing of agricultural and forestry products?
(4) To what extent have supported investments contributed to enhancing market access and market share of agricultural and forest holdings, including sectors such as the sector of renewable energy?
(5) To what extent have supported investments contributed to improving the competitiveness of the agricultural and forestry sector?

MEMBER STATES DO NOT EFFECTIVELY MONITOR MEASURE 123 PROJECTS

73. The two common result indicators for measure 123 focus on the effects on the food processing companies. They provide little information on the achievement of added value or the effects on producers. None of the Member States audited has introduced additional result indicators that would serve this purpose. Furthermore, four years into the programming period, Poland and Romania had not provided complete information regarding the two common result indicators and the methodologies used by Spain (Castilla y León), France and Italy (Lazio) were not reliable. Castilla y León, for example, took projections from the business plans at the time of grant application for just six out of 444 projects and used these as an indicator for the increase achieved in enterprises' financial performance for the measure as a whole.

74. Of the Member States audited, only Lithuania and Poland monitored project results declared by the beneficiary after the grant payment and this concerned only the companies' financial results and employment.

MID-TERM EVALUATIONS ARE OF LIMITED USE FOR DEMONSTRATING THE EFFICIENCY AND EFFECTIVENESS OF THE MEASURE

75. The review of 23 mid-term evaluation (MTE) reports conducted as part of this audit revealed that the information needed to answer the evaluation questions is, in most cases, lacking and the assessment of project effectiveness is mainly based on theoretical arguments rather than on evidence from completed projects. These weaknesses are confirmed by a methodological assessment of mid-term evaluation reports, conducted by the Commission: 'The early timing of the MTE, but also insufficient monitoring, posed difficulties in terms of data availability and quality. These have been cited as the most important hindrances to come to reliable evaluation results'.

76. Eight of the 23 MTE reports reviewed by the Court gave no conclusions on the evaluation question 'To what extent have supported investments contributed to improving the competitiveness of the agricultural and forestry sector?' despite this being the EU objective for which the aid is given. The other reports mostly gave a positive assessment that agricultural competitiveness had been improved, while recognising that their conclusions were based on assumptions and expectations. These evaluations were of little use for demonstrating the effectiveness or efficiency of the measure as they failed to assess the 'extent' of any improvement (see ***Box 11***).

77. The impact of the weaknesses in monitoring and evaluating the results of the measure extends beyond the absence of information with which to manage and adapt the support in the current period. Such information should be available to inform the decision on whether an equivalent measure should be included in the next programming period from 2014. If it is, the Member States must decide whether to programme the measure and how much of the EU and their own budgets to allocate to it. The evidence is lacking to show whether investment support for food processing companies is an efficient and effective means of improving the competitiveness of agriculture. While the Commission has already introduced some improvements in data collection which is essential for the Member States and Commission to be able to account for the 9 billion euro budgeted for the current programming period — the results are likely to be too late to inform the important decisions concerning the programming of the 2014–20 period.

BOX 11

EVALUATION CONCLUSIONS BASED ON ASSUMPTIONS

Portugal — Azores

The evaluators reviewed the descriptions of the approved projects and formed the opinion that the investments contributed to improving competitiveness because the project descriptions included: generation of new products and products of higher added value; ability to introduce new technologies and processes and innovation; commitment to quality and differentiation; gains in efficiency in the processing of agricultural products; etc. Whether these projects actually achieved such results and how they affected the competitiveness of agriculture was not shown.

Germany — Bavaria

The evaluators' conclusion was that they 'assumed that increasing the competitiveness of the food industry will have a positive impact on the competitiveness of agriculture because (...) sales opportunities for the Bavarian agricultural products will be secured'. No evidence was presented to support this assumption.

CONCLUSIONS AND RECOMMENDATIONS

78. As part of the rural development policy, Member States may use the EU budget, co-financed with their national budgets, to give grants towards the costs of investments undertaken by food-processing and marketing companies. This is intended to add value to agricultural produce and thereby improve the competitiveness of agriculture.

79. This audit set the question 'Has the EU support to the food-processing industry been effective and efficient in adding value to agricultural products?' Because of weaknesses in programme design and in the Member States' project selection systems, this could not be demonstrated. The Court therefore concludes that the support has not been systematically directed to projects that effectively and efficiently add value to agricultural products.

80. The Court nevertheless found that the individual projects examined had been sustained. The investments had improved the financial performance or efficiency of many of the beneficiary companies audited, with a number of the projects adding some value to agricultural products. This is to be expected when giving grants for investments to food processing and marketing companies. However, this could not be attributed to the design of the measure or the Member States' systems and the Court found indications of deadweight and/or displacement in the majority of the projects audited.

81. Despite a programmed 5,6 billion euro from the EU budget there was a lack of evidence to demonstrate:

— that the companies needed a subsidy (as a sector or individually);

— the specific objectives that the subsidy was expected to achieve (and how); and

— the value added to agricultural products and the increase in competitiveness of agriculture obtained.

82. This situation has arisen through a combination of the poor quality of the RDPs, inadequate procedures in the Member States for implementing the measure and weaknesses in monitoring and evaluation.

83. The EU legislation gives Member States the possibility to tailor the measure to meet specific national or regional needs. The legislation sets few requirements or constraints: the onus is on the Member States to ensure that the measure is effective and efficient. Key to this are the RDPs, which set the national or regional objectives and scope of the measure (paragraphs 12 to 18).

84. Yet the RDPs audited mostly comprise only general objectives, sometimes verbatim copies from the EU legislation, and do not provide specific strategies to add value to agricultural products by strengthening their food industry. The rationale for how the measure would improve the competitiveness of agriculture in the Member State or region is missing. Nevertheless, the Commission approved these RDPs (paragraphs 19 to 28).

RECOMMENDATION 1

In their RDPs, Member States should clearly identify where and why public intervention is necessary to improve the added value of agricultural produce and hence the competitiveness of agriculture. 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 to demonstrate how the financial support for the food industry will improve the competitiveness of agriculture.

85. Eligibility conditions established by the Member States audited placed few additional limits on the types of investments or the beneficiaries eligible: in four of the six Member States reviewed, practically all food-processing companies were eligible. The EU legislation requires Member States to set selection criteria, which should allow the most effective and efficient of the eligible projects to be prioritised and those that do not represent value for money to be rejected. Only four of the six Member States set selection criteria and these were not applied in practice: while the Member States had budget available, they financed all eligible projects, regardless of their effectiveness and efficiency (paragraphs 29 to 41).

RECOMMENDATION 2

The Member States should define and continuously apply criteria that ensure the selection of the most effective, sustainable projects with respect to the Member States' specific objectives for improving the added value of agricultural products and the competitiveness of agriculture.

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

86. The Court found that Member States do not systematically direct the funding to projects for which there is a demonstrable need for public support. Without this, the measure risks becoming a handout — a general support to enterprises investing in the food-processing sector — with the attendant risk of distortion of competition and waste of scarce public money. As a consequence, the likelihood of deadweight is high and the results achieved by the projects cannot necessarily be attributed to the grant. Displacement reduces the efficiency of the measure as companies use the subsidised investments to gain market share and not necessarily to improve added value. The deadweight and displacement risks were largely ignored by the Member States and were not formally considered in any of the rural development programmes or selection systems audited (paragraphs 42 to 69).

RECOMMENDATION 3

The Commission and Member States should promote the adoption of best practices in respect of the mitigation of deadweight and displacement risks. This requires Member States to target the aid to 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 in project selection. The Commission should encourage Member States to adopt the practice whereby expenditure for investments would be eligible only from the date of grant approval.

87. Almost a fifth (18 %) of the EU budget for improving the competitiveness of agriculture is paid to food-processing and marketing companies but the effects on the competitiveness of agriculture can only be indirect and there is no clear intervention logic. It is therefore important that the Member States and Commission can demonstrate that the budget has been spent effectively and efficiently. Yet Member States do not collect information on the added value achieved for agricultural products or on the effect of the investments on the competitiveness of agriculture. Member States rely on evaluations for this, but the mid-term evaluations in 2010 were performed before there were tangible results and their conclusions were insufficiently evidence-based. As the results of *ex post* evaluations will not be available until after 2015, the Commission and Member States have an insufficient basis to assess the effectiveness of the 9 billion euro allocated to measure 123 when programming the aid for the 2014–20 period (paragraphs 70 to 77).

RECOMMENDATION 4

The Commission should take the opportunity of the new programming period to improve the CMEF in a way that it provides useful information on the achievements of the projects and measures financed. This implies the enhancement of ongoing evaluation activities and reconsideration of the utility of lengthy mid-term evaluation reports whose results are questionable.

This Report was adopted by Chamber I, headed by Mr Ioannis SARMAS, Member of the Court of Auditors, in Luxembourg at its meeting of 23 January 2013.

For the Court of Auditors

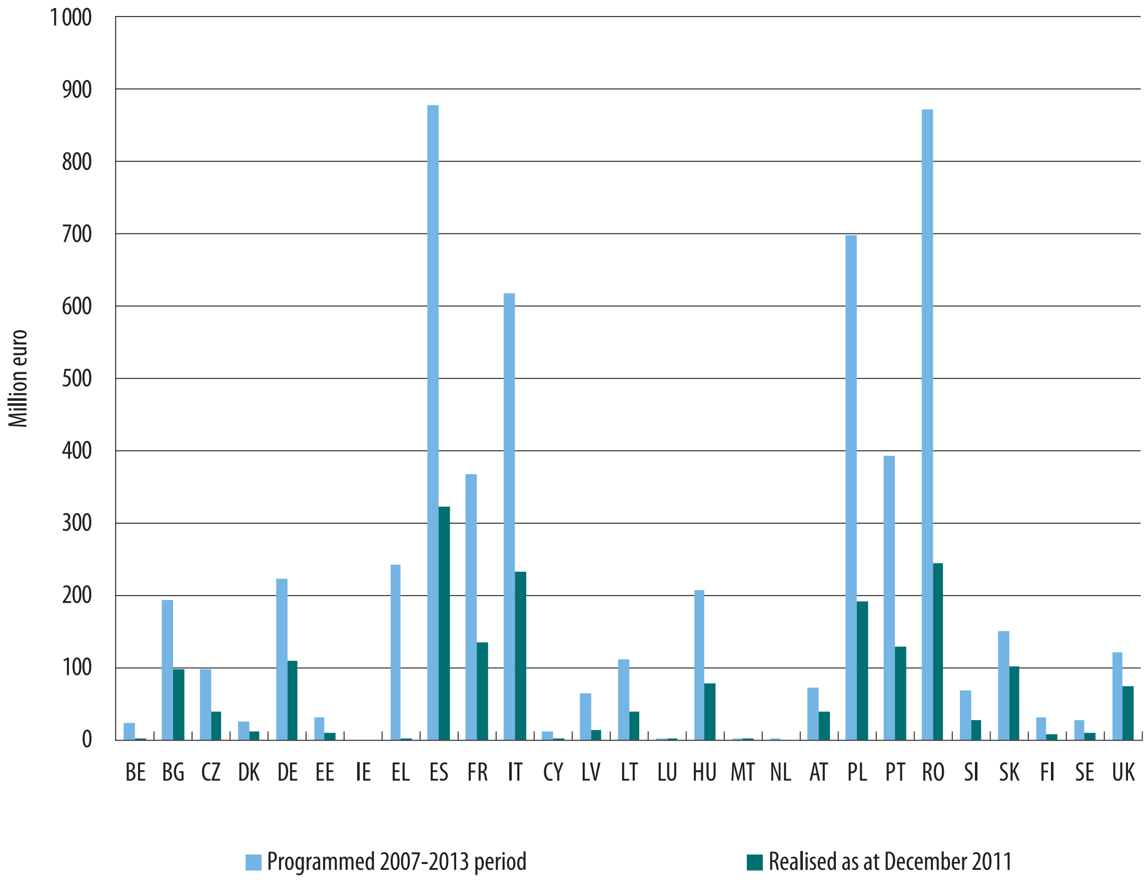
Vítor Manuel da SILVA CALDEIRA
President

ANNEX I

FIGURE –
EU-FUNDS FOR MEASURE 123 PROGRAMMED AND SPENT (AS AT DECEMBER 2011)

Programmed expenditure (2007–13): 5 557 735 472 euro

Implemented expenditure (2007–December 2011): 1 940 224 033 euro (34,9 %)



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). As at December 2011, no expenditure had been declared by the Netherlands. Ireland has not programmed measure 123.

ANNEX II

LIST OF PROJECTS AUDITED AND THE COURT'S ASSESSMENT OF THE EFFICIENCY AND EFFECTIVENESS OF THE GRANT

Member State	Description	Eligible costs (rounded) (euro)	Public aid as % of eligible costs	Sustainable [1]	Demonstrated added value for agricultural products	Indications of deadweight	Indications of displacement	Assessment of overall efficiency and effectiveness of the grant
Spain (Castilla y León)	Building extension and new equipment for meat processing	1 000 000	18 %	yes	high	some	few	medium
	Additional production line for potato processing	600 000	20 %	yes	low	strong	strong	very low
	Construction of a winery	1 500 000	10 %	yes	high	some	some	medium
	Additional production line for potato processing	2 200 000	34 %	yes	medium	some	some	medium
	Additional storage room for fruit	30 000	40 %	yes	low	strong	few [2]	very low
France	Additional production line for cutting and packaging cheese	800 000	20 %	yes	low	some	strong	very low
	Equipment for a new processor of organic vegetables	200 000	39 %	yes	high	few	few	high
	New equipment for winery	200 000	40 %	yes	medium	strong	some	low
	New equipment for meat processing and packaging lines	700 000	26 %	yes	medium	few	some	medium
	New equipment for winery	200 000	34 %	yes	high	strong	some	low
Italy (Lazio)	New equipment capable of processing simultaneously organic and conventional olives	200 000	40 %	yes	high	strong	few [2]	low
	New olive milling equipment with higher capacity	200 000	40 %	yes	low	few	few [2]	low
	Factory renovation and new chestnut processing and packaging equipment	250 000	40 %	yes	medium	some	few [2]	medium
	New facilities for storing, packaging and distribution of fruit and vegetables	900 000	38 %	yes	medium	few	some	medium
	New equipment for winery	250 000	40 %	yes	medium	strong	some	low
Lithuania	New grain drying and storage facilities	4 150 000	40 %	yes	low	some	strong	very low

1 Activity related to the project was sustained at the date of the audit visit.

2 Project aimed at capturing market share but this result had not been achieved at the date of the audit visit.

Member State	Description	Eligible costs (rounded) (euro)	Public aid as % of eligible costs	Sustainable[1]	Demon-strated added value for agricultural products	Indica-tions of deadweight	Indications of displace-ment	Assessment of overall efficiency and effec-tiveness of the grant
Poland	New equipment for a dairy	3 500 000	25 %	yes	medium	some	few	medium
	New equipment and transport vehicles for vegetable processor	700 000	40 %	yes	medium	strong	few	low
	New equipment for processing meat products	350 000	40 %	yes	medium	strong	few[2]	low
	New equipment for vegetable preparation and packaging	900 000	40 %	yes	medium	some	few	medium
Romania	New equipment for winery	1 100 000	50 %	yes	high	few	few	high
	New equipment for vegetable processing	1 500 000	50 %	yes	medium	some	some	medium
	New equipment for meat processing	400 000	50 %	yes	medium	some	some	medium
	New equipment and transport vehicles for grain milling	1 800 000	50 %	yes	low	some	strong	very low

[1] Activity related to the project was sustained at the date of the audit visit.

[2] Project aimed at capturing market share but this result had not been achieved at the date of the audit visit.

Efficiency		Indications of displacement		
		few	some	strong
Indications of deadweight	few	high	medium	low
	some	medium	medium	low
	strong	low	low	low

Overall efficiency and effectiveness		Efficiency		
		low	medium	high
Added value	low	very low	low	low
	medium	low	medium	medium
	high	low	medium	high

Assessment criteria	
Demonstrated added value for agricultural products	The project's contribution towards achieving the following results: — increase in market value (sales price) of products — quality increase of products (including improvements in hygiene, environmental standards and animal welfare) — development of new products and market outlets (responding to market opportunities for high quality products)
Indications of deadweight	— beneficiary's own assessment of the extent to which 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 — investment appraisal shows high rate of return (or short payback) and there are no indications that the beneficiary had difficulties in acquiring capital — the company's financial situation at the date of application shows a very good financial position
Indications of displacement	— beneficiary's own assessment of displacement — the beneficiary is in a stable or decreasing market with little product differentiation and the project's primary aim was to increase capacity/market share or increase efficiency/reduce costs — the project aimed at capturing activities from within the value added chain (packaging, labelling, transport, etc.)

ANNEX III

MID-TERM EVALUATION REPORTS REVIEWED

Bulgaria

Czech Republic

Germany — Bavaria

Germany — Brandenburg/Berlin

Germany — Mecklenburg-Vorpommern

Germany — Lower Saxony/Bremen

Spain — Andalucía

Spain — Castilla La Mancha

Spain — Castilla y León

Spain — Extremadura

France — Mainland (Hexagone)

Italy — Calabria

Italy — Emilia Romagna

Italy — Lazio

Italy — Puglia

Lithuania

Austria

Poland

Portugal — Mainland

Portugal — Azores

Romania

UK — England

UK — Wales

REPLY OF THE COMMISSION

EXECUTIVE SUMMARY

II.

Reading Recital 23 of Council Regulation (EC) No 1698/2005 together with Article 28, the Commission considers that the concept of the measure adding value to agricultural (and forestry) products as envisaged by the legislator is broad, which includes for example improving environmental protection, occupational safety, hygiene and animal welfare.

III.

The legislator did not foresee an *ex ante* 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[1] analysis of the area concerned, hence to target support according to identified territorial needs and structural weaknesses.

The Commission also wishes to underline that based on result indicators new products and new technologies have been supported and the gross value added has increased in some supported enterprises.

IV.

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 provisions[2].

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

Nevertheless, in its supervisory role, the Commission has insisted on several occasions on the need for greater selectivity[3] and targeting in the implementation of the measure.

1 SWOT = Strengths/Weaknesses/Opportunities/Threads.

2 Regulation (EC) No 1698/2005 and Regulation (EC) No 1974/2006 (Article 18 of Regulation (EC) No 1698/2005).

3 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

Joint reply to Point V.–VI.

The Commission considers that the purpose of the eligibility criteria defined by the Member States is not, per se, to exclude a specific company of a production 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 SMEs (with the exception of outermost regions). As concerns targeting, the Commission agrees with the Court that improvements in better targeting the support are needed at the level of Member States.

VII.

Although the impact to primary producers is indirect, the Commission's view is that the intervention logic is sufficiently clear. Indeed, by improving the handling/processing of agricultural products, for example to respond to changing marketing standards, the primary sector benefits from stabilised demand especially when new (innovative) products are developed and new market opportunities are opened. This improves the competitiveness of the agricultural sector of the territories concerned.

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

VIII. (a)

The Commission, aware of weaknesses in this field, 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 result 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.

VIII. (b)

The Commission has insisted on several occasions on the need for greater selectivity (see footnote 3).

The Commission proposals[4] foresee 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 shall generally be compulsory even in the case where available funds are sufficient.

VIII. (c)

The Commission will organise an exchange of best practices on the mitigation of deadweight and displacement risks with the Member States in the first semester of 2013.

4 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

VIII. (d)
The monitoring and evaluation framework for the period 2014–20 is currently being elaborated[5].

These ongoing proposals take account of the lessons learned from the current period and the need to measure the effectiveness of the funds spent. These proposals aim at improving the reporting on results and impacts of the policy by taking into account the information available at various stages of the programming period (see also reply to paragraph 88 and Recommendation 4).

INTRODUCTION

Box 1
Please see paragraph 15.

4.
Please see Commission reply to paragraphs 34 and 35.

AUDIT SCOPE AND APPROACH

9.
Please see Commission reply to paragraph 15.

5 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.

OBSERVATIONS

13.
The Commission agrees that the Member States have to target the measure according to sector's identified needs and structural disadvantages.

See also reply to paragraph 15.

15.
Reading Recital 23 of Council Regulation (EC) No 1698/2005 together with Article 28, the Commission considers that the concept of the measure adding value to agricultural (and forestry) products as envisaged by the legislator is broad, which includes for example improving environmental protection, occupational safety, hygiene and animal welfare, The requirement to identify needs in the RDP is linked to the specific needs of the programming area[6]. These needs are derived from the SWOT-analysis.

Common reply to paragraphs 16.–17.
The measure has evolved over the time from direct management to shared management and the legislator has chosen to limit the rules to a minimum to simplify the legislation and to better reflected the subsidiarity and shared management principle.

Common reply to paragraphs 18.–19.
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 provisions of Regulation (EC) No 1698/2005 and Regulation (EC) No 1974/2006).

21.
The Polish RDP identifies the main structural weaknesses of the food processing sector as poor vertical integration and the diversified structure, which require public intervention.

6 Article 43 of Commission Regulation (EC) No 1974/2006 of 15 December 2006 laying down detailed rules for the application of Council Regulation (EC) No 1698/2005 on support for rural development by the European Agricultural Fund for Rural Development (EAFRD) stipulates, 'For investment measures, Member States shall ensure that support is targeted on clearly defined objectives reflecting identified structural and territorial needs and structural disadvantages' (OJ L 368, 23.12.2006, p. 15).

REPLY OF THE COMMISSION

Box 3

In the case of Castilla y León, even though the RDP recalls the objectives listed in recital 23 of Regulation (EC) 1698/2005, an additional expected effect for improving farms and rural areas performance has also been established[7].

For France, regional plans are not subject to the Commission's approval. Nevertheless, in the Rhône-Alpes regional programming document, some priority to innovative and technological projects is given for networks of enterprises.[8]

22.

In relation to France, the Plan de Développement Rural Hexagonal (PDRH) sets out the general framework for each measure. Further specifications and targeting should be made at regional level within the regional programming documents (DRDR).

See also paragraph 37.

23.

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

Selection of the food sectors to be supported is the task of strategic programming with its SWOT-analysis including the identification of structural and territorial needs.

The Commission considers that while it is necessary for the Member States to establish eligibility criteria, they are not the only way to target the measure. Targeting of the aid can be achieved in many ways; through selection criteria, regional and sectorial differentiation and differentiation of aid intensities depending on the type of the investment as well as aid ceilings by which the Member State can make a preselection among the potential beneficiaries.

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

24.

The objectives set at RDP level are further translated into action via measure design and targeting. The consistency check made by the Commission ensures that the framework for policy action is coherent with EU objectives and provides appropriate guidelines for implementing the strategy.

25.

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

According to Annex II of Regulation (EC) No 1974/2006, 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. Checking that these issues are covered in each programme is part of the Commission's assessment procedure.

26.

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

7 See RDP pages 247 and 248. http://www.jcyl.es/web/jcyl/AgriculturaGanaderia/es/Plantilla100/1185746059889/_/_/_

8 See Volet régional Rhône-Alpes du Programme de Développement Rural Hexagonal, 10 August 2010, Pages 81–82 http://agriculture.gouv.fr/IMG/pdf/Rhone-Alpes_DRDR_V4_valide_100810_V2_101022.pdf

REPLY OF THE COMMISSION

27.
See replies in part two of the report.

28.
See replies in part three of the report.

29. First indent
See reply to paragraph 31.

Article 72 of Regulation (EC) No 1698/2005 requires that all supported projects need to be sustainable in the sense that Member State 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.

As regards evaluation, the information should be provided in the context of the CMEF.

29. Second indent
The measure design, including the eligibility and selection criteria, should be the result of strategic programming based on SWOT-analysis and reflecting the identified structural and territorial needs and structural disadvantages.

The activities covered by the measure include for example promoting the renewable energy production, improving environmental protection, occupational safety, hygiene and animal welfare.

29. Third indent
Please see Commission reply to paragraph 30.

The targeting of investment support (Article 43 of Commission regulation (EC) No 1974/2006) was introduced in this programming period exactly to limit deadweight and displacement effects.

30.
Article 28 of Council Regulation (EC) No 1698/2005 requires that support shall not be granted to enterprises in difficulty within the meaning of the Community guidelines on State aid for rescuing and restructuring firms in difficulty.

31.
It is the responsibility of Member States to establish how, and according to which criteria, to assess whether a project would actually improve the performance of the enterprise.

The Commission would like to point out that Article 28 of Council Regulation (EC) No 1698/2005 requires that investments in adding value to agricultural and forestry products must improve the overall performance of the enterprise and that support shall not be granted to enterprises in difficulty within the meaning of the Community guidelines on State aid for rescuing and restructuring firms in difficulty.

Article 24.2 (e) of Regulation (EU) No 65/2011 foresees 'Administrative checks on applications for support shall in particular include verification of: (e) the reliability of the applicant, with reference to any previous co-financed operations undertaken since 2000'.

Box 4
Italy (Lazio): As regards the checks performed by region's officials, the Commission's services have addressed the issue on the occasion of the Annual Meeting on 27/11/2012 with the Managing Authority and representatives of the Paying Agency and the matter will be adequately followed up.

33.
According to the principles of subsidiarity and shared management, project selection lies within the responsibility of Member States.

All Member States carried out an initial SWOT analysis and needs assessment that served as a basis for selecting relevant measures and respective objectives.

REPLY OF THE COMMISSION

34.
The Commission considers that several targeting mechanisms exist such as eligibility criteria (including differentiated aid rates) and selection criteria to channel EU funds and national funds to strategic objectives.

35.
Article 71(2) of Regulation (EC) No 1698/2005 establishes a general obligation to fix selection criteria. However, it is for MS to define the level of detail for the selection criteria.

According to Article 49 of the Commission's proposal for the next programming period, strategic programming will be further reinforced, with the result of an improved strategic targeting through the Union priorities for rural development and their focus areas.

36.
Although Castilla y León has no selection criteria strictly speaking, regional established criteria and strong eligibility criteria are also meant to be selective tools to target among potential beneficiaries.

Poland sought to achieve the intended targeting by means of the eligibility criteria and the way calls for applications were carried out. On 23 August 2012, the Polish Managing Authority subsequently initiated the process of introduction of selection criteria for measure 123.

37.
See reply to paragraph 15.

Projects that do not create direct added value for products, for example those improving the environmental protection, can be prioritised if they are part of the strategy.

As there is no standard definition of 'adding value', which can take different forms, assessment criteria should respond to the specific measure objectives.

For Lithuania, by Order of the Lithuanian Ministry of Agriculture[9] the selection criteria applied under measure 123 have been revised. The new criteria put a higher emphasis on adding value to agricultural products.

[9] Order No 3D-219 of 27-03-2012.

Box 6
As regards Romania, the Commission wishes to clarify that, although the majority of projects submitted exceed the minimum scoring for being selected, only the best scoring projects are financed. Up to December 2012, only about 37 % of the projects submitted under the measure 123 under the RO RDP had been selected.

Box 7
In Italy (Lazio) the Commission considers as a best practice, when applying selection criteria, the use of a minimum score to be achieved by each eligible project in order to be financed. Following observations formulated by the Commission and the Court of Auditors, the Region has now adopted a minimum score to be applied in future calls.

40.
The objective is to value endogenous resources and support local development as well as ensuring stability of local supply.

41.
According to Article 16 of Regulation (EC) No 1698/2005, it is the national/regional authority that establishes its priorities/strategies in relation with the *ex ante* analysis as refered to in Article 85.

42.
Article 72 of Regulation (EC) No 1698/2005 requires that all supported projects need to be sustainable in the sense that Member State 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.

As regards evaluation, the information should be provided in the context of the CMEF.

43.
The Commission considers that the interventions selected for support are in line with the specific priorities of the RDPs, respond to the assessed needs of the territory at the national and regional level in line with the SWOT analysis and satisfy the objectives of the relevant regulations on Rural Development in force. The interventions funded are linked to the basic agricultural production, aiming at reinforcing the existing local/regional SMEs (including co-operatives) which the legislator had in mind.

REPLY OF THE COMMISSION

44.
Risks are inherent to any investment project. If at the beginning the Managing Authority, using criteria established under its responsibility, assesses that the project has the potential to increase the overall performance of the enterprise and respects any additional eligibility condition set at RDP level, then it can receive support.

It lies within Member States reponsibility to establish how and with what criteria assessing whether a project would actually improve the performance of the enterprise.

46.
The Commission welcomes the Court's positive assessment.

48.
The Commission considers that the improvement of the efficiency of the sector is one of the means to contribute to the competitiveness of agriculture, as referred to in recital 23 of Regulation (EC) No 1698/2005.

Box 9
For France, Rhône-Alpes, such packaging upgrade project is a standard and logical way of developing and securing company development, all normally performing companies arrive at certain stage to develop own capacities in different areas (packaging, logistic, IT, technologies …)

In the example shown by the Court for Castilla y León, increasing storage capacity concerns the commercialisation of the fruit and vegetables while capturing a greater market, which helps improving the overall performance of the company, in line with Art. 28.(a) and (b) of Regulation (EC) No 1698/2005.

In Romania: From the information received regarding the respective project it appears that it contributes to increasing and modernising the local network for collecting products.

50.
The Commission considers that support to food industry can, in addition to creating new jobs, also be considered to contribute to maintain jobs in rural areas.

52.
The Commission considers that public support may be necessary and efficient in circumstances of market failures especially to provide positive externalities and public goods.

53.
The Commission considers that the audited Member States identified sector's weaknesses. As part of the strategic programming process Member States are required to ensure that support is targeted on clearly defined objectives reflecting identified structural and territorial needs and structural disadvantages (Article 28 of Regulation (EC) No 1698/2005 and 43 of Regulation (EC) No 1974/2006).

54.
The Commission considers that the eligibility and selection criteria should serve as a basis for targeting the support to the identified objective needs of the sector for different types of investments.

The Commission would like to point out that Article 28 of Council Regulation (EC) No 1698/2005 requires that investments in adding value to agricultural and forestry products must improve the overall performance of the enterprise and that support shall not be granted to enterprises in difficulty within the meaning of the Community guidelines on State aid for rescuing and restructuring firms in difficulty.

55.
In Lithuania, the criterion 'high rate of return on the investment' was last in the list of six selection criteria which are in priority order, and the priority 'lower intensity of support requested' was ranked above it (fourth). As from 2011 this criterion has been changed by the LT authorities with the current version, applicable in 2012 being '*projects with a higher return on assets*'.[10]

[10] Order of the Lithuanian MoA No 3D-219 of 27-03-2012.

REPLY OF THE COMMISSION

Common reply to paragraphs 56.–57.

The risk deriving from the fact that project costs occurred before the date of submission of the support application can be claimed retroactively, has been addressed by the Commission:

— In its proposal of September 2010 for the amendment of Regulation (EC) No 1698/2005 and in respect of investment operations under measures falling within the scope of Article 42 of the Treaty (TFEU), the Commission has proposed that only expenditure which has been incurred after an application has been submitted to the competent authority shall be considered eligible[11]. In the Commission's view, this should limit the risk of deadweight.

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

58.

For Lazio, as part of the procedure of preliminary expression of interest ('*domanda di pre-adesione*'[12]), beneficiaries might have started to implement projects before the completion of the application, especially the procedural and administrative preparation.

Box 10

The Commission will investigate further this case in order to analyse the justification for the additional payment.

[11] The Lisbon alignment proposal — COM(2010) 537 Final dated 30.9.2010.

[12] The so-called '*domanda di pre-adesione*' is an instrument that the Region has implemented exclusively during the initial phase of implementation of the measure (for the first open call), by allowing an early start of the projects to ensure the continuity of the interventions during the transition from the previous programming period to the current one, reducing the risk of interruption of the operations, and accelerating the implementation of the programme.

59.

The Commission considers that the possibility of being admitted to public funding can generate an incentive to implement projects which would not have taken place if no funding was available.

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

As for Castilla y León, during the last monitoring committee of 15 June 2012, the Commission encouraged the region to shorten projects approval and payment delays, without jeopardising the sound management of the EU funding.

In Romania's case, the Commission is encouraging MS to shorten the delay for project approval, while making a balance between the processing of applications within a reasonable timescale without compromising the sound financial management of EU funds. The length of selection process is mainly due to the high number of applications received under each call for proposals.

60.

Castilla y León is assessing possible deadweight effect. Lessons drawn from this exercise will lead to improved administrative procedures to assess and mitigate risks.

61.

It is expected that the synthesis of Mid-term evaluations[13] (MTEs) carried out on behalf of the Commission will give information on how the issue of deadweight was addressed, based on the MTE reports that provided an estimation/calculation of impacts of their programmes. However, since the MTE synthesis is not structured according to particular measures but according to overarching themes, it will not necessarily provide a clear view as to the specific role of measure 123 in the calculation of deadweight effects.

[13] The Synthesis of Mid-Term Evaluations 2007–13 will be published end of 2012/beginning of 2013.

REPLY OF THE COMMISSION

62.
A certain displacement in the processing and marketing sector may be acceptable if the overall net benefit for the primary agricultural sector through a more efficient processing and marketing is achieved.

The Commission does not consider it an inefficient use of EU funds if a subsidy entails an increase of the marketing share at the expense of a competitor. The subsidy may lead to a more efficient (economically and/or environmentally) installation, which overall may contribute to increase the competitiveness of the agriculture in the programming area.

The Commission considers that if the investment support is well targeted (using among others eligibility and selection criteria, including differentiation in aid rates) and based on clearly identified gaps/needs[14], 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.

Common reply to paragraphs 63.–64.
The Commission considers that the interventions selected for support in line with the specific priorities of the RDPs, respond to the assessed needs of the territory at the national and regional level in line with the SWOT analysis and satisfy the objectives of the relevant regulations on Rural Development in force. Therefore the Commission considers that displacement can exist and that under certain circumstances it may even lead to an improvement of the economic situation (e.g. rationalisation).

Common reply to paragraphs 65.–66.
In general terms, the Commission considers that:

The Member States have the obligation to adopt a strategic approach to programming that takes into account the specific situation and needs of the different rural areas and beneficiaries covered by the programme. This helps in limiting the risk of displacement by targeting the aid to those in real need. In addition, the instrument of the National Strategy Plan further provides consistency across different regions/areas and should ensure an adequate and balanced allocation of public resources.

See also reply to 63.

[14] Article 43 of Regulation (EC) No 1974/2006.

66.
The Commission considers that the interventions selected for support in line with the specific priorities of the RDPs, respond to the assessed needs of the territory at the national and regional level in line with the SWOT analysis and satisfy the objectives of the relevant regulations on Rural Development in force. The interventions funded are linked to the basic agricultural production, aiming at reinforcing the existing local/regional SMEs (including cooperatives). Therefore the Commission considers that displacement can exist and that under certain circumstances it may even lead to an improvement of the economic situation (e.g. rationalisation).

Common reply to paragraphs 67.–69.
According to the principles of subsidiarity and shared management, project selection lies within the responsibility of Member States. The Commission has insisted on several occasions on the need for greater selectivity[15].

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 provisions[16].

The monitoring and evaluation framework for the period 2014–20 is currently being elaborated.[17]

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

[16] Regulation (EC) No 1698/2005 and Regulation (EC) No 1974/2006 (Article 18 of Regulation (EC) No 1698/2005).

[17] 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.

REPLY OF THE COMMISSION

The proposals for the monitoring and evaluation system for the period 2014–20 seek to better adjust the timing of evaluations to the information available at various stages of the programming period. There is no longer the requirement of a mid-term evaluation, instead extended annual implementation reports shall be submitted in 2017 and 2019 in which (among other things) progress towards achieving the objectives of the programme is to be set out and assessed (see proposal for the Common Provisions Regulation (CPR) art. 44). In order to be able to deliver the necessary information, Member States are required to carry out evaluations during the programming period according to an evaluation plan (see proposal for CPR art. 49).

70.
The forthcoming synthesis of Mid-term evaluations is expected to give an overview of the implementation of the measure based on the 92 MTEs of the MS and regions. This will include information on the rates of achievement of the result indicators linked to measure 123 (Number of enterprises introducing new products and/or techniques and Increase in gross value added in supported enterprises) — see reply to §76 for more details.

In the *ex post* evaluation, Member States should again report on the achievement of the result indicators, this time covering the full programming period.

73.
It is up to the Managing Authority to determine where additional indicators are relevant and therefore need to be developed and monitored[18]. The intention is not to have an exhaustive set of additional indicators but rather to have some additional indicators defined to make sure that potential specificities of the RDP could be monitored and evaluated.

The Commission, aware of weaknesses in MS methodologies to assess some indicators, established methodological guidelines in 2010 that were distributed and explained to the people in charge of the evaluation within the MS. Better and more reliable figures are now expected.

[18] 'Each rural development programme shall specify a limited number of additional indicators specific to that programme' — see Regulation 1698/2005, Article 81 §2.

In Romania, the issue of missing indicators has been raised during Annual Review Meetings and Romania is trying to provide those via a project to be financed under technical assistance.

74.
In the respect of the shared management, the Common Monitoring and Evaluation Framework (CMEF) handbook offers some flexibility to MS on how they implement their monitoring and evaluation. MS should identify the right balance for their monitoring system to ensure good quality data at a acceptable cost.

75.
The forthcoming synthesis of MTEs is expected to provide a more complete picture on the information contained in the MTE reports as it covers all 92 MTEs of the MS and regions. This includes information on measure 123 with respect to the implementation of the measure[19] and on the achievement of the result indicators that the measure should contribute to[20].

Furthermore, the synthesis of MTEs will give an overview of the impacts of programmes on the basis of available information from those MTEs that have performed such estimations/calculations, although exact quantification of these impacts is likely to remain difficult at this stage of the implementation of programmes.

Where quantitiative information on impacts is not available, the Commission does not consider it bad practice for the evaluation reports to draw on conceptual analysis and theoretical arguments on the effects of certain measures if these arguments are well founded.

The proposals for the monitoring and evaluation system for the 2014–20 period address the difficulties of assessing impacts at the moment that the MTEs were carried out by providing a different approach (see reply to §88 — Rec 4 for more details).

[19] Achievement of related output indicators, number of enterprises supported holdings and Total volume of investment.

[20] Number of enterprises introducing new products and/or techniques and Increase in gross value added in supported enterprises.

REPLY OF THE COMMISSION

76.
The synthesis of MTEs is expected to give an overview on the response rates to the evaluation questions. One reason why EQs linked to measure 123 may only have been answered partly is the too early timing of the MTE than made it difficult to come to a reliable assessment of impacts at the mid-term stage of the programming period.

Box 11
Portugal — Azores
See reply to paragraph 77.

Germany — Bavaria
See reply to paragraph 62.

77.
Please see reply to paragraph 75 on the information contained in the forthcoming synthesis of MTEs, which is expected to provide an indication of the current performance of the measure and a useful background for the decision on whether to programme the measure in the future.

The Commission also wishes to underline that based on result indicators new products and new technologies have been supported and the gross value added has increased in some supported enterprises.

The 9 billion euro budgeted for the current period will be subject to an *ex post* evaluation.

CONCLUSIONS AND RECOMMENDATIONS

79.
Reading Recital 23 of Council Regulation (EC) No 1698/2005 together with Article 28, the Commission considers that the concept of the measure adding value to agricultural (and forestry) products as envisaged by the legislator is broad, which includes for example improving environmental protection, occupational safety, hygiene and animal welfare.

80.
A certain displacement in the processing and marketing sector may be acceptable if the overall net benefit for the primary agricultural sector through a more efficient processing and marketing is achieved.

The Commission does not consider that in case a subsidy entails an increase of the marketing share at the expense of a competitor, this automatically leads to an inefficient use of the EU funds. The subsidy may lead to a more efficient (economically and/or environmentally) installation, which overall may contribute to increase the competitiveness of the agriculture in the programming area.

The Commission considers that if the investment support is well targeted (using among others eligibility and selection criteria, including differentiation in aid rates) and based on clearly identified gaps/needs[21], the risk of deadweight and displacement is minimised. The targeting of investment support (Article 28 of Regulation (EC) No 1698/2005 and Article 43 of Regulation 1974/2006) was introduced in this programming period exactly to limit deadweight and displacement effects coming out of earlier evaluations.

81. First indent
The legislator did not foresee an *ex ante* 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[22] analysis of the area concerned, hence to target support according to identified territorial needs and structural weaknesses.

81. Second indent
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 provisions[23].

[21] Article 43 of Regulation (EC) No 1974/2006.

[22] SWOT = Strengths/Weaknesses/Opportunities/Threats.

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

REPLY OF THE COMMISSION

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

Nevertheless, in its supervisory role, the Commission has insisted on several occasions on the need for greater selectivity[24] and targeting in the implementation of the measure.

81. Third indent

Although the impact to primary producers is indirect, the Commission's view is that the intervention logic as established by the legislator is sufficiently clear. Indeed, by improving the handling/processing of agricultural products, for example to respond to changing marketing standards, the primary sector benefits from stabilised demand of their produce. This is the case especially when new (innovative) products are developed and new market opportunities are opened. This improves the competitiveness of the agricultural sector of the territories concerned.

To remedy the weaknesses in methodologies developed by Member States (MS) to assess some indicators, the Commission established methodological guidelines in 2010[25]. These guidelines were distributed and explained to the people in charge of the evaluation within the MS. More reliable figures are now expected.

82.

The monitoring and evaluation framework for the period 2014–20 is currently being elaborated[26].

These ongoing proposals take account of the lessons learned from the current period and the need to measure the effectiveness of funds spent by better adjusting the reporting on results and impacts of the policy to the information available at various stages of the programming period (see also reply to paragraph 87 and Recommendation 4).

84.

The Commission considers that the intervention logic/rationale of the measure is sufficiently clear. By restructuring and developing physical potential and promoting innovation the measure actually aims at modernising and fostering the competitiveness of the agricultural sector through increased added value of local products.

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 provisions[27].

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

Nevertheless, in its supervisory role, the Commission has insisted on several occasions on the need for greater selectivity[28] and targeting in the implementation of the measure.

Recommendation 1 — First part

See second part of this recommendation.

Recommendation 1 — Second part

The Commission agrees with the recommendation and has proposed to strenghten the legal framework for the next programming period so that appropriate *ex ante* quantified targets (close to result-type indicators) are set for each of the focus areas of the Union priorities, on the basis of common result indicators. 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.

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

[25] The methodological guidance on specific indicators by the European Evaluation network for Rural Development (http://enrd.ec.europa.eu/evaluation/evaluation-methodologies/guidance-on-specific-indicators/introduction/en/introduction_en.cfm).

[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.

[27] Regulation (EC) No 1698/2005 and Regulation (EC) No 1974/2006 (Article 18 of Regulation (EC) No 1698/2005).

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

REPLY OF THE COMMISSION

85.
The Commission has insisted on several occasions on the need for greater selectivity[29] in the current programming period.

For the next programming period, the Commission proposals[30] foresee 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 shall generally be compulsory even in the case where available funds are sufficient[31].

Recommendation 2 — First part
The Commission understands that the first part of the recommendation is addressed to Member States. It 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.

For the future period the Commission has proposed that the Member States should demonstrate that an appropriate approach has been defined laying down principles with regard to the setting of selection criteria for projects, which takes into account relevant targets.

Recommendation 2 — Second part
As regards the application of selection criteria, the Commission agrees and is prepared to encourage Member States to more efficient use of the selection criteria during the rest of the current programming period. In addition, the Commisision has proposed for the next programming period that selection criteria should be defined for operations under all measures[32].

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

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

[31] 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, the use of the selection criteria will be optional in case of sufficient funds.

[32] 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, the use of the selection criteria will be optional in case of sufficient funds.

86.
The Commission agrees with the Court that improvements in better targeting the support is needed at the level of Member States.

When the investment support is well targeted and based on clearly identified gaps/needs, the risk of deadweight and displacement is minimised. The targeting of investment support (Article 43 of Regulation (EC) No 1974/2006) was introduced in this programming period exactly to limit deadweight and displacement effects coming out of earlier evaluations.

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 combinaisons 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.

Recommendation 3
The Commission will organise an exchange of best practices on the mitigation of deadweight and displacement risks with the Member States in the first semester of 2013.

To reduce the deadweight risk the Commission has introduced in the legal proposal for the next programming period[33] that only expenditure which has been incurred after an application has been submitted to the competent authority shall be considered eligible.

87.
Although the impact to primary producers is indirect, the Commission's view is that the legislator has established intervention logic that is sufficiently clear. Indeed, improving the handling/processing of agricultural products, for example to respond to changing marketing standards, the primary sector benefits from stabilised demand especially when new (innovative) products are developed and new market opportunities are opened. This improves the competitiveness of the agricultural sector of the territories concerned.

[33] Article 67(2) of the Rural Development proposal.

REPLY OF THE COMMISSION

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

The forthcoming synthesis of MTEs is expected to give an overview of the available information on measure 123 with respect to the implementation of the measure[34] and on the achievement of the result indicators[35].

The Commission also wishes to underline that based on results indicators new products and new technologies have been supported and the gross value added has increased in some supporting enterprises.

The 9 billion euro budgeted for the current period will be subject to an *ex post* evaluation.

Recommendation 4

The proposals for the monitoring and evaluation system for the period 2014–20 introduce a number of changes. There is no longer the requirement of a mid-term evaluation, instead extended annual implementation reports shall be submitted in 2017 and 2019 in which (among other things) progress towards achieving the objectives of the programme is to be set out and assessed[36]. In order to be able to deliver the necessary information, Member States are required to carry out evaluations during the programming period according to an evaluation plan (see proposal for CPR art. 49). In this way, the reporting on results and impacts of the policy will be better adjusted to the information available at various stages of the programming period.

34 Achievement of related output indicators, number of enterprises supported holdings and Total volume of investment.

35 Number of enterprises introducing new products and/or techniques and Increase in gross value added in supported enterprises.

36 See proposal for CPR: Common Provisions Regulation (Art 44).

European Court of Auditors

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AS PART OF THE EU'S RURAL DEVELOPMENT POLICY GRANTS ARE MADE AVAILABLE TO ENTERPRISES THAT PROCESS AND MARKET AGRICULTURAL PRODUCTS, WHICH SHOULD ALSO RESULT IN IMPROVING THE COMPETITIVENESS OF THE AGRICULTURAL SECTOR.

THE COURT'S AUDIT EXAMINED WHETHER THE EU SUPPORT HAD BEEN EFFECTIVE AND EFFICIENT IN THIS RESPECT, BUT FOUND THAT MEMBER STATES DO NOT DIRECT THE FUNDING TO PROJECTS FOR WHICH THERE IS A DEMONSTRABLE NEED FOR PUBLIC SUPPORT. WITHOUT THIS, THE MEASURE RISKS BECOMING A HANDOUT — A GENERAL SUPPORT TO ENTERPRISES INVESTING IN THE FOOD-PROCESSING SECTOR — WITH THE ATTENDANT RISKS OF DISTORTION OF COMPETITION AND INEFFICIENT USE OF SCARCE PUBLIC MONEY.

THE COURT PROVIDED RECOMMENDATIONS THAT SHOULD ALLOW THE COMMISSION AND THE MEMBER STATES TO REMEDY THE WEAKNESSES MENTIONED.

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