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I

(Information)

COURT OF AUDITORS

SPECIAL REPORT No 4/97

on the audit of certain aspects of German reunification measures involving EAGGF
compensation payments and export refunds, together with the Commission's replies

*(97/C 144/01)**(Submitted pursuant to Article 188C (4), second indent, of the EC Treaty)*

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1. INTRODUCTION

1.1. The reunification of Germany on 3 October 1990 presented potential production surpluses and animal disease problems to the European Communities. For example, the new *Länder* had a stock of some 1,9 million cows as at 30 June 1990 of which some 666 000 had been tested positive for enzootic bovine leucosis (EBL) ⁽¹⁾, a virus disease which leads to the growth of lymph tumours. Veterinary opinion is that the meat and milk from infected animals (with the exception of those where tumours have already developed) is fit for human consumption.

1.2. A number of measures were adopted by the EC to deal with the potential production surpluses and animal disease problems. The observations in this report arise from an audit of which the principal objective was the legality and regularity of export refunds granted in the context of German reunification. During the course of this audit it became apparent that export refunds were granted on products from a market sector which had benefited directly or indirectly from other EC subsidies. The report therefore does not reflect a comprehensive audit of German reunification measures. It does however comment on decisions leading to the cumulation of subsidies in the context of German reunification and on the Commission's control of compensation payments for the eradication of enzootic bovine leucosis in the new *Länder*. *Table 1* summarizes the measures and the cost to the EC budget. In the general context of export refunds, it contains observations relating to the granting of export refunds on products of poor quality.

Background to the measures

Enzootic bovine leucosis

1.3. In the former German Democratic Republic, milk and beef production was concentrated in Landwirtschaftlichen Produktionsgenossenschaften (LPGs). Within the LPG organization the animals were divided into herds which were completely free of EBL; herds with a mixed stock (Sanierungsbestände) and 100 % EBL-positive herds (Auffangstationen). Animals from the 'Sanierungsbestände' which tested EBL positive had been traditionally transferred to the 'Auffangstationen' where they continued producing milk until the end of their milking life.

1.4. The EC had had eradication programmes which involved paying compensation for the slaughter of infected animals, the costs being shared between budgets of Member States and the EC. As a result, by 1990 the EC was almost free of EBL. It was therefore desirable

⁽¹⁾ Source: Statistics from Bundesanstalt für Viruserkrankungen der Tiere.

that the Federal Republic of Germany introduced a programme to eradicate EBL from the herds in the new *Länder* which it did with effect from 3 October 1990. The programme was to run over three years. Under Council Decision 90/424/EEC ⁽²⁾ and Commission Decision 92/5/EEC ⁽³⁾, the EC contributed to the costs of all animals slaughtered under the programme after 1 October 1991. The cost to the EC budget for the period 1 October to 31 December 1991 was ECU 14,5 million.

Export refunds

1.5. Within the Commission it was considered desirable that the meat from animals slaughtered under the eradication scheme should not find its way on to the EC internal market for fear of depressing prices. Both the Commission and German veterinary services were and are of the opinion that such meat is fit for human consumption. A scheme was therefore drawn up to dispose of the meat to the former trading partners of the new *Länder*, supported by an export refund, financed by the EC and with a supplement financed by Germany's national budget. The special refunds were authorized by Commission Regulations (EEC) No 2762/90 ⁽⁴⁾ and (EEC) No 2769/90 ⁽⁵⁾ on condition that the products exported were the subject of agreements concluded by the former German Democratic Republic with third countries before 3 October 1990. The reason for imposing this condition was to ensure the export of beef from the former German Democratic Republic which would otherwise have caused problems on the internal market. The scheme foresaw contracts which would involve the slaughter of approximately 700 000 cows. This figure was later reduced to 600 000. It was to be executed over the period 3 October 1990 to 31 December 1991. The cost to the EC in terms of export refunds for beef of new *Länder* origin exported with a customs control date after 1 October 1991, the operative date for the EC contribution to the EBL eradication scheme, is in the order of ECU 44 million ⁽⁶⁾.

Cessation of milk production

1.6. Milk production in the new *Länder* was also a problem. In 1989, the last year before reunification, annual milk deliveries were in the order of 7,8 million tonnes. The EC milk quota scheme had to be introduced

⁽²⁾ Council Decision 90/424/EEC of 26 June 1990 (OJ No L 224, 18. 8. 1990).

⁽³⁾ Commission Decision 92/5/EEC of 3 December 1991 (OJ No L 4, 9. 1. 1992).

⁽⁴⁾ Commission Regulation (EEC) No 2762/90 of 27 September 1990 (OJ L No 267, 29. 9. 1990).

⁽⁵⁾ Commission Regulation (EEC) No 2769/90 of 27 September 1990 (OJ No L 267, 29. 9. 1990).

⁽⁶⁾ Source: Export refund data supplied on magnetic tape by HZA Hamburg Jonas, the responsible paying agency.

and this required a reduction in milk deliveries, as established for the 1989 calendar year, of around 20 % to limit annual deliveries to 6,2 million tonnes. To help meet this quota limit Council Regulation (EEC) No 3577/90⁽⁷⁾ provided for the 1989 reference quantity to be reduced by a flat percentage without payment of compensation to arrive at a basis reference quantity of 6,8 million tonnes. The same Regulation provided for a further reduction of 3 % by way of definitive cessation of milk production, equal to 204 120 tonnes to be achieved by 31 March 1991 at a rate of compensation of ECU 42 per 100 kgs of reduction to be paid to the producers. The scheme did not require the animals to be slaughtered. The compensation was intended to cover loss of income from reduced milk production. The cost to the EC budget of this scheme for the year ending 15 October 1991 was ECU 72 million and ECU 11 million in the following year⁽⁸⁾. Commission Regulation (EEC) No 3776/90⁽⁹⁾ laid down detailed rules for fixing compensation for the definitive discontinuation of milk production.

1.7. In addition to the definitive cessation measure, Council Regulation (EEC) No 775/87⁽¹⁰⁾ provided for the temporary withdrawal in the other Member States of a proportion of the reference quantities on payment of a compensation of ECU 10 per 100 kgs reducing over five 12-month periods to ECU 7 per 100 kgs. This measure was extended by Regulation (EEC) No 3577/90 to producers in the territory of the new *Länder*. The rate of compensation was fixed at ECU 21 per 100 kgs. The cost to the EC budget for the application of this measure in the territory of the new *Länder* in the year ending 15 October 1991 was ECU 27 million and in the succeeding year ECU 36 million⁽¹¹⁾. The reduction to be achieved by this measure was 306 180 tonnes.

1.8. The number of cows needed to meet the milk quota of 6,2 million tonnes for the new *Länder* was, according to DG VI, 1,2 million. At the end of June 1991 the actual number had been reduced to 1,4 million and by the end of December 1991 to 1,2 million⁽¹²⁾. The milk production was 5,8 million tonnes for the calendar year 1991 and 5,3 million tonnes⁽¹³⁾ for 1992.

⁽⁷⁾ Council Regulation (EEC) No 3577/90 of 4 December 1990 (OJ No L 353, 17. 12. 1990).

⁽⁸⁾ Source: Declarations of expenditure from Germany to the Commission for budget lines B1-2 0 6 6 and B1-2 0 6 7 for the years ending 15 October 1991 and 15 October 1992.

⁽⁹⁾ Commission Regulation (EEC) No 3776/90 of 19 December 1990 (OJ No L 364, 28. 12. 1990).

⁽¹⁰⁾ Council Regulation (EEC) No 775/87 of 16 March 1987 (OJ No L 78, 20. 3. 1987).

⁽¹¹⁾ Source: Declarations of expenditure from Germany to the Commission for budget lines B1-2 0 6 6 and B1-2 0 6 7 for the years ending 15 October 1991 and 15 October 1992.

⁽¹²⁾ Source: Statistisches Bundesamt, Wiesbaden.

⁽¹³⁾ Source: Statistisches Bundesamt, Wiesbaden.

2. OBSERVATIONS

Cumulation of subsidies

2.1. For the reduction in milk production the slaughter of 390 000 cows was necessary and for the eradication of EBL 600 000 cows had to be slaughtered in 1991. The Commission services were aware of the danger of double compensation during a period when subsidies for the reduction in milk production, the eradication of EBL and export refunds could all be obtained by the slaughter of one and the same animal.

2.2. The Commission services considered the possibility of introducing a system under which this risk would be minimized by first paying compensation for slaughtering leucosis-infected cows and subsequently paying compensation for any further reduction in cow numbers needed to meet milk quotas. There is no contemporary document which shows why this approach was not followed.

2.3. The relevant legislation authorizing payments for the definitive cessation of milk production and for the temporary reduction of reference quantities, Council Regulations (EEC) No 3577/90 of 4 December 1990 and (EEC) No 3776/90 of 19 December 1990, and Commission Decision 92/5/EEC of 3 December 1991 authorizing the financial contribution towards the cost of the EBL eradication programme made no reference to the problem of overcompensation.

2.4. The Court's audit on the spot in the new *Länder* revealed that beef from animals slaughtered and compensated for under the EBL eradication scheme, was subsequently exported with the benefit not only of the EC refund but also of the German national supplement authorized by Commission Regulation (EEC) No 2762/90. Undertakings receiving EBL eradication compensation were also in receipt of compensation for the definitive cessation of milk production and for the temporary withdrawal of a proportion of the reference quantity.

2.5. In many instances examined during the audit, the total amount of subsidies exceeds the value of individual animals. An example of the subsidies paid as a direct or indirect result of the slaughter of one animal is given at Annex 1. The total of the subsidies for the slaughter of this one cow, valued at ECU 681 by the German veterinary services, is calculated as ECU 1 081, of which ECU 798 came from the EC budget. In its reply the Commission contests the relevance of Annex 1. According to the Commission the presentation in Annex 1 does not take into account the different objectives and

the specific conditions of each measure. The Court considers paragraphs 2.1 to 2.5 to give sufficient information on these objectives and measures. Annex 1 only serves to give an illustration of the total amount of subsidies for one cow. The Commission does not contest the amounts mentioned.

Enzootic bovine leucosis eradication programme — *Land Brandenburg*

2.6. Commission Decision 92/5/EEC provided for the EC to contribute towards costs incurred in Germany by way of compensation to owners for the slaughter of cattle infected with EBL in the new *Länder*. A two-year programme was approved, entering into force on 1 October 1991.

2.7. Examination of summaries of the underlying claims forming the basis of the EC contribution for the period 1 October to 31 December 1991 for *Land Brandenburg* established that cattle slaughtered before the operative date of 1 October 1991 had been incorrectly included. The error has now been quantified for two regions in *Land Brandenburg*, Potsdam and Frankfurt/Oder as 1 335 animals, with a resulting overcompensation by the EC of some ECU 179 000.

Enzootic bovine leucosis eradication — Suspect claims

2.8. In one case *prima facie* evidence has been found that 129 animals were not slaughtered implying that false slaughter lists had been presented in support of the EBL claim from the LPG. The failure to slaughter also has serious implications for the effective control of the disease. The case has been referred to the German authorities by the Court for consideration of the evidence and investigation.

2.9. Interim replies from the German authorities, the last of which was dated 27 February 1996, indicate that this was not an isolated case. Other cases have been detected in the course of the Commission's follow up on-the-spot checks (see paragraph 2.13 below).

Commission's on-the-spot checks of enzootic bovine leucosis eradication expenditure

2.10. Article 24 (7) of Council Decision 90/424/EEC provides for the Commission to make regular on-the-spot checks, with the cooperation of the competent national authorities, on the application of the programmes receiving a financial contribution from the Community.

2.11. On 29 June 1994, at the time the Court's audit was initiated in DG VI, no financial checks had been

carried out on the spot in respect of the Community's contribution of ECU 14,5 million to the 1991 EBL eradication programme for the territories of the new *Länder* authorized under Commission Decision 92/5/EEC.

2.12. The Commission services considered that the average compensation per animal to be slaughtered under the EBL eradication scheme should be ECU 199 and not ECU 576 as proposed by the German authorities. (According to the claim submitted by Germany for the period 1 October to 31 December 1991 the average compensation was ECU 286 per animal.) They further questioned the need to pay any compensation at all for cull cows. No evidence has been presented to the Court that these considerations were followed up with the German authorities as proposed.

2.13. The Commission has subsequently reacted positively. On-the-spot financial checks were commenced in April 1995. These checks have confirmed the Court's observations in paragraphs 2.6 to 2.9 and have established that:

- (a) claims made in respect of animals slaughtered prior to 1 October 1991 were incorrectly charged to the EC budget;
- (b) claims were made in respect of animals which had not been slaughtered;
- (c) claims were made twice for the slaughter of the same animal;
- (d) claims were made for animals slaughtered after the expiry of the time limit.

As a result the German authorities have been requested by the Commission to reimburse some ECU 11 million to the EC budget by way of a financial correction.

2.14. Furthermore the Commission's request for the financial correction referred to the fact that claims were made for animals which were slaughtered for export of the beef with export refunds thus resulting in a double subsidy.

Export refunds — General consideration of quality aspects

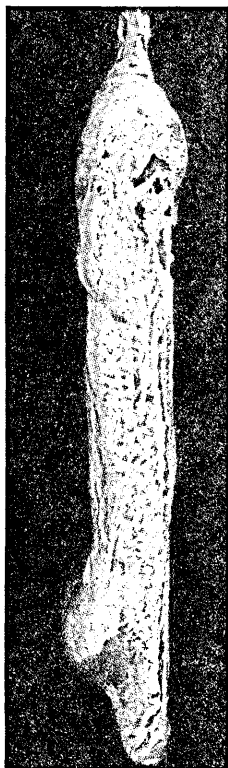
2.15. The former USSR veterinary services decided to stipulate in the technical specifications to the contracts for the supply of beef to the former USSR, that the beef should come from holdings which had been free of EBL in the preceding six months. The Commission was not aware of these contractual requirements at the time the Commission Regulations authorizing export refunds were adopted on 27 September 1990.

2.16. Former USSR veterinary controls established that contrary to this contractual specification, substantial quantities of the beef supplied to the former USSR came from EBL-infected animals. This led to a complaint indicating that the beef in question was fit for consumption only after processing (e.g. beef conserves, etc.).

2.17. In addition to the fact that a substantial quantity of the meat came from animals infected with EBL it also

was of poorest quality classification. The photograph below contrasts a Class P carcass which would have been typical of many former German Democratic Republic animals with a good quality Class E one. The existing legislation provides for the full rate of export refund to be paid on products regardless of their commercial quality provided they are of sound and fair marketable quality. Top quality beef commanding top prices attracts the same rate of refund as the poor quality beef described above. It is questionable whether financing inferior quality products at the same rate as good quality products is sound use of EC funds.

COMMUNITY SCALE FOR THE CLASSIFICATION OF CARCASSES OF ADULT BOVINE ANIMALS



E — EXCELLENT

All profiles convex to superconvex:
exceptional muscle development

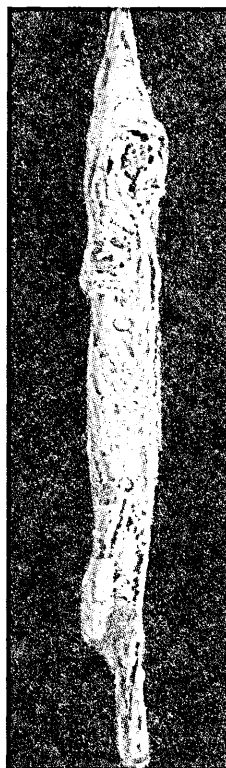
Round: very rounded

Back: wide and very thick, up to the
shoulder

Shoulder: very rounded

Topside spreads markedly over the symphysis
(symphysis pelvis)

Rump very rounded



P — POOR

All profiles concave to very concave: poor
muscle development

Round: poorly developed

Back: narrow with bones visible

Shoulder: flat with bones visible

3. CONCLUSIONS

Cumulation of subsidies

3.1. The cost to the EC budget in 1991 was ECU 72 million for compensation for the definitive cessation of milk, ECU 27 million for compensation for the temporary withdrawal of reference quantities and ECU 14,5 million for compensation for the slaughter of animals infected with EBL. The Commission services proposed these schemes in the full knowledge that prior to the assimilation of the new *Länder* into the EC on 3 October 1990, contracts had already been concluded with the former trading partners of the former German Democratic Republic for supplies of beef financed in part by EC export refunds totalling some ECU 44 million and which necessitated the slaughter of some 600 000 cattle. The slaughter of this number of cows could have played a major role in reducing the milk-producing cattle to the number required to meet the milk quota and, had these all been cows infected with leucosis, in the eradication of EBL. A substantial proportion of the ECU 99 million paid in 1991 for the reduction in milk production and the ECU 14,5 million paid in 1992 for animals slaughtered under the EBL eradication programme in 1991 could therefore have been avoided. Moreover the fact that the total subsidies granted directly or indirectly for the slaughter of individual animals largely exceeded their value as calculated by the German veterinary services, can only be considered as mismanagement of Community funds. In review of the Commission's reply the Court is aware of the specific circumstances the Commission had to deal with. Nevertheless, according to the Court the Commission's handling of the case contains a number of serious shortcomings for the following reasons:

- (a) the cumulation of export refunds, the EBL slaughter premiums and the milk cessation premiums, subsidies which overlapped each other considerably;

- (b) the fact that the Commission was fully aware of and wished to avoid the cumulation of these subsidies;

- (c) the fact that export refunds have been granted on products of inferior quality and, as it turned out afterwards, contrary to the requirements in the contracts with the former USSR.

Control of enzootic bovine leucosis eradication expenditure

3.2. The initial failure of the Commission to carry out on the spot checks of the EBL eradication expenditure has been rectified as noted in paragraph 2.13 above and as a result Germany has been requested to reimburse some ECU 11 million. This underlines the need for the Commission to meet its obligations in respect of such controls promptly.

Export refunds

3.3. In the context of German reunification, the Commission could not have been aware of the potential quality problems caused by contractual requirements when proposing the legislation authorizing the special export refunds for beef from the new *Länder*. The Commission's decision on the granting of refunds at the time it was taken was a sensible one. It has subsequently been established however that a significant quantity of this beef failed, in the deal with the former USSR, to conform with contractual specifications. Moreover and apart from this specific case the Court points out that it has already drawn attention to the general problem of refunds being granted on exports of inferior quality or on downgraded products in its Special Report No 7/93⁽¹⁴⁾. In that context the Court suggests that the Commission re-examine its policy in respect of granting refunds on such products.

This Report was adopted by the Court of Auditors in Luxembourg at its meeting of 10 April 1997.

For the Court of Auditors

Bernhard FRIEDMANN

President

⁽¹⁴⁾ Special Report No 7/93, OJ No C 53, 19. 2. 1994.

ANNEX 1

(Referred to in paragraph 2.5)

EXAMPLE OF SUBSIDIES PAID IN RESPECT OF THE SLAUGHTER OF COW NO 3409

Characteristics

Eight-years lactation

The live weight was 400 kg and deadweight 211 kg.

The meat classification was P2 (lowest quality classification on the Europ scale).

	ECU
Veterinary valuation	681
Transaction values	
Price paid for the cow by the slaughterhouse to the farm	354
Enzootic bovine leucosis compensation	327
Definitive cessation of milk production (estimate per animal) ⁽¹⁾	<u>400</u>
Total receipts for the farm	1 081
Purchase price paid by exporter to slaughterhouse	420
Exporters sales price	202
Export refunds	<u>354</u>
Total receipts for the exporter	556
Summary of subsidies	
<i>Financed by the EC</i>	
Enzootic bovine leucosis compensation	163,5
Definitive cessation of milk production ⁽¹⁾	400
Export refunds	<u>234</u>
Total	797,5
<i>Financed by Germany</i>	
Export refunds	120
Enzootic bovine leucosis compensation	<u>163,5</u>
Total	<u>283,5</u>
Grand total	<u><u>1 081</u></u>

⁽¹⁾ The calculation of the definitive cessation of milk production by cow is based upon the Commission's estimate of 28 November 1990 which states 'the milk quota scheme foresees a reduction of 20 % in milk production. This means the slaughtering of 390 000 cows for which producers get a compensation equivalent to ... around ECU 400 per cow.'

TABLE 1

Summary of costs from measures applicable in the former German Democratic Republic referred to in paragraph 1.2

Measure	EEC budget item	Budget year 1991 (million ECU)	Budget year 1992 (million ECU)	Source
Export refunds	B1-2100	n.a.	44	Export refund data supplied on magnetic tape by HZA Hamburg Jonas, the responsible paying agency
Definitive cessation	B1-2066	72	11	Declarations of expenditure from Germany to the Commission for budget Items B1-2066 and B1-2067 for the years ending 15 October 1991 and 15 October 1992
Temporary withdrawal	B1-2067	27	36	Declarations of expenditure from Germany to the Commission for budget Items B1-2066 and B1-2067 for the years ending 15 October 1991 and 15 October 1992
EBL eradication	B2-5100	n.a.	14,5	Commission's calculation of 5 October 1992 for the reimbursement of Germany

THE COMMISSION'S REPLIES

PRELIMINARY STATEMENT

1. First of all attention should be drawn to the very unusual political background to the measures concerning German reunification.

The political objective adopted by Germany and accepted by the Council and the Commission was simple and clear: to integrate the five new *Länder* into the Community, and hence into the common agricultural policy, as quickly as possible. This meant that all the rules of the CAP, with its benefits, constraints and disciplines, would apply to the new *Länder* with no transitional period and even, in the case of milk, retrospectively. That is why it was decided to make a drastic cut in milk production through a programme combining retirement and the large-scale slaughter of animals.

In order to implement this political decision, which had been very clearly expressed at the highest level, in the best possible circumstances, the Commission asked its staff to carry out the operation at the lowest possible cost to Community funds (which is why, for example, the Commission negotiated a national complement to the normal refund) and with no disturbance to the Community market (which is why the Commission supported a large-scale operation to sell to non-member countries, particularly the USSR, which had been organized by the government of the former German Democratic Republic).

When reunification came about under these political conditions, the Commission was faced by an extremely serious market situation, particularly in the beef/veal sector. The political background to German reunification and the shock caused to the management of the agricultural markets by the immediate entry to the Community of the new *Länder* should also be borne in mind.

The political imperative was therefore to help the former German Democratic Republic to adapt immediately to Community membership and to minimize any disturbances this might cause on the Community market. Decisions had to be taken very rapidly and in broad agreement with the German Government, which was itself going to support heavy costs. Although some errors subsequently came to light and had to be addressed, the exercise as a whole was highly successful.

2. The Commission was not idle in monitoring implementation of the measures taken.

A survey of veterinary expenditure on the leucosis programmes in 1991/92/93 was carried out and resulted in a recovery procedure (now in progress). Further discussions between the Commission and the German authorities took place in October 1996 so this matter is not settled. With regard to the problem of double payment or undue payments for slaughter to eradicate leucosis, the Commission's enquiries have resulted in criminal proceedings in Germany and the sending of a letter announcing a recovery order for DM 20 million.

In addition to the point mentioned by the Court, in November 1991 the EAGGF began, with the cooperation of the German authorities, an investigation into the export to Poland of animals falsely declared to be pure-bred breeding animals. This action by the EAGGF led, through the 1991 clearance of accounts procedure, to a financial correction of DM 54 million.

Similarly, after all the export operations from the former German Democratic Republic had been completed at the end of 1993, a further investigation concentrating specifically on the matters addressed by the Court's staff began. Financial corrections totalling DM 30 million, for three different amounts of irregularities detected by the Commission in this operation to export beef/veal to the former USSR, were imposed in the 1992 clearance of accounts.

If proof were needed, this measure demonstrates that, despite everything referred to earlier, the Commission's main concern in the politico-economic circumstances of reunification was to protect the Community's financial interests and correct any irregularities detected, even though 'circumstances' might have suggested a lighter touch.

Export refunds

1.5. In addition to the supplement to the refund paid on exports from the former German Democratic Republic, the Commission fixed, for a number of products, quantities exceeding the normal stock referred to in Article 7 of Regulation (EEC) No 3577/90. As a result, the export refunds granted in respect of 158 000 tonnes

of beef/veal regarded as 'normal stock' were not financed by the EAGGF but met from the German national budget.

2. OBSERVATIONS

Cumulation of subsidies

2.1 to 2.4. The Court states that the Commission was aware of the risk of duplication of aid for a single animal. Even though such cases could arise in practice, the Commission would stress that different measures, with different aims, different conditions of eligibility and applying to different numbers of animals were involved.

- Compensation for milk producers in the former German Democratic Republic under Annexes V and VI to Council Regulation (EEC) No 3577/90 of 4 December 1990 was not intended to compensate the producer for the slaughter of a dairy cow but to pay him a certain amount for reducing his right to produce milk without paying the supplementary levy imposed on producers in the former German Democratic Republic following reunification. The Commission does not consider that this compensation should be included in the amount which a particular producer in eastern Germany could receive for one and the same cow, as is done in Annex 1 to the Report.
- On the specific topic of export refunds, it should be noted that such refunds are independent of other aids and are granted solely to eliminate overproduction from the Community market and maintain market prices at an acceptable level. In economic terms, it makes no difference whether a different aid (private storage, public storage, abandonment of milk production, etc.) has already been paid for the same animals or whether different animals are exported. The refund still permits disposal of a rapid increase in supply which could not be absorbed by the domestic market.

The Commission sees no objection to granting, for one and the same cow, payments under Decision 90/424/EEC (programme for the eradication of leucosis) and export refunds when the meat from that cow is subsequently exported to a non-member country. While the payment under a programme for the eradication of disease is made to the owner of the cow, the export refund has a quite different purpose and is paid not to the owner of the cow but to the meat exporter so that surpluses on the meat market can be cleared.

In any case, German exporters were entitled to export refunds from 3 October 1990 and any restrictions on beef/veal in the former German Democratic Republic would have violated the principle of equal treatment, which is common to all the market organizations.

Restricting compensation for a reduction in milk production to those cows free of leucosis, but slaughtered to comply with milk quotas, would not only have constituted treatment different from that applied in the former Community, but would also have ignored the basic difference between the value of a cow and the right to produce milk under the Community quota scheme. The right to produce free of supplementary levy is worth considerably more than a dairy cow.

2.2 and 2.3. The Court sought evidence of the consideration given to the various issues raised about the financing of the beef sector in the new *Länder*. The negotiations and subsequent policy of the beef sector were made on the highest level by persons fully briefed on the issues raised. The Commission does not make a habit of recording the discussions held at high level, only the outcome of these discussions. In this case, the finance granted was considerably lower than that initially requested by the German authorities.

Furthermore, with regard to the financing of the reduction in milk production, the possibility considered by the Commission of first financing the eradication of bovine leucosis (referred to in paragraph 2.2) was raised in the course of a very rapid negotiating process after the Council had adopted Regulation (EEC) No 3577/90 of 4 December 1990, which finally established the system of quotas applicable to the former German Democratic Republic, provisional measures for which had already been adopted by Regulation (EEC) No 2684/90 of 26 September 1990.

That consideration, which was overtaken by events, stood no chance of being included since it ran counter to the various aims fixed for each measure (see the general reply to paragraphs 2.1 to 2.4). To have included it would have led to producers in the former German Democratic Republic being treated differently from those elsewhere in the Community. It is therefore clear that other considerations, which were also developed during this process, prevailed, since they fitted in better with Community rules and practices.

2.5. The presentation in Annex 1 aggregates a series of figures whose relevance the Commission contests, since it takes no account of the different aims of each measure and the specific conditions which had to be observed.

The Commission took the policy decision to give absolute priority to the rapid achievement of the aims fixed for each measure. Looking back, the Commission sees every reason to be satisfied that the aims laid down:

- reduction of milk production,
- potential reduction in beef/veal production,
- eradication of bovine leucosis,
- stabilization of market prices, and
- avoiding a substantial increase in intervention,

had been fully and swiftly achieved, thereby keeping Community expenditure to a strict minimum and avoiding substantial supplementary expenditure to be charged to the EAGGF budget.

Enzootic bovine leucosis eradication programme — *Land Brandenburg*

2.7. Since the errors detected by the Court in the implementation of this measure resulted from the over-declaration of expenditure to the EAGGF, recovery will be pursued by the Commission.

Enzootic bovine leucosis eradication — Suspect claims

2.8 and 2.9. This case, like a number of similar cases, is being monitored by the Commission. Legal action against those responsible is being taken by the German authorities, acting at the instigation of the Commission.

The last reply of the German authorities on exports originating in the former German Democratic Republic was dated 4 November 1996.

Commission's on-the-spot checks of enzootic bovine leucosis eradication expenditure

2.11. The Commission began its on-the-spot checks in April 1995 and sent its conclusions to the German authorities in December 1995 with a request that they recover DM 20 million in respect of 1991 and 1992.

2.12. In its reply to paragraph 2.4, the Commission has explained that no record is kept of high-level discussions. Only the outcome is recorded.

Furthermore, the Commission does not consider that the different aids can be aggregated and would stress that the compensation finally requested by Germany was considerably lower than the original figure and was estimated on the basis of the market situation.

Export refunds — General consideration of quality aspects

2.15 and 2.16. The Commission was not consulted about the trade clauses referred to because they were agreed by the former USSR and the former German Democratic Republic before reunification.

In any case, the only valid criterion in the Commission's view is whether, for export refunds to be granted, the product has to be sound, fair and marketable quality (Article 13 of Regulation (EEC) No 3665/87). A refund may not be granted or refused on the basis of trade clauses without regard to the quality criteria which apply throughout the Union. In general, if the purchasing country imposes special conditions concerning the nature of the meat, veterinary certificates may be drawn up at the request of the purchaser or the exporter. No such request was made and the situation at the time in the new *Länder* was not best suited for the implementation of effective veterinary checks.

In view of the veterinary opinion on the suitability of this meat for human consumption, the Commission cannot refuse to finance the refunds eligible under Article 13 of Regulation (EEC) No 3665/87.

2.17. Differentiating export refunds by the quality of meat would in principle indeed be desirable. However, it could not be administered and controlled at a reasonable cost. The current nomenclature for refunds includes an amount differentiated between, on the one hand, male adult bovine animals and their meat, and, on the other, female animals and their meat. This distinction imposes a series of administrative constraints and fairly cumbersome checking methods. To differentiate by quality of meat, tariff headings would have had to be created for each classification of carcase and each cut of meat, differentiated refund rates introduced and extra checks imposed, particularly on exports of boned pieces, which account for over 80 % of total exports of fresh or frozen beef/veal.

3. CONCLUSIONS

Cumulation of subsidies

3.1. The Court concludes that the Commission did not exercise the care and diligence required when proposing the measures taken in the former German Democratic Republic. It suggests that all the existing problems could have been resolved through the conclusion of export contracts between the former German Democratic Republic and its trading partners.

The Commission does not agree with this conclusion, which is based on the aggregation of aids with different aims and which, in its view, takes no account of the complex and chaotic situation which then prevailed or of the various objectives to be achieved to resolve the problems facing Germany and the Commission.

Furthermore, in its paragraph 2.16, the Court refers to the contractual clauses imposed by the USSR which restricted acceptable meat to that from collective farms which had been free of leucosis for at least six months. Since the USSR required meat to come from animals free of leucosis, it is unrealistic to conclude that the export refund would have made granting the premium for the eradication of leucosis superfluous. In any case, the existence of a contract with the former USSR did not in itself offer any guarantee of the export of quantities in question, which would not have been disposed of without Community and national finance.

Regarding the accusation of mismanagement of Community funds, the Commission disagrees, and it refers to the replies given to paragraphs 2.1 to 2.5.

Export refunds

3.3. As far as the final suggestion of the Court is concerned, the Commission agrees that this would be a desirable policy to apply; however, the Commission considers that, unfortunately, a policy of export refunds depending on the degree of quality of the product is unrealistic, as it would imply tight controls over the grading of all meat slaughtered in the EU and over the storage and transport of all meat, if the quality at export were to be determined with any degree of assurance.

The one and only criterion existing is the one that requires a 'sound, fair and marketable quality' of the product. To go beyond this criterion would create more problems than it would actually solve in terms of controls and management of the system, would undoubtedly go against the trend of simplification that the Commission is trying to follow in the export refunds domain and, last but not least, would make it very difficult to detect and prevent attempts to circumvent these additional conditions.

The Commission will, however, request the Member States to pay particular attention to the respect of the 'sound, fair and marketable quality' condition during their export scrutinies of beneficiaries' records.

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