

Special Report

Basic Payment Scheme for farmers – operationally on track, but limited impact on simplification, targeting and the convergence of aid levels

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



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ABBREVIATIONS

AR	Annual Report
BPS	Basic Payment Scheme
CAP	Common Agricultural Policy
DG	Directorate General
EU	European Union
ha	hectare
IACS	Integrated Administration and Control System
LPIS	Land Parcel Identification System
PE	Payment entitlement
SR	Special Report
SAPS	Single Area Payment Scheme
SPS	Single Payment Scheme
TFEU	Treaty on the Functioning of the European Union
WTO	World Trade Organisation

GLOSSARY

1992 reform of the CAP: The first major reform of the CAP ('the MacSharry reform') which entailed a reduction of intervention prices in the arable and beef sectors. As compensation for expected losses of income, the reform introduced direct payments for arable crop producers and for land to be taken out of production (set-aside).

2003 reform of the CAP: Introduced the decoupling of direct payments from agricultural production to enhance farmers' market orientation of and made payments conditional upon compliance with basic standards concerning the maintenance of land, the environment, food safety, animal and plant health and animal welfare (known as cross-compliance).

2013 reform of the CAP: Emphasized three policy objectives (viable food production, sustainable management of natural resources and climate action and balanced territorial development), the first of which mentions agricultural income specifically. It continued the system of direct payment decoupled from production introduced by the 2003 reform of the CAP.

Active farmer: Farmers who either carry out minimum activities on land naturally kept in a state suitable for grazing or cultivation or whose agricultural activities are not marginal. Member States have considerable leeway in defining the detailed criteria. Applicants must be able to demonstrate that they enjoy the decision making, benefits and financial risks, related to the agricultural activity on each parcel of land for which they have applied for payment entitlements.

Agricultural activity: (i) Production, rearing or growing of agricultural products and keeping animals for farming purposes; (ii) maintaining an agricultural area in a state which makes it suitable for grazing or cultivation; or (iii) carrying out a minimum activity, as defined by Member States, on agricultural areas naturally kept in a state suitable for grazing or cultivation.

Basic Payment Scheme (BPS): Basic income support scheme for farmers, based on payment entitlements. In order to receive direct payments, farmers have to 'activate' their payment

entitlements together with eligible agricultural land. The support is independent of ('decoupled from') agricultural production and income.

Common Agricultural Policy (CAP): A European policy aiming at viable food production, stabilisation of agricultural markets, income of farmers, availability of food supplies, sustainable management of natural resources and climate action, and balanced territorial development in rural areas.

Convergence: The process of adjusting payment entitlements to more equitable values per hectare. By 2019, payment entitlements will be adjusted to a national or regional average value (internal convergence). In parallel, the values of BPS payment entitlements will be adjusted, as a result of the EU's decision to seek a more equitable distribution of direct support between Member States (external convergence).

Decoupled support: Support which is not tied to the production of a specific agricultural product.

Direct payments (DP): Support schemes for farmers provided by the European Agricultural Guarantee Fund, commonly referred to as 'Pillar 1' of the CAP. They primarily aim to provide income support for farmers, but should also contribute to achieving other objectives related to land use, such as soil protection, biodiversity enhancement and climate change mitigation. There is a national budgetary ceiling for each Member State.

Economies of size: ability of a farmer to lower the average costs of production by increasing the areas farmed.

Farmer: A natural or legal person, or group of natural or legal persons, regardless of the legal status granted to such a group and its members by national law, whose holding is situated within the EU, and who carries out an agricultural activity.

Greening payment: Area-based payment for practices that benefit the environment and climate.

Holding: All the units used for agricultural activities and managed by a farmer situated within the territory of a single Member State.

National reserve: For the purpose of allocating payment entitlements primarily to new farmers or to farmers in special situations, each Member State operates a national reserve. The national reserve incorporates the difference between the respective national BPS ceiling and the total value of all allocated payment entitlements.

Negative list: List of businesses or activities such as airports, waterworks, real estate services or permanent sport and recreational grounds who are not considered 'active farmers' unless they can prove that their agricultural activities are not marginal.

Paying agency: A Member State body responsible for managing agricultural support payments.

Payment entitlement ('BPS entitlement'): Transferable right that entitles an active farmer to a stated amount of support if declared together with one hectare of eligible agricultural land.

Single Payment Scheme: Income support scheme for farmers decoupled from production and introduced by the 2003 reform of the CAP. In order to receive direct payments, farmers had to have payment entitlements and 'activate' them together with eligible agricultural land.

Windfall Profit: Profit that occurs unexpectedly, for example from changes in legislation.

WTO Agreement on Agriculture: Result of negotiations in the 1986–94 Uruguay Round where member countries of the World Trade Organisation (WTO) agreed to improve market access and reduce trade-distorting subsidies in agriculture.

EXECUTIVE SUMMARY

I. The 2013 reform of the Common Agricultural Policy introduced a new basic payment scheme (BPS) for farmers, which is applied in 18 Member States¹. BPS, like its predecessor, the Single Payment Scheme (SPS), aims to provide a basic income support to farmers and thus contribute to viable food production in the EU, without distorting production decisions. With an annual expenditure of around 18 billion euro granted to some 4 million farmers it is the EU's biggest income support scheme for farmers.

II. Our main audit question in this report was whether Commission and Member States set the BPS properly on track. We conclude that the scheme is operationally on track, but that its impact on simplification, targeting and the convergence of aid levels is limited.

III. The introduction of the BPS required substantial efforts by the national authorities but the control systems of the Member States we visited largely mitigated the risk of incorrect calculation and allocation of entitlements. The resulting BPS payments were overall not materially affected by error. However, in 2017, in some cases BPS entitlement values were still inaccurate, calculated only provisionally or based on estimates, and some paying agencies we visited faced particular difficulties.

IV. The Commission provided Member States with extensive guidance in this process. In spite of the clarifications provided, Member States did not always interpret specific calculation rules consistently and did not provide all monitoring information to the Commission. Overall, the Commission's own audits yielded good results, but it could have demanded more from the certification bodies.

V. One of the guiding principles of the 2013 reform of the CAP was simplification. The complex EU rules on BPS and eligible land contained numerous options and exceptions for implementation of the scheme. Calculation rules and options chosen by Member States did

¹ Belgium, Denmark, Germany, Ireland, Greece, Spain, France, Croatia, Italy, Luxemburg, Malta, the Netherlands, Austria, Portugal, Slovenia, Finland, Sweden and the United Kingdom. The remaining Member States, which joined the EU in 2004 or 2007, apply a similar but transitory scheme, the Single Area Payment Scheme (SAPS).

not always favour simplification, but sometimes added complexity, increased the burden on national administrations, and allowed some farmers to realise windfall profits.

VI. The 2013 CAP reform introduced a negative list aimed at excluding beneficiaries whose primary function was not agriculture. Use of this list was only partly effective, could result in differing treatment of similar applicants and represented a significant administrative burden for paying agencies. In consideration of these difficulties, Council and Parliament agreed that – as from 2018 – Member States can decide whether they reduce the criteria by which applicants can demonstrate their ‘active farmer’ status, or discontinue the application of the ‘negative list’.

VII. The reform also extended the categories of land on which support is payable, and enabled Member States to take measures reducing the risk of speculative claims. In an attempt to better target support at agricultural land, however, it created difficult implementation problems.

VIII. The 2013 reform of the CAP represented a move towards more equal support levels per hectare. Under the reform, as a general rule, all payment entitlements activated in 2019 in a Member State or in a region should have a uniform unit value, but only six of the 18 Member States chose this option for the whole or a major part of their territory and a seventh by 2020. As a derogation, the other Member States were allowed to take historical factors into account when calculating the value of payment entitlements which farmers should have in 2019. Member State choices have had a significant impact on the degree of redistribution of support and farmers could in some cases freeze particularly high support levels resulting from past levels of subsidy.

IX. As a scheme essentially related to areas, BPS support tends to favour larger farms. Due to the design of the scheme, the Commission expects that with the 2013 CAP reform the capitalisation of the support in land prices will increase, which benefits owners of agricultural land.

X. BPS support is a significant source of income for many farmers but has inherent limitations. It does not take account of market conditions, use of agricultural land or the

individual circumstances of the holding, and it is not based on an analysis of the overall income situation of farmers.

XI. The objective of the Treaty to ensure a fair standard of living of farmers and the general CAP objective of viable food production and farmers' incomes have not been translated into measurable targets yet and there is no baseline to which the results achieved could be compared.

XII. As regards the current BPS scheme applicable until 2020, we make a number of recommendations to the Commission concerning the calculation and allocation of BPS entitlements, addressing the appropriate implementation of paying agencies' key controls, the Commission's systems for disseminating information among Member States, and the role of certification bodies.

XIII. As regards the development of its proposals for the next programming period, we recommend that the Commission analyse the factors impacting income for all groups of farmers, their income support needs and the value of the public goods that farmers provide, and that it links, from the outset, the proposed measures to appropriate operational objectives and baselines against which the performance of the support could be compared.

INTRODUCTION

1. Increasing agricultural productivity and thus ensuring a fair standard of living for farmers are key objectives of the Treaty and a major concern of the Common Agricultural Policy (CAP)². Prior to 1992, the CAP focused on supporting guaranteed prices (intervention prices) for agricultural products. This resulted in substantial overproduction and disproportionate growth in EU expenditure. The 1992 reform of the CAP reduced intervention prices for cereals and beef, and obliged larger farms to set aside part of their land. To compensate for the expected income losses that followed the fall in cereal and beef prices, producers received direct payments which were coupled to sown areas or animal numbers. The overall level of spending was restricted by sector specific regional or national ceilings.
2. The 2003 reform of the CAP left the overall level of direct support unchanged, but introduced a system of income support for farmers related to agricultural areas but without obligation to produce ('decoupling'), known as the Single Payment Scheme (SPS). A similar but transitory decoupled scheme, the Single Area Payment Scheme (SAPS), was available for farmers in Member States that joined the EU in 2004 and 2007. As support in various agricultural sectors was successively integrated into the SPS, it became the largest EU income support scheme for farmers.
3. In our previous work on the SPS we found that this scheme ensured a certain level of income support and gave farmers freedom to produce what was in demand in markets. However, we also identified a lack of precision in the way key terms such as 'farmer', 'eligible land' and 'agricultural activity' were defined. We recommended that support should be targeted at 'active farmers', that eligible land and agricultural activity should be more clearly defined, and that the calculation of payment entitlements should be based on current

² See Article 39 of the Treaty of on the functioning of the European Union (OJ C 326, 26.10.2012, p. 47).

farming conditions in the various regions³. We also found that the SPS contained calculation errors and internal control weaknesses in Member States and recommended that paying agencies correct errors and adopt clear procedures to include effective checks on the reliability of the data underlying the calculations and on the accuracy of payment entitlements⁴.

4. The 2013 reform of the CAP continued the system of decoupled support but was accompanied by a slight reduction in the overall budget available for direct payments for the period from 2014 to 2020⁵. It introduced a new structure of direct payments to farmers which consists of the basic payment scheme (BPS)⁶, which is also open to Member States that introduced the SAPS, a payment for agricultural practices beneficial for the climate and the environment⁷ and support for young farmers⁸. In addition, Member States can avail themselves from a number of options expected to better target the support to farmers in sectors or regions with economic difficulties, or at smaller farms.

5. The BPS took effect as from claim year 2015 (with payments financed by the 2016 EU budget) and 18 Member States currently apply the scheme⁹. It is the largest EU direct support scheme for farmers, costing around 18 billion euro per annum and is financed

³ Special Report No 5/2011 'Single Payment Scheme (SPS): issues to be addressed to improve its sound financial management'.

⁴ Special Report No 8/2014 'Has the Commission effectively managed the integration of coupled support into the SPS?'.

⁵ Annex II of Regulation (EU) No 1307/2013 of the European Parliament and of the Council of 17 December 2013 establishing rules for direct payments to farmers under support schemes within the framework of the common agricultural policy and repealing Council Regulation (EC) No 637/2008 and Council Regulation (EC) No 73/2009 (OJ L 347, 20.12.2013, p. 608).

⁶ Title III, Chapter 1, Section 1, of Regulation (EU) No 1307/2013.

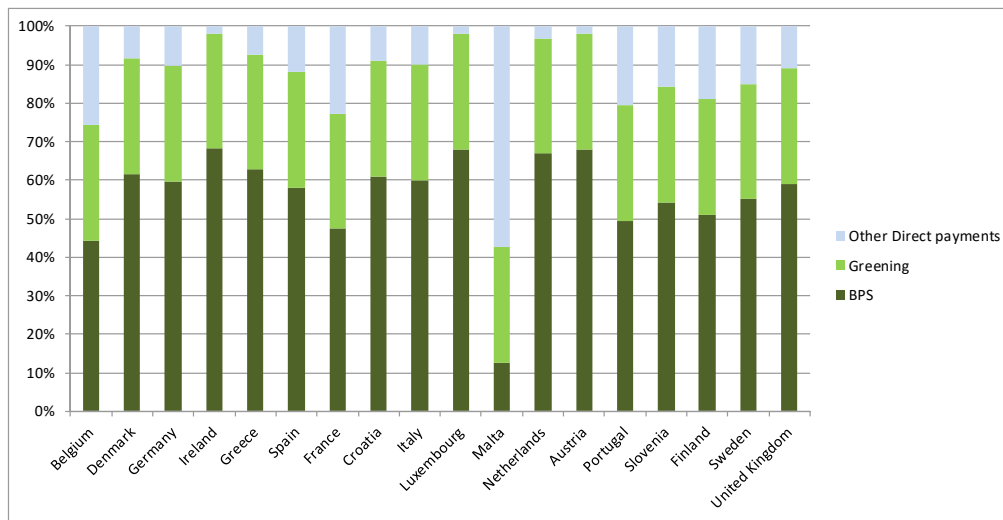
⁷ The so-called 'greening payment'; Article 43(1) of Regulation (EU) No 1307/2013.

⁸ Article 50 of Regulation (EU) No 1307/2013.

⁹ Belgium, Denmark, Germany, Ireland, Greece, Spain, France, Croatia, Italy, Luxemburg, Malta, the Netherlands, Austria, Portugal, Slovenia, Finland, Sweden and the United Kingdom. The other Member States continued to apply the SAPS.

entirely from the EU budget. In 2015 some 4 million EU holdings were receiving BPS support. Based on Member States' decisions about how to allocate the national budgetary ceiling to the various direct support schemes, the Commission calculates the amounts available for BPS support each year which ensures that a maximum of the available budget can be disbursed to the farmers¹⁰. As a consequence, the share of BPS support in total EU direct payments can vary significantly across Member States (see **Figure 1**).

Figure 1 – Share of BPS support in EU direct payments per Member State in 2015



Source: European Court of Auditors.

6. The EU legal framework of the 2013 CAP reform defines viable food production as a general objective of direct support¹¹. BPS, like its predecessor, the SPS, aims to provide basic income support for farmers without distorting production decisions¹². This should provide a

¹⁰ See **Annex I**.

¹¹ Article 110 of Regulation (EU) No 1306/2013 of the European Parliament and of the Council of 17 December 2013 on the financing, management and monitoring of the common agricultural policy and repealing Council Regulations (EEC) No 352/78, (EC) No 165/94, (EC) No 2799/98, (EC) No 814/2000, (EC) No 1290/2005 and (EC) No 485/2008 (OJ L 347, 20.12.2013, p. 549).

¹² See recital 24 of Regulation (EC) No 1782/2003 of 29 September 2003 establishing common rules for direct support schemes under the common agricultural policy and establishing certain support schemes for farmers and amending Regulations (EEC) No 2019/93, (EC) No 1452/2001, (EC) No 1453/2001, (EC) No 1454/2001, (EC) No 1868/94, (EC) No 1251/1999, (EC)

safety net for farmers exposed to a high volatility of market prices for their products and thus help to stabilise their income while allowing them to make production decisions on the basis of the market demand. As a decoupled support scheme, it is independent of agricultural production and is thus in line with international trade agreements¹³.

7. The payment of support is conditional to maintaining agricultural areas in a state which makes them suitable for grazing or cultivation. It thus has the effect of helping to preserve the EU's agricultural production potential and thus avoid the abandonment of land. Holdings in receipt of the support have to comply with minimum maintenance standards to ensure the good agricultural and environmental conditions of the land and have to respect certain obligations regarding food safety, animal and plant health and animal welfare for their farm (cross-compliance). This should contribute to achieve other general CAP objectives related to land use, such as soil protection, biodiversity and climate change mitigation.

Key elements of the basic payment scheme

8. Access to BPS support is conditional upon possession of payment entitlements ('BPS entitlements'). Each entitlement gives its holder a transferable right to an annual payment of a given amount of BPS support, provided that it is declared together with one hectare of eligible agricultural land ('activation'). In principle, this comprises all arable land, permanent grassland and land under permanent crops. The maximum total value of all BPS entitlements in a given region or Member State is contained within a fixed budgetary ceiling.

9. Eligibility for the BPS (and possession of BPS entitlements) is also a precondition for farmers to receive other direct payments such as the 'greening' payment, the redistributive payment¹⁴ and the payment for young farmers. Most Member States chose to pay the 'greening' payment - and many the 'young farmers' payment - as a fixed percentage of the values of the payment entitlements activated by applicants. This means that an incorrect

No 1254/1999, (EC) No 1673/2000, (EEC) No 2358/71 and (EC) No 2529/2001 (OJ L 270, 21.10.2003, p. 1).

¹³ WTO Agreement on Agriculture (OJ L 336, 23.12.1994, p. 22).

¹⁴ Article 41 of Regulation (EU) No 1307/2013.

allocation of BPS entitlements (in terms of value or number) also affects the correctness of payments under other direct support schemes.

10. BPS is addressed to farmers. Farmers are defined as all natural, legal or groups of persons having an agricultural activity by which they either produce agricultural products, maintain agricultural land in a state which makes it suitable for grazing or cultivation, or carry out a minimum activity on agricultural areas naturally kept in a state suitable for grazing or cultivation.

11. From 2015, to ensure that support is better targeted to 'active farmers', certain businesses that could be involved in land management but whose business purpose was only marginally targeted at an agricultural activity such as airports, railway services, waterworks, real-estate services or persons managing permanent sport or recreational grounds and who had received direct payments above the threshold set by Member States¹⁵, had to prove that their agricultural activities were significant if they applied for support. Member States were entitled to adopt tighter rules by adding further businesses to the list or by generally excluding all persons whose agricultural activities formed only an insignificant part of their overall economic activities or whose principal business activities did not consist of carrying out agricultural activities.

12. Under the former SPS, the values of payment entitlements in most Member States depended on the value of the historical support payments coupled to production which each farmer had received in a given reference period¹⁶. As a result, individual support levels per hectare could thus vary significantly between farmers depending on their historical support levels¹⁷.

¹⁵ Article 9(2) and (4) of Regulation (EU) No 1307/2013.

¹⁶ As a rule, these were the average coupled payments farmers received in the years from 2000 to 2002.

¹⁷ Most Member States calculated SPS payment entitlements solely on the basis of historical payments. For details, see Annex I of Special Report No 5/2011 'Single Payment Scheme (SPS): issues to be addressed to improve its sound financial management'.

13. The 2013 CAP reform aimed to remove - or at least reduce - these historical components in the values of payment entitlements over time and approximate them towards uniform values per hectare by 2019 at the latest ('internal convergence'). In order to avoid disruptive financial consequences for farmers, Member States could maintain a historical component in the value of payment entitlements beyond 2019. This meant that the value of farmers' historical payments under previous, coupled support schemes will continue to be reflected in the values of BPS entitlements until another future reform of the CAP. However, as set out in **paragraph 67** below, the impact of these divergences will be reduced over the period to 2019.

14. Between 2016 and 2019, the amounts available for BPS further change, because Member States will see their national ceilings increase or decrease ('external convergence')¹⁸.

15. Member States had a choice of three basic models for establishing the value of BPS entitlements (see **Figure 2**):

¹⁸ Other adjustments may occur if Member States decide to modify the allocation of direct payments to specific schemes, e.g., if they need more (or less) support for young farmers. In this case, Member States have to linearly reduce (or increase) the value of all BPS payment entitlements.

Figure 2 – Basic models for implementing the BPS

Flat-rate in 2015
All BPS entitlements in a Member State (or region) have the same value.
Full convergence towards a flat-rate by 2019 (or 2020)
Farmers receive BPS entitlements on the basis of their individual 2014 reference amount. By 2019, this value will be adjusted to a uniform flat-rate.
Partial convergence by 2019
Member States had to ensure that by 2019 every BPS entitlement will be worth at least 60 % of the respective national or regional average unit value. This increase in value is financed by those farmers who hold above-average value BPS entitlements. Member States could cap the reductions of these farmers' BPS entitlements at 30 %.

Source: European Court of Auditors.

16. Within the basic BPS models, Member States had a variety of options for implementing the scheme. These options enable Member States to give effect to national preferences for the level at which they wanted to apply the scheme (national or regional), the calculation of reference amounts for farmers and values of their BPS entitlements, how to better target support at 'active farmers' and how to determine the area eligible for allocation of BPS entitlements¹⁹.

Calculation and allocation of BPS entitlements

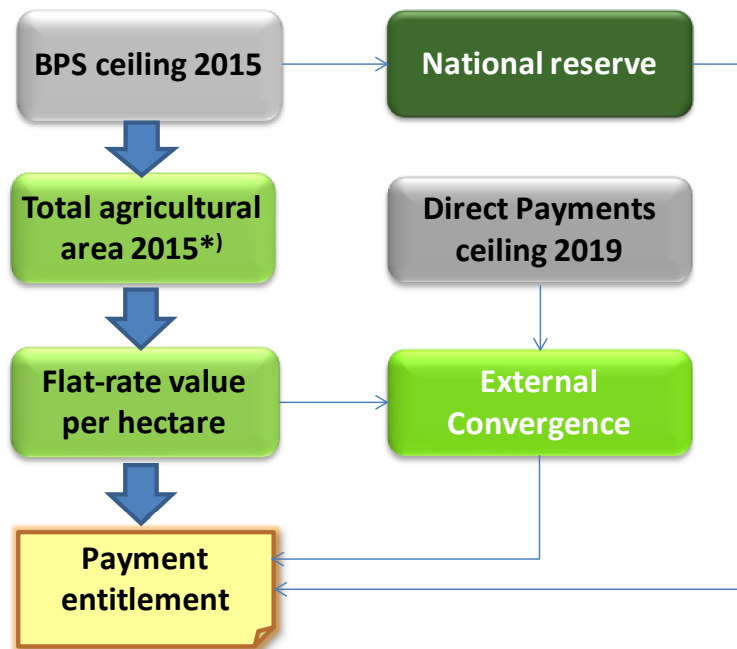
17. Member States had to establish BPS entitlements in 2015 and allocate them to farmers. They also had to earmark a certain amount of the available budget in a national reserve to

¹⁹ See [Annex II](#) for the options chosen by Member States.

allocate BPS entitlements to young farmers, farmers commencing their agricultural activity or farmers in specific situations²⁰.

18. As a rule, in all BPS models the number of payment entitlements allocated to farmers was equal to the number of eligible agricultural hectares they farmed in 2015. The value depended on the specific BPS model which the Member State or region had chosen. Where Member States already applied a flat-rate model of the BPS in 2015, all farmers in a given region received BPS entitlements at the same unit value per hectare (see **Figure 3**).

Figure 3 – Elements for calculating BPS entitlements (flat-rate model)



^{*)} Excluding area for PE from the national reserve

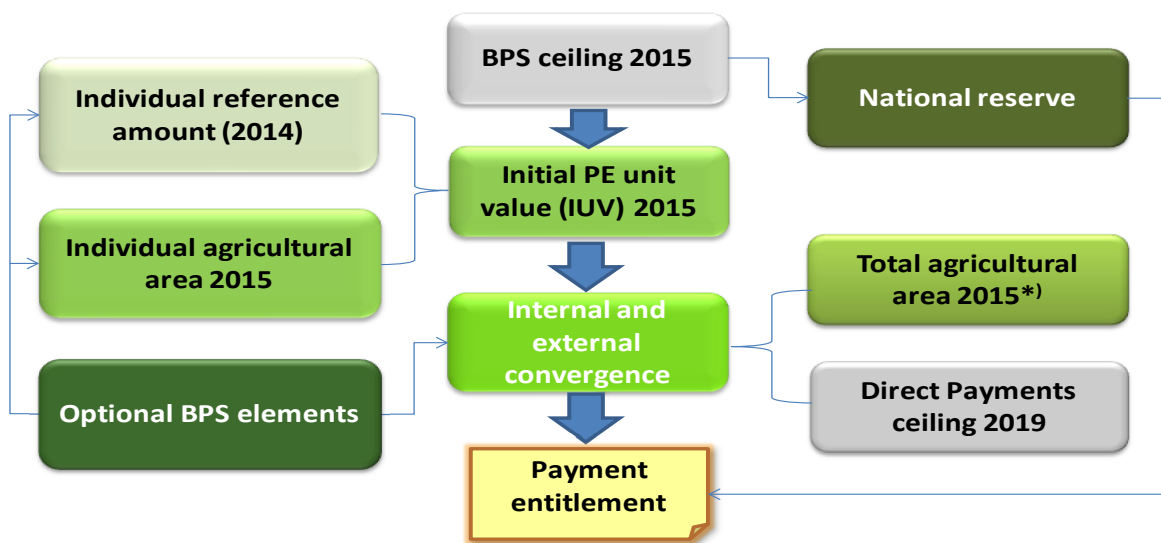
Source: European Court of Auditors.

²⁰ E.g. to prevent land from being abandoned or in cases of *force majeure* or exceptional circumstances.

19. In those Member States which opted for a convergence model of BPS, i.e. which did not apply uniform per hectare values in 2015, the national authorities in principle based their calculations on six elements (see **Figure 4**)²¹:

- the 2015 total eligible agricultural area of all ‘active farmers’ in a given Member State or region;
- the agricultural area eligible in 2015 for each individual applicant;
- the 2015 applicants’ individual reference amount for 2014²²;
- the total reference amounts for 2014 for all 2015 ‘active farmers’;
- the national or regional ceilings applicable in 2015 for the BPS;
- the national or regional target value (national or regional average) for 2019.

Figure 4 – Elements for calculating BPS entitlements (convergence models)



Source: European Court of Auditors.

²¹ Articles 24 to 26 of Regulation (EU) No 1307/2013.

²² In principle, these were the direct payments which a farmer had received in 2014 or the value of SPS entitlements owned.

20. All convergence models shared the feature that Member State paying agencies had to establish the individual reference amount for each farmer and deal with changes in a farmer's personal situation such as mergers, divisions or transfers of land that occurred between 2014 and 2015. To avoid complexity, Member States that had applied SPS on a regional basis could maintain existing SPS entitlements, which became BPS entitlements²³.

The roles of the Commission and Member States in introducing the BPS

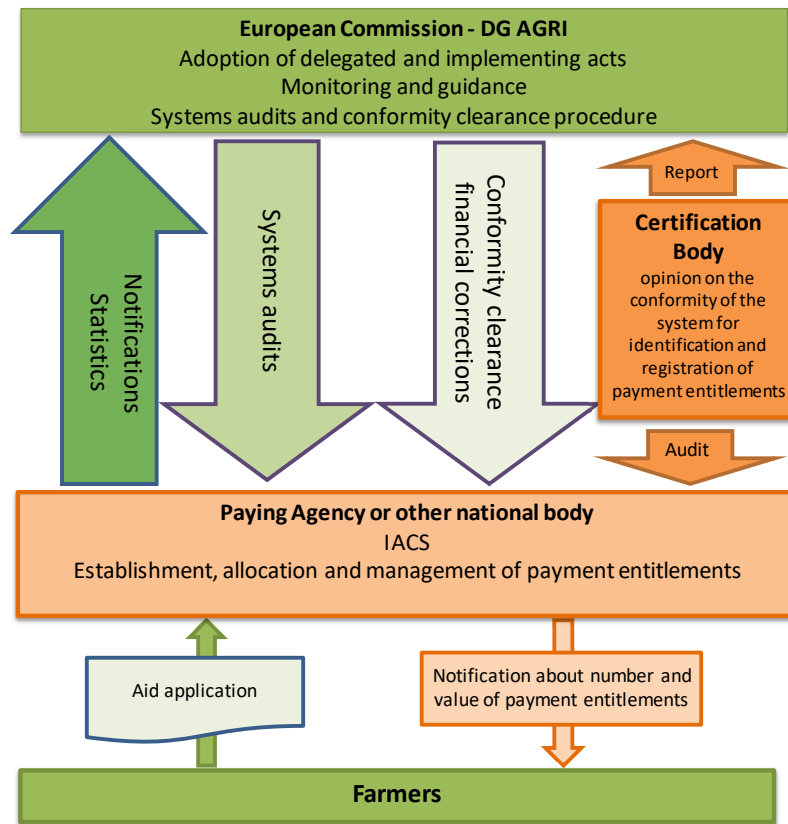
21. The Commission and Member States are jointly responsible for managing the BPS and other direct payment schemes. However, the Commission retains ultimate responsibility for implementing the budget²⁴. This means that the Commission had to ensure that the BPS was implemented correctly by means of appropriate delegated legal acts, by monitoring the management of the BPS in the Member States and by compliance audits of the control systems for administering the scheme. In the event that national implementation does not comply with the EU legal framework, the Commission can apply financial corrections.

22. Member States calculated BPS entitlements and recorded them in a specific database. They also had to ensure that accredited paying agencies subsequently paid BPS support to farmers. For this purpose, the national authorities were required to use the Integrated Administration and Control System (IACS) in order to ensure that payments were correct and that irregularities were prevented. Using reliable information about agricultural areas and a system of automated cross-checks, the IACS should also support farmers in making correct declarations and thus efficiently identify potential irregularities. In addition, an independent national certification body was required to audit the legality and regularity of all EU expenditure which the paying agencies disbursed. ***Figure 5*** shows the Commission and Member State roles in implementing the BPS.

²³ Denmark, Sweden, Finland and the United Kingdom (England) chose this option. In this case, the 2014 values and numbers of SPS entitlements had to be adjusted to the 2015 available BPS budget and eligible areas. In England all SPS entitlements already had a regional uniform value per hectare in 2014.

²⁴ Article 317 TFEU.

Figure 5 – Commission and Member State roles in implementing the BPS



Source: European Court of Auditors.

AUDIT SCOPE AND APPROACH

23. The objective of this audit was to determine whether in 2015 the Commission and the Member States introduced the BPS in line with the EU legal framework and the objectives of the CAP. In this context, we also reviewed features resulting from the design of the BPS as a scheme providing decoupled income support for farmers. We sought to answer the main audit question:

Basic payment scheme for farmers - did the Commission and the Member States set the scheme properly on track?

24. In order to answer this question, we checked whether:

- the Member States' control systems mitigated the risk of BPS payment entitlements being calculated incorrectly;

- the Commission adequately supported the Member States' introduction of the basic payment and sufficiently supervised and audited Member States;
- the introduction of the BPS contributed to simplification for both farmers and administrations and was in line with the objectives of the CAP.

25. We carried out our audit between September 2016 and April 2017 and it included:

- a survey sent to all 18 Member States which had introduced the BPS to obtain key data and information on their set-up and implementation. Where appropriate, we used the results for our reporting;
- visits to the European Commission - Directorate General for Agriculture and Rural Development - and to six Member States (Germany (Niedersachsen), Greece, Spain, France, Italy and the United Kingdom (England and Scotland)) selected on the basis of their share of the EU budget available for the BPS and the specific model they had chosen for implementing the scheme. We carried out interviews, analysed procedures and data and examined relevant documents;
- the audit of a sample of 400 files of farmers' payment entitlements from claim year 2015. We selected them partly at random and partly on the basis of a risk assessment in order to review the calculations of BPS entitlements and the key controls applied.

In addition, we considered the results of our work for the 2016 statement of assurance.

OBSERVATIONS

Control systems of Member States visited largely mitigated the risk of incorrect calculation and allocation of BPS entitlements but national choices could pose particular challenges for some paying agencies

Most Member States coped with challenges and, overall, BPS payments to farmers were not affected by a material error...

26. All the Member States we visited had to face a number of challenges in implementing the BPS. Their nature depended largely on the options they had chosen. In particular, they had to:

- check the applicants' entitlement to BPS support i.e. whether they had been beneficiaries of direct support in 2013 and were 'active farmers' in 2015;
- establish the individual reference amount of each farmer where the Member State did not apply a flat-rate per hectare;
- determine each farmer's eligible agricultural area 2015 on the basis of the most recent information from the Land Parcel Identification Systems (LPIS) and the checks on-the-spot. This could also require the identification of land not eligible prior to the introduction of the BPS;
- establish the value of the BPS entitlements for 2015 to 2019 after completing all checks and calculations;
- inform the farmers concerned by the end of 2015 or, where the national authorities only had provisional data at hand, by 1 April 2016;
- pay BPS and other direct support by 30 June 2016.

27. Most Member States coped with the challenges and terminated their calculations within or close to the legal deadlines. However, for Spain, France, Italy, the Netherlands, Austria, Sweden and the United Kingdom (Scotland) which were unable to make final

payments to all farmers within the legal deadline of 30 June 2016, the Commission allowed payments without reductions up to 15 October 2016²⁵.

28. On the basis of the data available, across the EU, payments based on BPS entitlements were overall not materially affected by error²⁶. However, calculation errors could affect payments to many individual farmers and reduce the reliability of the databases of BPS entitlements as explained hereafter.

...but in some cases BPS entitlement values were inaccurate, calculated only provisionally or based on estimates...

29. We found that Member States (or regions) had, for the most part, correctly applied the general calculation rules and, with the exception of Italy and one region in Germany (Mecklenburg-Vorpommern), respected the applicable national or regional ceilings. However, in some cases we found that BPS entitlement values were inaccurate, calculated only provisionally or based on estimates, affecting the distribution of payment across individual farmers:

- (a) In the United Kingdom (Scotland), the authorities had not correctly applied the calculation rules for determining the 2019 target flat-rate values and the annual budgetary adjustments until that year. In the Netherlands, the authorities calculated an incorrect convergence value for the adjustment of payment entitlements towards the 2019 flat rate. However, this did not affect the total amount of payments in Scotland and the Netherlands but had only a small impact on the distribution of payments across individual farmers.
- (b) France and the United Kingdom (England and Scotland) used provisional data or estimates, as they encountered particular difficulties in calculating definitive BPS

²⁵ Article 5(4) of Regulation (EU) No 907/2014 (OJ L 255, 28.8.2014, p. 18). The Commission is obliged to reduce or exclude from EU financing payments, which Member States make to the farmers after expiry of the legal deadlines. In this case, the Member States have to finance the part of the payments, which the Commission does not reimburse from their own budget.

²⁶ See paragraph 1.15 and chapter 7 of our Annual Report 2016 of the implementation of the budget for the financial year 2016 (OJ C 322, 28.9.2017, p. 1).

entitlement values in good time. This impacted the accuracy of BPS entitlement values, because changes in one element of the calculation (such as the total eligible area) entailed potential changes in other elements (such as the value of entitlements) and could have further implications for the calculation of convergence. It also meant that farmers did not know the definitive value of their BPS entitlements before applying for the next claim year. We describe below some of the different issues faced.

- (i) In France, the paying agency was still in the process of calculating the definitive value of the 2015 BPS payment entitlements in May 2017 and had not formally allocated them to farmers. The delay is explained by the late introduction of a new system for land parcel identification, difficulties in identifying non-agricultural areas and significant delays in the 2015 on-the-spot checks of farmers, which the French authorities only completed in December 2016²⁷.
- (ii) The United Kingdom (England and Scotland) encountered significant delays in calculating payment entitlement values, because in England, which had opted to maintain the former SPS entitlements, full land-cover data were not available on time. Thus, the authorities could only estimate the final eligible area which, however, was a key element needed to calculate payment entitlement values accurately. Moreover, a new computer system for processing claims did not perform as expected and forced the paying agency to return to paper applications. This caused serious difficulties as regards adjusting BPS entitlements to eligible areas and meeting the payment deadline²⁸. In Scotland, the authorities also encountered difficulties in processing all claims in good time, partly because they had a backlog in the identification of eligible permanent grassland. They made only illustrative calculations of BPS entitlement values in order to

²⁷ According to the data which the French authorities provided, the provisional values were by between 0.5 % and 2.9 % lower than the likely actual values in 2015 while for the following years the authorities had not yet made any calculation.

²⁸ Under the specific BPS model applied in England, payment entitlements that exceeded the eligible areas which farmers declared in their aid applications had to be cancelled. Those not duly cancelled could result in irregular support payments in later claim years.

meet the deadlines for disbursing support, but in May 2017 they had still not established final values²⁹.

...and some paying agencies visited faced particular difficulties

30. Paying agencies had to set up effective key controls to ensure that the number and value of BPS entitlements allocated to farmers were accurate. This involved cross-checking the eligibility of areas which farmers had declared in their aid applications against the data in the LPIS³⁰ and against historical reference data, as well as verifying the authenticity of the supporting documentation provided by farmers and reviewing of the calculation of BPS entitlements. We describe in the following paragraphs some of the different issues faced in the Member States we visited.

31. In Italy, a central coordination body outside the internal control framework of the Italian paying agencies was responsible for calculating BPS entitlements and allocating them to farmers. It had not completed all checks regarding the eligibility of farmers and there were still uncertainties about the eligibility of a significant share of the permanent grassland. This resulted in an iterative process by which the same coordination body had to recalculate the values of around one third of BPS entitlements after they had initially been allocated. Finally, their total value exceeded the national budgetary ceiling. According to EU legislation, this would have required a further adjustment of the value of all Italian BPS entitlements. The impact on the payments of support to the farmers is likely to be small overall, but could be more significant at individual farmer level. Recalculations were still ongoing in April 2017

²⁹ Depending on the region, we estimate the overall impact for Scotland on the actual 2019 flat-rate values to be by 2.9 % lower and 4.6 % higher than the values which the authorities had calculated.

³⁰ See also Special Report No 25/2016 'The Land Parcel Identification System: a useful tool to determine the eligibility of agricultural land – but its management could be further improved'.

and affected also the values of BPS entitlements and subsequent support payments for future years³¹.

32. Reliable information in the LPIS on the actual eligible area of the parcels claimed was another key factor for correctly establishing BPS entitlements. In two of the six Member States we visited, we found that information in the LPIS was overall up-to-date. In France, Italy and the United Kingdom it was in the process of being updated, largely in parallel with the calculation of BPS entitlements³². The Greek paying agency, which had made major efforts over several years to correctly identify permanent grassland, lacked the necessary national funds to update the entire LPIS with the most recent available information. Thus, in 2015, the authorities had to base the calculation of BPS entitlements on images dating back to 2008 for more than half of the territory concerned³³.

33. Around 90 % of all permanent grassland in Greece and more than 25 % of the country's agricultural area is public land. For this type of land, the Greek authorities calculated the BPS entitlements on the basis of the average regional number of animals per hectare and the number of animals which each farmer had declared in their aid application³⁴. However, unreliable information in the animal register made it more difficult to calculate the number of BPS entitlements allocated to farmers accurately³⁵.

³¹ In order to cover the financial risk the Italian authorities decided to hold back 7 % of the payments for application year 2016.

³² In July 2016 the Commission decided to withhold 3 % of the monthly payments relating to area-related aid declared by France in respect of the year 2015 for the significant delays in updating the LPIS.

³³ By the year 2017 more recent ortho-images were available but 33 % of the agricultural had not been updated.

³⁴ Article 39(2) of Commission Implementing Regulation (EU) No 809/2014 of 17 July 2014 laying down rules for the application of Regulation (EU) No 1306/2013 of the European Parliament and of the Council with regard to the integrated administration and control system, rural development measures and cross compliance (OJ L 227, 31.7.2014, p. 69).

³⁵ This was underpinned by error rates which the national authorities had found in their animal related checks, although not all errors may relate to weaknesses in the animal register.

The Commission adequately supported the introduction of the BPS but could have demanded more from the certification bodies

Overall, the Commission supervised the implementation process well and provided extensive guidance...

34. The wide range of options for Member States which EU legislation envisaged made the provisions more complex which carried the risk of misinterpretation and ambiguity. The Commission succeeded in providing implementing provisions on time³⁶. However, Member States required additional guidance from the Commission regarding their specific model of implementation. Consequently, since 2014 the Commission has issued more than 400 guidance notes to Member States and held bilateral meetings with the national authorities in order to ensure smooth implementation of the BPS and the other EU direct support schemes. In spite of the clarifications provided, Member States did not always interpret specific calculation rules consistently.

...but Member States did not provide all monitoring information

35. As the Commission is responsible for monitoring the scheme, all Member States applying the BPS had to inform the Commission about their choices which allowed the Commission to carry out an in-depth analysis of their compliance with the EU legal framework and take follow up action. However, in May 2017 the Commission still lacked key information such as the total value of the 2015 BPS entitlements allocated to farmers from France and Italy which together accounted for 31 % of the available budget. The lack of this information made the monitoring of the scheme more difficult. Under EU legislation, the

³⁶ Commission delegated Regulation (EU) No 639/2014 of 11 March 2014 supplementing Regulation (EU) No 1307/2013 of the European Parliament and of the Council establishing rules for direct payments to farmers under support schemes within the framework of the common agricultural policy and amending Annex X to that Regulation and Commission implementing Regulation (EU) No 641/2014 of 16 June 2014 laying down rules for the application of Regulation (EU) No 1307/2013 of the European Parliament and of the Council establishing rules for direct payments to farmers under support schemes within the framework of the common agricultural policy (OJ L 181, 20.6.2014, p. 1 and p. 74).

Commission was not entitled to reduce payments to Member States if they did not submit specific statistical information on the BPS on time.

Overall, the Commission's own audits yielded good results...

36. The Commission had launched in good time the audit of the implementation of the BPS in the Member States, which produced good results, although a lack of resources prevented them from carrying out all audits on-the-spot as planned. Due to the early timing of most of the visits, the Commission was also unable to assess the quality of the certification bodies' review of the calculation of BPS entitlements.

37. The Commission audit work focused mainly on reviewing samples of transactions and the eligibility of areas declared. It placed less emphasis on validation of general calculations, the internal controls applied and whether Member States had systems in place which allowed for close monitoring of the management of BPS entitlements such as the calculation of and compliance with applicable ceilings, and the management of the national reserve including procedures for cancelling BPS entitlements.

...but it could have demanded more from the certification bodies

38. All EU expenditure which Member State paying agencies disburse is subject to an annual certification audit by an organisationally independent body. These auditors should provide an opinion, drawn up in accordance with internationally accepted audit standards, on the completeness, accuracy and veracity of the paying agencies' annual accounts, on the proper functioning of their internal control system and on the legality and regularity of the expenditure for which reimbursement has been requested from the Commission³⁷. As the value of the BPS entitlements is a key element for the calculation of the amounts of support disbursed to farmers, the certification bodies' check of the calculation of BPS entitlements was particularly important. With the ongoing convergence and possible adjustments of BPS entitlement values this is also relevant for subsequent financial years.

³⁷ See also Special Report No 7/2017 'The certification bodies' new role on CAP expenditure: a positive step towards a single audit model but with significant weaknesses to be addressed'.

39. The Commission specified in its guidelines for the certification bodies that their checks should include an ‘assessment of the procedures in place to ensure the correct allocation of BPS entitlements’ and asked the certification bodies to express an opinion as to whether paying agencies had set up a proper system for identifying and registering BPS entitlements and applied appropriate controls to the establishment of the scheme. The Commission guidelines required compliance testing of ten transactions, but did not explain what checks the certification bodies were supposed to make regarding the accuracy of the calculations.

40. In the Member States we visited the certification bodies had interpreted the Commission guidelines in different ways and the number of transactions that the Commission recommended for compliance testing was too low to arrive at valid overall conclusions on the accuracy of the calculation of BPS entitlements.

41. The Commission’s guidelines did not specify the role of certification bodies where BPS entitlements calculations involved other bodies than paying agencies; as a result:

- in Germany (Niedersachsen), the accuracy of this calculation was not subject to any review by a certification body, because the calculation had been performed by a central coordination body not subject to a certification audit;
- in Italy, the certification body simply mentioned that, at the time it was drafting its report, the coordination body had not finished calculating BPS entitlements;
- in France, the certification body confirmed that the paying agency had correctly applied the calculation method established by the Ministry of Agriculture, but reported that data were not yet final and that they did not review certain calculations.

Some calculation rules and options chosen by Member States could add complexity, increase the burden on national administrations, and allow some farmers to realise windfall profits

Some rules for establishing BPS entitlements required complex calculations

42. One of the core objectives, and key requirements, of the 2013 CAP reform was to reduce the administrative burden and the Commission and Member States should have

taken this into account when shaping the relevant provisions for the direct support scheme³⁸.

43. The choice of the model for calculating BPS entitlements had a significant impact on the complexity facing national authorities. While the flat-rate model applied in Germany, France (Corsica), Malta and the United Kingdom (England) promised simple calculations of the values and numbers of entitlements, this was less true of the convergence models applied in other Member States or regions with their detailed and specific calculation rules which Member States often complemented by national or regional implementing provisions. This could not only give rise to calculation errors, but also imposed substantial additional work on paying agencies³⁹.

The options chosen by some Member States could impose a significant burden on national administrations...

44. Member States could, according to objective criteria, further differentiate their territory and apply the BPS at regional level. Such criteria included institutional structure (e.g. Germany), regional agricultural potential (e.g. the United Kingdom (England and Scotland)) or agronomic characteristics (e.g. Greece and Spain).

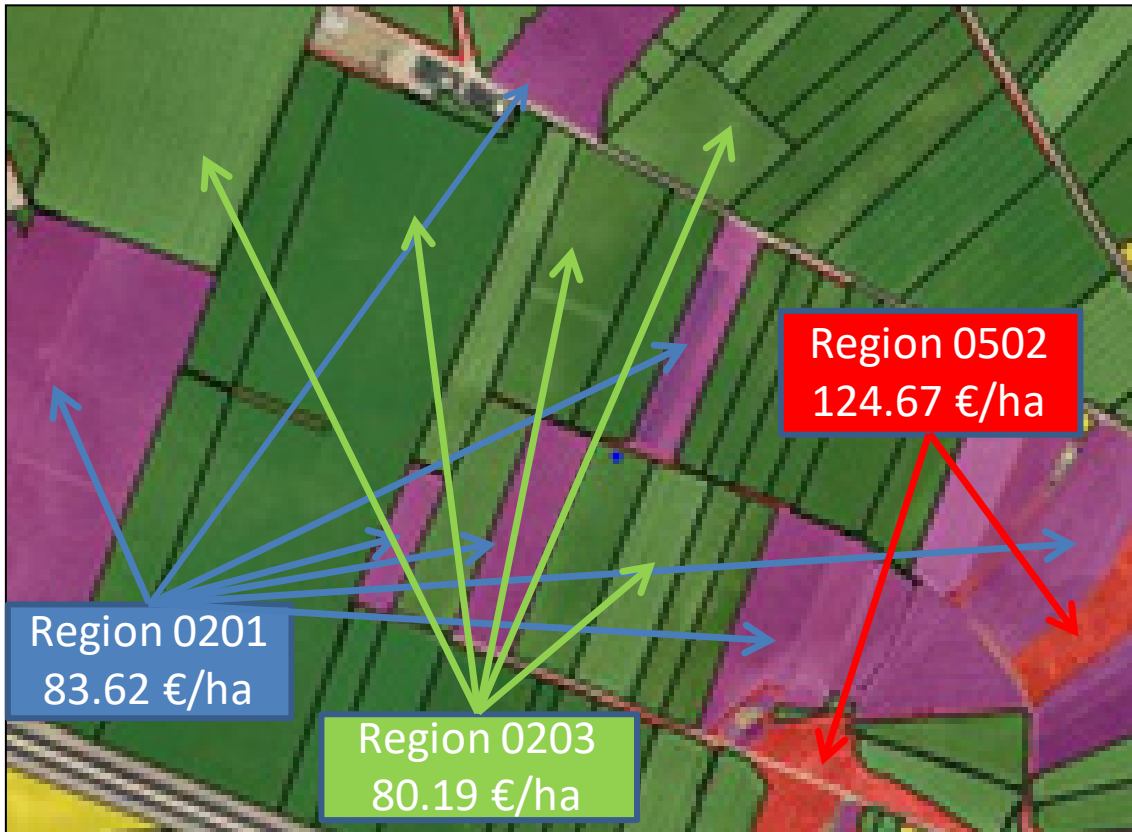
45. In this context, Spain introduced 50 new BPS regions which the national authorities defined on the basis of agronomic characteristics and their 2013 land use. These regions extended across some 316 'comarcas agrarias' meaning that land belonging to a single BPS region could be found in several comarcas and Autonomous Communities across mainland Spain. However, in many of the regions the average unit values of BPS entitlements varied only marginally. While this regionalisation complied with the EU legal framework, it added complexity to land management. Farmers could only use their entitlements in the region for

³⁸ Recital 2 of the Preamble to Regulation (EU) No 1307/2013.

³⁹ E.g., the authorities in France received ca. 360 000 claims for allocation of BPS payment entitlements, 46 000 of which involved modification of the reference amount and checks of supporting documents. In parallel, they had to treat some 12 million anomalies which they identified in the cross-checks with the LPIS. They had to recruit around 700 additional temporary staff to be able to process this unexpected workload.

which they had originally been allocated which could concern individual agricultural parcels in the same village (see **Figure 6**).

Figure 6 – Complex regional BPS implementation in Spain



Source: European Court of Auditors based on data from the Spanish authorities (FEGA).

In contrast to Spain, Greece used a much less complex model based on agricultural characteristics and covering only three regions.

46. Challenges to smooth implementation of the BPS were posed not only by the Member State's choice of BPS model but also by the options which EU legislation envisaged for defining eligible areas. This was expected to enhance the targeting of the support but could seriously delay the calculation of BPS entitlements and impact the accuracy of their value (see **Box 1**).

Box 1 – Member State choices that contributed to significant delays for implementation of the BPS

As a rule, all areas taken up by arable land, permanent grassland and permanent crops are eligible for BPS. In addition, in order to protect certain landscape features such as hedges, ponds, ditches, trees in line, in groups or in isolation, field margins or terraces, Member States could decide that they also were eligible for the allocation of BPS payment entitlements. However, under greening payment rules, Member States could define other landscape features as ‘ecological focus areas’ which were not eligible for the BPS. Where a Member State decided so, all features had to be checked and recorded in the national LPIS. France opted for a framework, whereby the French authorities in a major update of their LPIS had to register and supervise around 45 million such landscape features and establish whether they were eligible for BPS and greening, for greening only or were not eligible at all. Where farmers declared parcels that also contained ineligible features, they had to be checked manually and often farmers had to be contacted to clarify the issue, even though the amounts of support in question were marginal. This contributed significantly to the delays in the calculation of BPS entitlements and the payment of support in France.

In Italy, the minimum level of agricultural activity required for the eligibility of a significant share of permanent grassland⁴⁰ varied according to the location of parcels, and numerous exceptions applied at regional level. The Italian authorities had to identify all parcels to which the specific conditions applied by means of their land registry reference and then cross-check them against the farmers’ aid applications. This procedure was still ongoing by the end of our audit and the Italian authorities were unable to tell us when they would complete their work. This detailed approach added complexity and caused a significant delay in calculating payment entitlements and making support payments.

...and some farmers could generate windfall profits by significantly reducing the size of their holdings

47. For the Member States that applied a convergence approach for the BPS⁴¹, a specific risk arose of farmers being overcompensated by the introduction of the BPS, because they had significantly reduced the number of hectares farmed between the reference period

⁴⁰ Areas kept naturally in a state suitable for grazing or cultivation, areas which form part of established local practices for livestock grazing and poor pasture.

⁴¹ See *Figure 2*.

(2014) and 2015. This made it possible to concentrate the reference amount derived from a larger area on a smaller area, enabling these farmers to realise a windfall profit.

48. Member States could claw back the windfall profit⁴². Seven Member States, out of 13 where it was applicable, used this option⁴³, which also enabled them to reallocate these funds more effectively, for example by allocating BPS entitlements to young farmers. However, in Italy the authorities did not properly identify all farmers who had made windfall profits, or applied the rules in other cases incorrectly. In France, the authorities initially decided to apply the windfall profit clause, but were unable to do so in practice (see **Box 2**)⁴⁴.

Box 2 – Examples of windfall profits due to a reduction of holding sizes

The size of windfall profits could be significant. In Spain the authorities clawed back reference amounts of more than 75 million euro from more than 7 000 farmers which they could use for allocation to start-up farmers. This represents around 3 % of the BPS support paid in Spain.

As France did not apply the windfall profit clause, the total level of windfall profits which farmers realised is not known. However, we found individual farmers who had received direct payments in 2014 but who in 2015 transferred nearly all their land to other farmers, including family members. In extreme cases they kept just a small piece of land, sometimes only 0.01 ha on which they were allowed to accumulate their entire reference amount which resulted in BPS entitlement values of up to 9 000 euro and more. This was legally possible, because France, unlike other Member States, had not established a minimum area of land that farmers needed in order to claim for BPS entitlements⁴⁵.

⁴² Article 28 of Regulation (EU) No 1307/2013.

⁴³ See **Annex II**. This option was not applicable in five Member States (Denmark, Sweden and Finland decided to keep SPS entitlements, while Germany and Malta had a BPS flat rate in 2015).

⁴⁴ In both France and Italy, the authorities could not provide data about the total financial impact of the non-application of the windfall profit clause.

⁴⁵ See **Annex II**.

The individuals or companies receiving the land were able to receive entitlements from the national reserve as new farmers.

The new rules aimed at improving targeting of support, but were only partly effective

The new rules introduced requirements for specific checks on certain categories of aid applicants...

49. The 2013 CAP reform aimed at a better targeting of EU direct support to genuine farmers and introduced the so called ‘active farmer’ concept⁴⁶. This concept provided for mandatory additional eligibility requirements for two categories of aid applicants: persons who mainly farmed land which is naturally kept in a state suitable for grazing or cultivation⁴⁷ and persons with business activities identified by a negative list. The latter could be re-admitted, on condition that they could demonstrate that their agricultural activities were ‘not insignificant’.

50. The new rules allowed Member States to exempt applicants of up to 5 000 euro in annual direct payments from any checks or to establish their own alternative criteria, according to which applicants could be re-admitted and benefit from EU direct support. Eleven out of 18 Member States applied the maximum threshold of 5 000 euro in all or part of their territory⁴⁸. Also, Member States were entitled to generally refrain from paying support to persons whose agricultural activities formed only an insignificant part of their overall economic activities or whose principal business objects did not consist of agriculture.

51. As BPS is decoupled from agricultural production, it was not possible to require that farmers had to earn an income from farming to be eligible for support. Beneficiaries could in principle outsource all agricultural activities on their land to third parties without losing their

⁴⁶ Recital 10 of the Preamble to Regulation (EU) No 1307/2013. See also paragraphs 29-31 of Special Report No 5/2011.

⁴⁷ See **paragraph 61**.

⁴⁸ For more detail see **Annex III**.

status as ‘active farmers’. However, farmers should have decision-making power, benefits and financial risks in relation to the agricultural activity on the land claimed.

...and some Member States achieved good results...

52. We found that based on administrative data such as commercial or tax registers, Spain and Italy achieved good results in identifying applicants with no agricultural activities or only marginal ones⁴⁹. The Netherlands informed us that the national authorities excluded around 4 % of the applicants, because their principal business or company object was not targeted at agricultural activity and who could thus not be taken up in the official business register.

53. However, while in general they asked applicants to declare whether they had activities on the negative list, all the Member States we visited had difficulties in properly identifying the applicants for whom they had to check the status as ‘active farmers’, either because the application form was not sufficiently clear, or because in certain cases they did not sufficiently investigate into cases of possible circumvention.

...but implementation was only partly effective and represented a significant administrative burden...

54. Depending on national choices, the number of applicants subject to checks on the significance of their agricultural activities could vary significantly: in some cases most applicants in a Member State or region were under the applicable thresholds, and in most cases Member States had decided not to extend the negative list. Those applicants on the negative list and above the threshold could provide evidence that either i) their direct payments amounted to at least 5 % of their non-agricultural income in the most recent fiscal year, ii) their principal business object was agriculture or iii) their agricultural activities were not insignificant. For the latter option, Member States had again much leeway to define criteria. While some Member States used criteria such as the share of non-agricultural income in total income, Germany and the United Kingdom (with the exception of Scotland)

⁴⁹ The Spanish authorities considered their approach to be broadly effective, because in 2015 they received some 35 000 claims applications fewer than in 2014. They explained this decrease with an information campaign on the new rules for ‘active farmers’ and ‘agricultural activity’. However, for other Member States no such information is available.

also accepted applicants who declared they had activities on the negative list as ‘active farmers’, if their eligible number of hectares exceeded a size close to the national or regional average. This could result in situations where applicants with activities mentioned on the negative list were excluded if they had less land than this threshold, while applicants having more hectares than the threshold could be admitted irrespective of whether their activities were marginal or not.

55. Finally, in most Member States visited the authorities excluded only very few persons, because most persons falling into the scope of the negative list fulfilled one of the options to be re-admitted. For example, in Germany the authorities had initially made an in-depth check of around 1 000 applicants who had declared to have activities on the negative list. This caused a significant administrative burden but resulted in the exclusion of only 26 applicants from access to BPS.

...and could result in differing treatment of similar applicants

56. Lastly, the criteria which the Member States adopted could result in different treatment of applicants in comparable situations, because the national authorities interpreted EU legislation differently or did not extend the negative list to entities typically involved in land management with either insignificant agricultural activities or whose principal business object did not consist of an agricultural activity (see **Box 3**).

Box 3 – Examples of different treatment of comparable situations

In Germany, the authorities took the position that horse-riding clubs or riding schools only had to prove their status as ‘active farmers’ if they had permanent sports facilities such as a manège for horse training. In France, the authorities considered riding clubs and similar activities to fall within the category of sport and leisure, meaning that all identifiable applicants with such activities were checked for active farmer status. This resulted in around 700 applicants being excluded from direct payments.

Authorities in Italy decided to include public entities on the negative list, with certain exceptions. Therefore, municipalities and forest authorities were in principle excluded from the allocation of BPS entitlements. Germany and the United Kingdom (England) did not extend the negative list to such

entities. As a result, municipalities and forest authorities with a role in the maintenance of public land were in principle eligible for the allocation of BPS entitlements.

From 2018 Member States can decide to simplify the criteria or to discontinue the application of the ‘negative list’

57. As part of the revision of the financial rules applicable to the general budget of the EU the Commission proposed allowing Member States greater discretion in applying the definition of ‘active farmer’ so as to render the system considerably less burdensome either by reducing the number of criteria available to applicants for demonstrating ‘active farmer’ status, or by ceasing to apply the provisions⁵⁰. The latter proposal was justified by concerns that the difficulties and the administrative costs of implementing the active farmer clause outweighed the benefit of excluding a very limited number of non-active beneficiaries from the direct support schemes. In October 2017, Council and Parliament agreed that, as from 2018, Member States can decide whether they reduce the criteria by which applicants can demonstrate their ‘active farmer’ status, which leaves applicants less options for being re-admitted, or discontinue the application of the negative list⁵¹.

⁵⁰ Proposal for a Regulation of the European Parliament and of the Council on the financial rules applicable to the general budget of the Union and amending Regulation (EC) No 2012/2002, Regulations (EU) No 1296/2013, (EU) No 1301/2013, (EU) No 1303/2013, (EU) No 1304/2013, (EU) No 1305/2013, (EU) No 1306/2013, (EU) No 1307/2013, (EU) No 1308/2013, (EU) No 1309/2013, (EU) No 1316/2013, (EU) No 223/2014, (EU) No 283/2014, (EU) No 652/2014 of the European Parliament and of the Council and Decision No 541/2014/EU of the European Parliament and of the Council (Omnibus Proposal).

⁵¹ Regulation (EU) No 2017/2393 of the European Parliament and of the Council of 13 December 2017 amending Regulations (EU) No 1305/2013 on support of rural development by the European Agricultural Fund for Rural Development (EAFRD), (EU) No 1306/2013 on the financing management and monitoring of the common agricultural policy, (EU) No 1307/2013 establishing rules for direct payments to farmers under support schemes within the framework of the common agricultural policy, (EU) No 1308/2013 establishing a common organisation of the markets in agricultural products and (EU) No 652/2014 laying down provisions for the management of expenditure relating to the food chain, animal health and animal welfare, and relating to plant health and plant reproductive material, OJ L 350, 29.12.2017, p. 15. The change does not affect the rules for minimum activities on land naturally kept in a state suitable for grazing or cultivation.

The new rules extended the categories of land on which support is payable...

58. Farmers could only receive BPS entitlements and payment of BPS and other area related direct support if they had eligible agricultural land at their disposal. Member States could also extend eligibility to permanent grassland where grass and other herbaceous forage were not predominant. In practice this concerned areas of heathland or woodland in regions where the use of such land was part of established local practices⁵². Under the previous SPS, the eligibility of such land for support had not been sufficiently clear⁵³.

...and enabled Member States to take measures reducing the risk of speculative claims ...

59. We have found in the past that, under the SPS, investors could acquire high-value payment entitlements and declare them together with low-value land that required only minimal maintenance work or no work at all⁵⁴. This resulted in EU income support paid to persons not involved in agriculture. We found Member States which took measures under the BPS which partially remedied this situation or which intended to reduce the risk of speculative claims (see **Box 4**).

Box 4 – Effective mitigation of the side-effects of decoupling direct support

In the United Kingdom (Scotland), the authorities decided to apply the BPS regionalisation in order to improve the targeting of support to farmers in areas with higher agricultural potential or to those actively using their land. They decided to define specific regions which included the most marginal land ('rough grazing'). In Member States which opted for BPS regionalisation, such as the United Kingdom (Scotland), payment entitlements may be transferred or activated only within the same region. This makes it impossible to transfer higher-value BPS entitlements from other regions to this type of land. By 2019, all BPS entitlements within such regions will be adjusted to a very low value per hectare, which better reflects the low agricultural potential of the land. Farmers actively using

⁵² In October 2017 Council and Parliament agreed on additional changes to land eligibility rules, allowing Member States to further extend the definition of permanent grassland to land that does not contain grass or herbaceous forage.

⁵³ See paragraph 36 of Special Report No 5/2011.

⁵⁴ See paragraphs 66 to 68 of Special Report No 5/2011.

their land for production may benefit from a newly introduced specific support scheme for sheep which aims to reduce the risk of land abandonment and a decline in production. Although in 2015 individual investors still received significant amounts of support, the measures taken will gradually increase the targeting of support by 2019.

In Spain, large areas of permanent grassland were not used for many years. There was a risk that applicants would declare this land for the sole purpose of receiving BPS entitlements, even though they had not performed agricultural activities on it. The Spanish authorities decided to allocate BPS entitlements on the basis of the land claimed in May 2013 (i.e. before farmers could have become familiar with the 2013 CAP reform adopted in December 2013) if this area was smaller than in 2015. Moreover, they only accepted claims for this type of land if farmers provided evidence that they were actually using it for agricultural activities and, in doubtful cases, launched on-the-spot checks.

...but also created difficult implementation problems

60. Under EU legislation, land is in general only eligible if farmers use it for an agricultural activity⁵⁵. This helps to avoid land abandonment and prevent deterioration of habitats. We found that most Member States had defined a regular minimum annual activity such as grazing or, alternatively, mowing that was suitable for maintaining the agricultural potential of the land or preventing the deterioration of habitats. Member States could also stipulate the characteristics of an agricultural area which, if complied with, deem the land being used for an agricultural activity⁵⁶. It proved difficult for Member States who chose this option to define specific characteristics: France and the United Kingdom (England), for instance, defined broad characteristics such as ‘not covered by dense scrub’ (England) or ‘no predominance of unwanted weeds’ (France). This could leave farmers uncertain as to the eligibility of their land and result in the allocation of BPS entitlements for abandoned areas.

61. Moreover, areas in regions with particular climate conditions or poor soil quality may not require specific regular activities to maintain their agricultural potential. The new rules

⁵⁵ Article 32(2)(a) of Regulation (EU) No 1307/2013.

⁵⁶ Article 4(1) of Regulation (EU) No 639/2014.

stipulated that such areas ‘naturally kept in a state suitable for grazing or cultivation’ were only eligible if farmers carried out a certain minimum activity on them⁵⁷.

62. Member States were free to decide if they had ‘areas naturally kept in a state suitable for grazing or cultivation’. For example, France and Italy had defined areas in mountain regions above a certain altitude on which they required regular grazing or mowing as the minimum agricultural activity. However, the authorities in the United Kingdom (Scotland) considered that under EU legislation in force such minimum activity did not necessarily have to be an agricultural activity or be related to land management (see **Box 5**).

Box 5 – Minimum activities on land naturally kept in a state suitable for grazing or cultivation

The United Kingdom (Scotland) defined poor permanent grassland (‘rough grazing’) as ‘land naturally kept in a state suitable for grazing or cultivation’. These areas were only eligible if farmers used them for agricultural production or, alternatively, carried out an environmental assessment of the land in each calendar year. This comprised a map and description of the farm environment, surveys of breeding birds, mammals, butterflies and plant health; and monitoring of habitats. In 2015, such assessments were available for around 190 000 ha.

⁵⁷ Article 4(1)(iii) of Regulation (EU) No 1307/2013.

Picture 1 – Land naturally kept in a state suitable for grazing and subject to environmental assessment



Source: European Court of Auditors.

The assessment entailed substantial costs for beneficiaries but provided valuable environmental data. However, their relationship to the objective of income support for farmers was weak.

63. The new rules also allowed Member States to allocate BPS entitlements to agricultural areas where grass or other herbaceous forage was not predominant. These could be wooded pasturages or grazeable heathland, on condition that farmers traditionally used such land for animal grazing. Typically, grazing is the only activity able to maintain such land in good condition, distinguish it from non-agricultural land and avoid it being damaged or abandoned⁵⁸. However, making support conditional on the possession of animals would not be in line with the decoupled nature of the BPS. Thus Member States faced the difficulty of designing rules to ensure that the land is sufficiently maintained.

⁵⁸ Such areas are significant in the United Kingdom (Scotland), Spain, Italy and Greece but also in other Member States not covered by our audit.

The 2013 reform of the CAP was a move towards a more uniform distribution of support per hectare and it remains difficult to establish the efficiency of BPS support for farmers' incomes

The 2013 reform of the common agricultural policy was conceived as a move towards more uniform support per hectare...

64. Under the 2003 CAP reform, farmers received income support mostly on the basis of their level of direct support in the years 2000 to 2002. Although the 2003 CAP reform already allowed Member States to reduce these historical elements in the SPS entitlement values or approximate them to a uniform amount per hectare, only a few Member States decided to do so⁵⁹.

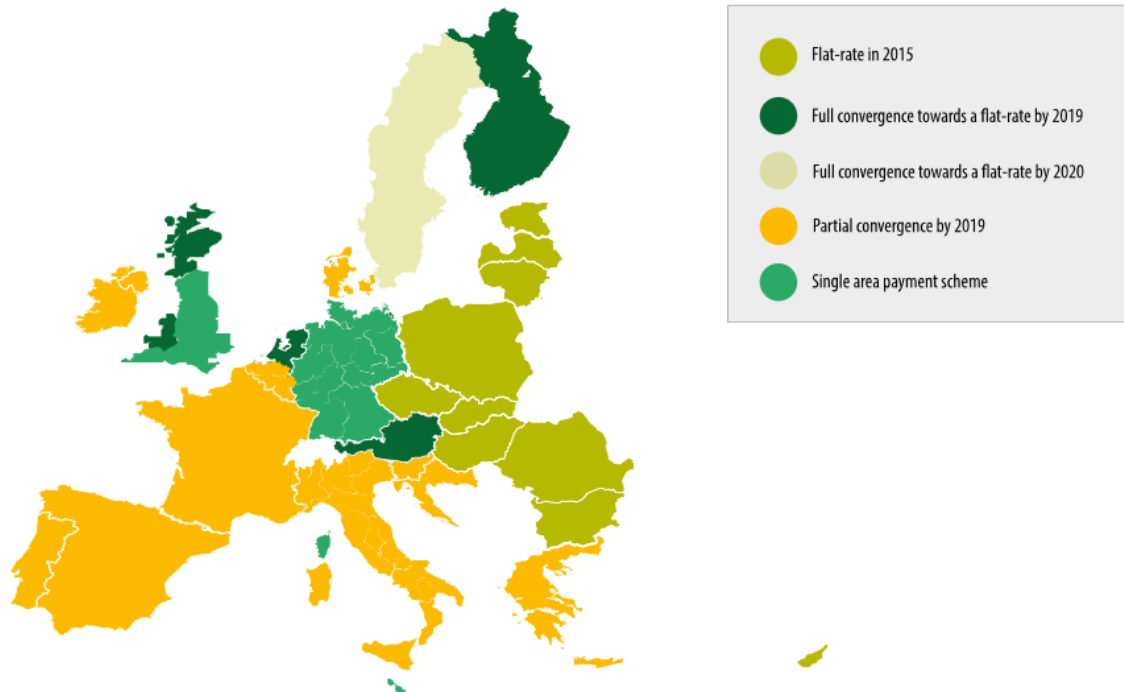
65. The 2013 reform of the CAP represented a move towards more equal support levels per hectare. Under the reform, 'as a general rule, all payment entitlements activated in 2019 in a Member State or in a region should have a uniform unit value'⁶⁰. As a derogation, in order to avoid disruptive financial consequences for farmers, Member States were allowed to take historical factors into account when calculating the value of payment entitlements which farmers should have in 2019. Six of the 18 Member States applying the scheme will pay a uniform value per hectare within their regions by 2019, and a seventh by 2020 (see ***Figure 7***)⁶¹.

⁵⁹ Paragraphs 46, 55 and 58 of Special Report No 5/2011.

⁶⁰ Recital 23 of the Preamble to Regulation (EU) No 1307/2013.

⁶¹ Germany, Malta, the Netherlands, Austria, Sweden (2020), Finland and the United Kingdom (with the exception of Northern Ireland).

Figure 7 – Member State implementation of the BPS



Source: European Court of Auditors.

...but the majority of Member States have chosen the option of partial convergence...

66. The transition to a flat-rate BPS model could lead to a significant redistribution of support across farmers and agricultural sectors and thus significantly affect the income situation of individual farmers.

67. Against this background, eleven Member States opted for a partial convergence model. This model ensures that by 2019 all BPS entitlements will have a unit value of at least 60 % of the national or regional average. France (mainland) chose a more ambitious model under which all farmers will be entitled to 70 % of the average national unit value per hectare by 2019, in order to facilitate a later adjustment towards uniform support per hectare. A majority of these eleven Member States decided to limit the reduction of the entitlement values of those farmers who were above the 2019 average to a maximum of 30 %, as allowed by EU legislation.

68. We found that not only the choice of the BPS model but also the criteria for the regional allocation of available budgetary ceilings could have a significant effect on the level of redistribution and farmers could retain particularly high support levels resulting from past production (see **Box 6**).

Box 6 – Effects of redistribution depending on the BPS model applied

The Spanish BPS model is based on regional agricultural potential and takes account of factors such as the type of land or crop in 2013. The design of the 50 regions resulted in 50 different 2019 target unit values ranging from around 60 euro to 1 430 euro. The amounts redistributed to farmers under convergence between 2015 and 2019 represents only 5.9 % of the Spanish BPS ceiling. Italy had not made this choice and decided to define only one region with a 2019 target value per hectare of around 217 euro. The redistribution of support from 2015 to 2019 between farmers and regions will represent 10.7 % of the total annual BPS ceiling⁶².

69. The establishment of the national ceilings on the basis of historical support levels and the variety of Member State choices for the allocation of the national ceiling for direct payments to the available schemes means that average levels of BPS support vary significantly (see **Table 1**).

⁶² Spain and Italy were largely comparable in the distribution of direct support prior to the 2013 CAP reform.

Table 1 – Average 2015 Values of BPS payment entitlements

Member State	Region	BPS-Regions	Average 2015 value of a BPS entitlement (euro) ¹⁾	Share of BPS in EU direct payments (%)
Belgium	Flanders	1	235	59
	Wallonia	1	122	32
Denmark		1	201	62
Germany		13 ²⁾	155 -192	60
Ireland		1	183	68
Greece		3	258 / 314 / 386	63
Spain		50	60 - 1 430	58
France		2	135 ³⁾ / 144	47
Croatia		1	79	61
Italy		1	229	60
Luxembourg		1	185	68
Malta		1	76	13
Netherlands		1	289	67
Austria		1	200	68
Portugal		1	99	49
Slovenia		1	165	54
Finland		2	110 / 126	51
Sweden		1	127	55
United Kingdom	England	3	45 / 170 / 172	68
	Northern Ireland	1	235	68
	Scotland	3	14 ³⁾ / 51 ³⁾ / 141 ³⁾	60
	Wales	1	121	58

¹⁾ in Member States not applying a flat rate per hectare individual values can significantly deviate from the values in the table

²⁾ 1 region by 2019

³⁾ provisional values

Source: European Court of Auditors.

Furthermore, for farmers in comparable situations, there is a risk that significantly different levels of support may negatively affect competition conditions and interfere with the commonality of the CAP.

...and it remains difficult to establish the efficiency of BPS support for farmers' incomes

70. The 2013 CAP reform ensures that by the year 2019 farmers will receive a minimum support per hectare. A standard amount of support per hectare, by definition, does not take account of the specific conditions of the farm such as the cost of farming, the income generated, the profitability of the farm or the need for EU income support. As the overall

amount of support paid to a holding is proportional to the number of hectares farmed, BPS tends to favour larger farms who can realise economies of size more than smaller farms⁶³. Some large-scale extensive farms or land managers with a historically low level of support could be affected by substantial increases in EU income support without this being associated with a change in the way they farm, in their costs or in the market (see **Box 7**).

Box 7 – Examples of redistribution as a result of the 2013 reform without changes in farming pattern⁶⁴

In Italy we found an extensive sheep and cattle breeder with around 270 ha of eligible land, mostly public poor grassland. Before 2015 the farmer had received around 5 000 euro in annual direct support. With the introduction of the BPS the farmer received BPS entitlements whose value increased to around 61 000 euro.

In the United Kingdom (Scotland), we found a farmer who owned several thousand hectares of poor permanent grassland. The farmer had never been involved in agricultural production but before the reform he had bought payment entitlements from other farmers and thus benefitted from around 27 000 euro in SPS support. With the introduction of the BPS, he received BPS entitlements of a total value of more than 34 000 euro. Due to convergence their value will go up to around 130 000 euro by the year 2019.

⁶³ At the level of the payments Member States may smoothen these effects by applying a reduction to amounts exceeding 150 000 euro per farmer or by granting a redistributive payment per hectare to all farmers for a number of hectares not exceeding 30 ha or the average size of the farm. The majority of Member States applies a reduction of 5 %.

⁶⁴ The actual level of support paid to these farmers has to be increased by the greening payment which in 2015 corresponded to 50.2 % of the BPS entitlement value in Italy. In the United Kingdom (Scotland), depending on the region where the parcels were located, in that year the greening payment amounted to between 83 and 4 euro per hectare and in Germany (Niedersachsen) to 87 euro. In Italy and Scotland farmers breeding cattle or sheep could under certain conditions benefit from coupled support which is paid per animal and farmers in Germany from a redistributive payment of 50 euro for the first 30 ha and another 30 euro for the area up to 46 ha.

In Germany (Niedersachsen) the authorities extended the eligibility of land to heathland. As a consequence, a sheep breeder with several hundred hectares of such land was allocated additional BPS entitlements of 65 000 euro.

71. We could not assess yet the full effects of the 2013 CAP reform on the income of farmers and the viability of their holdings. However, we observed already in previous reports that a system exclusively related to areas led to an increase in the market price of agricultural land and land leases as well as the appearance of new categories of aid applicants⁶⁵. The Commission expects that, due to the design of the BPS and other area related support payments, the 2013 CAP reform will be associated with a further increase of the capitalisation of decoupled support in land values⁶⁶. In other words, a major share of BPS support benefits the owners of agricultural land.

72. While BPS support is a significant source of income for many farmers, the scheme has inherent limitations. It is paid regardless of whether a farmer has a low or high income and may thus be in need of public support or not and regardless of the type of land use and the costs related to it. Too little is known about the non-farm incomes of farmers to evaluate whether the support given is appropriate⁶⁷. Only a few Member States decided to allocate BPS entitlements on the basis of the agronomic or socio-economic characteristics of the regions thereby differentiating the support between these regions accordingly⁶⁸ or to

⁶⁵ See paragraphs 27-31 and 53 of Special Report No 5/2011.

⁶⁶ See <https://ec.europa.eu/jrc/en/publication/impact-2013-cap-reform-decoupled-payments-capitalization-land-values>.

⁶⁷ We found in another audit that the quantity and quality of statistical data used to analyse farmers' incomes had significant limitations. See paragraphs 27, 47, 50 and 77 of Special Report No 1/2016 'Is the Commission's system for performance measurement in relation to farmers' incomes well designed and based on sound data?'

⁶⁸ Greece, Spain, France (Corsica) and the United Kingdom (with the exception of Northern Ireland). Austria used a specific option which allowed for the allocation of a lower number of BPS entitlements for mountain areas.

exclude areas from allocation where they considered that farmers were generally not in particular need of BPS support⁶⁹.

73. The objective of the Treaty to ensure a fair standard of living of farmers and the general CAP objective of viable food production that is directly linked to the BPS have not been clearly defined and translated into measurable targets and there is no baseline against which the effectiveness and efficiency of the support in enhancing farmers' incomes could be measured. It is also not known which distribution of support across the farming population is the most effective and efficient to ensure viable food production throughout the EU and a fair standard of living of farmers. Therefore, it remains difficult to assess the performance of BPS support in achieving its main objective and whether it could be achieved by other distributions of support entailing lower budgetary costs⁷⁰.

CONCLUSIONS AND RECOMMENDATIONS

74. Our main audit question in this report was whether Commission and Member States set the BPS properly on track. We conclude that the scheme is operationally on track, but that its impact on simplification, targeting and the convergence of aid levels is limited.

75. The introduction of the BPS required substantial efforts by the national authorities, because they had to establish and allocate BPS entitlements to some four million farmers. Overall, most Member States met these challenges. They largely mitigated risks of incorrect calculation, and support payments were not affected by a material level of error. However, in 2017, in several Member States, BPS entitlement values were still calculated only provisionally, based on estimates or affected by calculation errors, and some paying agencies we visited faced particular difficulties in key controls and identification of eligible areas (***paragraphs 26 to 33***).

⁶⁹ E.g. France for parcels planted with vineyards.

⁷⁰ See paragraph 81 of Special Report No 1/2016.

Recommendation 1

The Commission should ensure the appropriate implementation of key controls by Member States and that Member States correct BPS entitlements where values are significantly affected by the non-application of the relevant rules or the absence of up-to-date land use information.

Target implementation date: 2018

76. Overall, the Commission had well supervised the implementation of the BPS but this could not always ensure a consistent interpretation of the complex calculation rules. Also, some Member States had not duly submitted key information which made the Commission's monitoring of the scheme more difficult (**paragraphs 34 and 35**).

77. Overall, the Commission's own audits yielded good results, but it could have demanded more from the certification bodies in their checks of key controls on the allocation of BPS entitlements, and of the accuracy of the annual calculation of BPS entitlements (**paragraphs 36 to 41**).

Recommendation 2

The Commission should:

- (a) Review and take stock of the effectiveness of its systems for disseminating information among Member States, with a view to maximising their consistent interpretation and application of the BPS legal framework.
- (b) Assess options for future legislation that would enable it to enforce the transmission of key information by Member States on the implementation of direct support schemes
- (c) Clarify the respective roles of the Commission and of the certification bodies in checking the existence of effective key controls and the central calculation of BPS entitlements.

Target implementation date: 2018

78. Complex rules for the calculation of BPS payment entitlements and the range of options and exceptions chosen by some Member States for the eligibility of land and the design of

regions increased the burden on national administrations. This did not contribute to achieving the overall objective of simplification (**paragraphs 42 to 46**).

79. Where Member States did not use an option provided in EU legislation, farmers who had substantially reduced the areas farmed between 2014 and 2015 could realise windfall profits (**paragraphs 47 and 48**).

80. The new rules aimed at better targeting BPS support and other direct payments at active farmers. While some Member States achieved good results, the implementation of the 'active farmer' rules was only partly effective, caused a significant administrative burden and could result in differing treatment of similar applicants, without delivering the expected results. As a result, Council and Parliament agreed that – as from 2018 – Member States can decide whether they reduce the criteria by which applicants can demonstrate their 'active farmer' status or discontinue the application of the 'negative list' (**paragraphs 49 to 57**).

81. The 2013 reform of the CAP extended the categories of land on which support is payable and enabled Member States to take measures reducing the risk of speculative claims. In an attempt to better target support at agricultural land, however, it created difficult implementation problems (**paragraphs 58 to 63**).

82. The 2013 reform of the CAP represented a move towards more equal support levels per hectare. Under the reform, as a general rule, all payment entitlements activated in 2019 in a Member State or in a region should have a uniform unit value. As a derogation, Member States were allowed to take historical factors into account when calculating the value of payment entitlements which farmers should have in 2019, an option known as partial convergence. Six of the 18 Member States applying the scheme will pay a uniform value per hectare for the whole or a major part of their territory by 2019⁷¹, and a seventh by 2020. The remaining eleven Member States opted for partial convergence. Member State choices have had a significant impact on the degree of redistribution of support and farmers could in

⁷¹ France decided to introduce a flat-rate system only for the region Corsica which accounts for just 0.6 % of the French budgetary ceiling for the BPS.

some cases freeze particularly high support levels resulting from past levels of subsidy (**paragraphs 64 to 69**).

83. The allocation of BPS entitlements in 2015 was in general proportional to the areas farmed in that year. Convergence towards more uniform rates per hectare had a significant impact on the distribution of support among farmers. As a scheme essentially related to areas, the BPS tends to favour larger farms. Due to the design of the BPS and other area related support payments, the Commission expects that the 2013 CAP reform will be associated with a further increase of the capitalisation of decoupled support in land values, which benefits owners of agricultural land (**paragraphs 70 and 71**).

84. BPS support is a significant source of income for many farmers but has inherent limitations. It does not take account of market conditions, use of agricultural land or the individual circumstances of the holding, and is not based on an analysis of the overall income situation of farmers (**paragraph 72**).

85. The objective of the Treaty to ensure a fair standard of living of farmers and the general CAP objectives of viable food production and farmers' incomes have not been translated into measurable targets yet and there is no baseline to which the results achieved could be compared. In a future scenario of reduced budgets, this makes it difficult to measure the performance of the support and establish whether the objectives could be achieved by other distributions of support and at lower budgetary costs (**paragraph 73**).

Recommendation 3

Before making any proposal for the future design of the CAP, the Commission should assess the income position for all groups of farmers and analyse their income support need, taking into account the current distribution of EU and national support, the agricultural potential of land, differences of areas mainly dedicated to agricultural production or maintenance, cost and viability of farming, income from food and other agricultural production as well as from non-agricultural sources, the factors for efficiency and competitiveness of farms and the value of the public goods that farmers provide.

The Commission should link, from the outset, the proposed measures to appropriate operational objectives and baselines against which the performance of the support could be compared.

Target implementation date: 2019

This Special Report was adopted by Chamber I, headed by Mr Phil WYNN OWEN, Member of the Court of Auditors, in Luxembourg at its meeting of 7 February 2018.

For the Court of Auditors

Klaus-Heiner LEHNE

President

ANNEX I**Budgetary ceilings for the basic payment scheme 2015 - 2020⁷²**

(in million euro)

Member State	2015	2016	2017	2018	2019	2020
Belgium	231.51	225.60	222.20	214.40	211.28	225.12
Denmark	565.12	564.77	553.02	546.80	539.58	581.97
Germany	3 063.11	3 042.98	3 022.78	3 005.47	2 988.16	3 128.96
Ireland	828.31	828.43	826.18	825.89	825.61	825.61
Greece	1 205.70	1 182.88	1 129.25	1 103.65	1 091.17	1 156.27
Spain	2 809.79	2 816.11	2 826.61	2 835.99	2 845.37	2 845.37
France	3 577.32	3 199.09	3 185.17	2 280.46	2 272.64	2 528.64
Croatia	79.65	87.94	108.75	126.00	143.25	138.04
Italy	2 345.13	2 314.33	2 245.53	2 217.39	2 189.26	2 189.26
Luxembourg	22.86	22.82	22.78	22.76	22.74	22.74
Malta	0.65	0.65	0.65	0.64	0.65	0.26
Netherlands	521.77	513.03	504.28	475.19	466.96	509.89
Austria	471.28	470.85	470.39	470.38	470.38	470.38
Portugal	279.10	284.81	274.19	273.50	279.56	279.56
Slovenia	74.80	73.58	73.62	71.58	71.12	71.12
Finland	267.42	269.56	262.27	262.55	262.84	262.84
Sweden	383.29	401.64	401.86	402.46	403.06	403.06
United Kingdom	2 100.80	2 091.38	2 112.70	2 102.72	2 092.65	2 346.80

⁷² Member States may decide to modify their initial decision on the allocation of their national ceiling for direct payments (Annex II of Regulation (EU) No 1307/2013). In this case there will be an adjustment of the annual budgetary ceiling for the BPS as well.

ANNEX II**Models of implementation of the basic payment scheme**

Member State	Region	Application at regional level	BPS Model	Keep SPS payment entitlements	Number of beneficiaries	Minimum size of holding	Minimum level of 2019 average per hectare	Maximum decrease of PE values by 2019	Reference amount SPS	Integration of direct payments other than SPS	Areas for calculation of number of payment entitlements	Windfall profit clause
Belgium	Flanders	no	Partial convergence	no	22 275	2 ha	60%	30%	2014 SPS payment entitlement values	no	2015 or 2013 if less	no
	Wallonia	no		no	13 666	1 ha				no	2015	no
Denmark		no	Partial convergence	yes	40 696	2 ha	60%	no	NA	no	2015	NA
Germany		13 regions in 2015 1 region in 2019	Flat rate 2015	no	320 786	1 ha	NA	NA	NA	NA	2015	NA
Ireland		no	Partial convergence	no	121 355	-	60%	no	2014 SPS payment entitlement values	yes	2015 or 2013 if less	no
Greece		3 regions	Partial convergence	no	684 306	0.4 ha	60%	30%	2014 SPS payment entitlement values	no	2015 but no arable land under permanent greenhouses	yes
Spain		50 regions	Partial convergence	no	784 938	0.2 ha	60%	30%	2014 SPS Payments	yes	2015 or 2013 if less	yes
France	Continental		Partial convergence	no	358 534 ¹⁾	-	70%	30%	2014 SPS Payments	yes	2015 but no vineyards (2013)	no
	Corsica		Flat rate 2015	no	2 004	-	NA	NA	NA	no	2015 but no vineyards (2013)	NA
Croatia		no	Partial convergence	no	72 152	1 ha	60%	no	2014 SPS Payments	yes	2015	yes
Italy		no	Partial convergence	no	982 002 ¹⁾	0.5 ha	60%	30%	2014 SPS Payments	yes	2015	yes
Luxemburg		no	Partial convergence	no	1 830	0.3 ha	0	no	2014 SPS Payments	NA	2015	no
Malta		no	Flat rate 2015	no	5 178	0.3 ha	NA	NA	NA	NA	2015	NA
Netherlands		no	Full convergence by 2019	no	47 029	0.3 ha	NA	NA	2014 SPS payment entitlement values	no	2015 but no arable land under permanent greenhouses	no
Austria		no	Full convergence by 2019	no	108 054	1.5 ha	NA	NA	2014 SPS Payments	yes	2015	yes
Portugal		no	Partial convergence	no	158 831	0.5 ha	60%	30%	2014 SPS Payments	yes	2015 or 2013 if less	yes
Slovenia		no	Partial convergence	no	55 465	1 ha	60%	30%	2014 SPS Payments	yes	2015	no
Finland		2 regions	Full convergence by 2019	yes	52 024	-	60%	no	NA	no	2015	NA
Sweden		no	Full convergence by 2020	yes	60 543	4 ha	NA	NA	NA	no	2015	NA
United Kingdom	England	3 regions	Flat rate 2015	yes	87 303	5 ha	NA	NA	NA	NA	2015	NA
	Northern Ireland	no	Partial convergence	no	23 327	3 ha	71.4%	no	2014 SPS payment entitlement values	no	2015	no
	Scotland	3 regions	Full convergence by 2019	no	18 243	3 ha	NA	NA	2014 SPS payment entitlement values	no	2015	yes
	Wales	no	Full convergence by 2019	no	15 348	5 ha	NA	NA	2014 SPS payment entitlement values	no	2015	yes

1) Provisional data

ANNEX III**Implementation of the 'active farmer' concept**

Member State	Region	Threshold for exemption from the application of the active farmer provisions (euro)	Extension of negative list	Extension to all applicants with only insignificant agricultural activities ¹⁾	Area threshold as from which activities are considered significant (ha)	Land naturally kept suitable for grazing or cultivation
Belgium	Flanders	0	no	no		yes
	Wallonia	350	no	no		no
Denmark	-	5 000	no	no		no
Germany	-	5 000	yes	no	38	yes
Ireland	-	5 000	no	no	32	no
Greece	-	5 000	no	yes		no
Spain	-	1 250	no	no		no
France	-	200	no	no		yes
Croatia	-	5 000	no	no		no
Italy	-	1 250 ²⁾	yes	yes		yes
Luxembourg	-	100	no	no		no
Malta	-	250	yes	no		no
Netherlands	-	0	yes	yes		no
Austria	-	1 250	no	no		no
Portugal	-	5 000	no	no		no
Slovenia	-	5 000	no	no		no
Finland	-	5 000	no	no		no
Sweden	-	5 000	no	no	36	no
United Kingdom	England	5 000	no	no	36	no
	Northern Ireland	5 000	no	no	26	no
	Scotland	5 000	no	no		yes
	Wales	0	no	no	21	yes

¹⁾ Article 9(3) of Regulation (EU) No 1307/2013

²⁾ 5 000 euro in disadvantaged or mountain areas

REPLIES OF THE COMMISSION TO THE SPECIAL REPORT OF THE EUROPEAN COURT OF AUDITORS

"BASIC PAYMENT SCHEME FOR FARMERS – OPERATIONALLY ON TRACK, BUT LIMITED IMPACT ON SIMPLIFICATION, TARGETING AND THE CONVERGENCE OF AID LEVELS"

EXECUTIVE SUMMARY

III. EU legislation required Member States to allocate payment entitlements to eligible hectares determined in the year of first allocation of payment entitlements, i.e. hectares considered eligible after the finalisation of administrative and On-the-Spot Control (OTSC). Similarly, the value of payment entitlements was to be calculated only when the number of payment entitlements had been established.

Similar inaccuracies in the BPS payment entitlements values were found during the Commissions conformity audits. The conformity procedures are on-going. Any financial risk to the EU budget for BPS expenditure will be covered through financial corrections.

IV. The Commission provided clear and unambiguous guidance, available to all Member States on the web-based system of Communication and Information Resource Centre for Administrations, Businesses and Citizens ("CIRCABC")¹. It is the Member States' responsibility to consult the available guidelines. Some information was not transmitted timely by a few Member States.

There were audit missions to check the Certification Bodies' work on BPS entitlements. In terms of testing to be performed on entitlements, the Commission guidelines cannot be too prescriptive, as the Certification Bodies are qualified auditors and in accordance with internationally accepted audit standards, they should use their professional judgement in carrying out the certification work. In some Member States, the Certification Body recalculated the entitlements for all transactions subject to substantive testing (i.e. for the statistically selected sample).

V. The co-legislation process resulted in several options for the implementation of the Basic Payment Scheme. However, it also contained the possibility for Member States to limit their choices. It is the Commission's impression that the Member States that applied a restrictive approach to the options of the CAP experienced a lower administrative burden.

VI. The negative list was not part of the Commission proposal but was introduced as a result of the political compromise. While the initial proposal of the Commission was to have a single test on all claimants (direct payments at least 5% of the total non-agricultural receipts), the co-legislators granted a number of policy choices on the implementation of the active farmer provision allowing Member States to take into account their national specificities.

VII. Targeting often leads to increased complexity in implementation. Clearly, any change in legal requirements, including definitions of eligibility, has repercussions on the administration and control systems (IACS). The Commission provided extensive support during the implementation of the last reform, including for the exercise of first allocation of payment entitlements.

IX. Direct payments are, in their vast majority, granted per hectare of eligible area and are, therefore, strongly correlated to the agricultural area of the farm. However, BPS should not be judged as a stand-alone scheme. BPS ensures that farmers receive a minimum support per hectare. The BPS is topped up by other payments that favour a redistribution of support. In fact, Commission analysis shows that direct payments per hectare decrease with increasing farm size and that the unit support is higher for small farms which on average have a lower income per worker.

¹ CIRCABS is a web-based service provided by the European Commission to share documents with Member States.

Land values are largely influenced by numerous factors other than CAP support: e.g. agricultural commodity prices, urban pressure, national land market regulations, taxes, duration of rental contracts etc. Moreover, in BPS Member States where entitlements can easily be traded without land, the income support is less capitalized into land prices.

X. The purpose of BPS is to improve the overall income situation of farmers. BPS support is area-based, decoupled from production and in most Member States linked to historical references. It does not focus on individual circumstances in each holding in order to avoid excessive administrative burden. Further targeting of the support is done through other schemes such as the young farmer payment, the redistributive payment, the small farmers' scheme and the voluntary coupled support.

The upcoming Impact Assessment, which forms part of the proposal of the new delivery model of the CAP, will analyse the current distribution and targeting of income support by farm size and type of farming taking into account income generated by agricultural activities. In addition, other revenues generated by non-agricultural activities, based on agricultural factors (such as agri-tourism) will be taken into account when assessing the relevance of income support overall. In regard with that, as the impact assessment is still at the inception stage, it is not yet possible to determine whether or not it will encompass all the factors referred to in this observation.

XI. To ensure a fair standard of living of farmers is indeed a CAP objective set out in the Treaty. The Commission's Communication on "*The future of food and farming*" proposes a new delivery model of the CAP in which the Union should set the basic policy parameters while Member States should bear greater responsibility and be more accountable as to how they meet the objectives and achieve targets that should be presented and justified in a strategic CAP plan. The Commission acknowledges the importance of the CAP objective of viable food production and has tasked an evaluation on the impact of CAP measures on "viable food production".

XII. Some recommendations were accepted and others rejected. Namely, the recommendations concerning the allocation and calculation of BPS entitlements, and concerning the role of Certification Bodies have been accepted. Yet the recommendation concerning the Commission's systems for disseminating information among Member States has been rejected.

XIII. Concerning the proposals for the next programming period, the Commission partly accepts the recommendation. The Commission Communication "The Future of Food and Farming"² proposes a new Delivery Model for the CAP. The Communication aims at greater subsidiarity allowing taking into better account the local conditions and needs against the objectives and targets. The Impact Assessment that will underpin the Commission proposal for the post-2020 CAP will take into account all available evidence on the performance of the policy so far, among others an analysis of some proposed factors, and will use this information when analysing specific solutions for the future.

In order not to prejudge the outcomes of the above-mentioned impact assessment, the Commission cannot accept the recommendation to link from the outset the proposed measures to appropriate operational objectives and baselines against which the performance of the support could be compared at this stage. However, in line with the Commission's Communication on "the future of food and farming", the way to assess the performance of any types of intervention, including where appropriate, income support, will be considered.

INTRODUCTION

3. At the occasion of the 2013 reform, the Commission addressed the weaknesses detected by ECA and thus the mandatory "active farmer" clause was introduced. Under the previous system (governed by Regulation (EC) No 73/2009), Member States could already exclude on a voluntary basis persons from access to direct support. The exclusions could take place if the agricultural activities formed

² COM(2017) 713 final.

only an insignificant part of the overall economic activities of these persons or if the business purpose was not or only marginally targeted at performing an agricultural activity. Only the Netherlands opted for this possibility.

Also, the definition of eligible land has been improved in order to include specific requirements on areas naturally maintained. Moreover, Member States are allowed to draw up the list of areas which are predominantly used for non-agricultural activity. The definition of farmer and of agricultural activity reflects the decoupled nature of direct payments and the corresponding need not to impose productive activities as eligibility criteria in light of WTO green box rules.

Similar errors and weaknesses were found during the Commission's conformity audits concerning SPS. The financial risk to the EU budget stemming from these errors and weaknesses was covered through financial corrections that were applied until appropriate corrective measures were taken by the concerned Member States to ensure the legality and regularity of the SPS expenditure.

12. See Commission reply to paragraph 13.

13. For Member States applying the model of partial convergence, the value of payment entitlements is based on historical elements and therefore historic differences in the per hectare support level remain. However, these differences in support level will decrease gradually by claim year 2019 as a result of the internal convergence process.

OBSERVATIONS

29. The overshooting of the BPS ceiling was also found during the Commission's conformity audit carried out in Italy. The conformity procedure is on-going. Any financial risk to the EU budget for BPS expenditure will be covered through financial corrections.

a) No conformity audit on the management and control system related to the BPS Payment Entitlements in UK-Scotland has taken place yet. In case errors are found in relation to the allocated Payment Entitlements, the resulting financial risks to the EU budget will be covered through financial corrections until appropriate corrective measures will be taken to ensure the legality and regularity of the BPS expenditure.

Concerning the Netherlands, the Commission is aware of the ECA finding indicating incorrect application of the internal convergence rules. This issue will be taken into account in the risk analysis for the Commission's audit planning.

b) The fact that farmers did not know the definitive value of their BPS entitlements before applying for the next claim year was also found during the Commission's conformity audit carried out in France and UK-England. The conformity procedures are on-going. Any financial risk to the EU budget will be covered through financial corrections.

Concerning UK-Scotland – see Commission reply to paragraph 29 a).

i) Similar delays were detected during the Commission's conformity audit carried out in France.

Taking account of the deficiencies, an Implementing Decision of the Commission (C(2016) 4287) was adopted on 12/07/2016 suspending monthly payments to France from July 2016 to July 2017 included. The suspension was at the level of 3% of direct payments claimed for reimbursement.

The conformity procedure is on-going. Any financial risk to the EU budget will be covered through financial corrections until appropriate corrective measures will be taken by the Member State to ensure the legality and regularity of the BPS expenditure.

ii) Similar weaknesses in the management and control system related to BPS were found during the Commission's conformity audits carried out in UK-England. The conformity procedure is on-going. Any financial risk to the EU budget due to these weaknesses will be covered through financial

corrections to be applied until appropriate corrective measures are taken to ensure the legality and regularity of the BPS expenditure.

Concerning UK-Scotland – see Commission reply to paragraph 29 a).

31. Similar weaknesses in the management and control system related to BPS were found during the Commission's conformity audits carried out in Italy. The conformity procedures are on-going. Any financial risk to the EU budget due to these weaknesses will be covered through financial corrections to be applied until appropriate corrective measures are taken to ensure the legality and regularity of the BPS expenditure.

32. The conformity audits carried out by the Commission in Greece, France, Italy, and the United Kingdom led to similar observation. The conformity procedure is on-going. Any financial risk to the EU budget due to these errors and weaknesses will be covered through financial corrections to be applied until appropriate corrective measures are taken to ensure the legality and regularity of the BPS expenditure.

33. The reliability of the information in the animal register will be verified during a conformity audit planned for the first half of 2018, according to the Multiannual Audit Programme for the period 2017-2020. Any financial risk to the EU budget will be covered through financial corrections to be applied until appropriate corrective measures will be taken to ensure the legality and regularity of the BPS expenditure.

34. The guidelines issued by the Commission were clear, unambiguous and consistent. In addition, as a general rule, any interpretative document or reply of a general interest is made available to all Member States via the web-based service CIRCABC. Representatives of all Member States having access to CIRCABC can subscribe to a system of alert that ensures they receive a notification each time a new document becomes available on CIRCABC. It is the Member States' responsibility to consult CIRCABC regularly to ensure that they apply the EU legislation correctly.

36. Some audit missions were indeed not carried out as planned in calendar years 2016 and 2017. With the available staff resources priority was given to the necessary follow-up of the 13 desk-audits launched in 2016, which in addition to Voluntary Coupled Support also covered BPS related items like the active farmer clause, the allocation of Payment Entitlements from the national reserve, etc.

The Commission reviewed the work of the Certification Bodies on legality and regularity on the basis of a risk analysis and so did not give particular priority to the work on BPS entitlements as the Certification Bodies' work covers both CAP Funds and all measures. There were some missions planned, specifically to look at the Certification Body's work on the BPS entitlements. For the missions the scope of which was not entitlements, the Commission did not specifically review the Certification Body's work on entitlements, unless there were particular risks associated. In the context of the financial clearance, all issues relating to BPS entitlements were followed up.

37. According to its Audit Strategy, the Commission conformity audit work is system based and risk based, i.e. it is focused on the verification of the key controls with the highest associated financial risk in case of non-compliance with the EU rules, for example, through the review of samples of transactions. Given the timing of such conformity audits, key controls with the highest associated financial risk were considered to be those linked to the first allocation of BPS Payment Entitlements as well as the allocation of new BPS Payment Entitlements from the national reserve, which is an important aspect of the management of the national reserve. The review of samples of transactions also allowed for the verification of important general calculation elements (i.e. different coefficients applied and annual averages calculated etc.).

Most of the conformity audits concerning the BPS Payment Entitlements were carried out in 2016. At that time (when the first allocation of the payment entitlements was just finalised or even not yet finalised and considering the important BPS implementation delays in certain Member States), the

procedures for the cancellation of unduly allocated Payment Entitlements was not assessed as posing a high financial risk.

39. The testing on entitlements to be performed by the Certification Bodies is twofold and it is laid down in the guidelines provided to Certification Bodies:

- firstly, on the procedures put in place by the Member State to ensure the correct allocation of entitlements and correct calculation of entitlements' value (cf. section 5.2 of Guideline 2). The main procedural aspects to be checked are detailed in section 7.2.2 of Guideline 3 since the allocation of entitlements should be tackled from a procedural (systems) perspective. This should be followed by compliance testing of particular transactions. Guideline 3 suggests 10 transactions. For the compliance testing, Guideline 2 clearly suggests using the list of Key and ancillary controls as a benchmark (cf. p.21 of Guideline 2 for FY2016);

- secondly, during the substantive testing of files for direct payments, a check on the arithmetical accuracy as well as a check on whether the final number of entitlements were taken for the payment should be performed by the Certification Body.

40. The Commission guidelines cannot be too prescriptive, as the Certification Bodies are qualified auditors and in accordance with internationally accepted audit standards, they should use their professional judgement in carrying out the certification work. In some Member States, the Certification Body recalculated the entitlements for all transactions subject to substantive testing (i.e. for the statistically selected sample).

41. The Commission's guidelines are general and cannot cater for all situations in the Member States. Nonetheless, the guidelines are clear as to the work to be performed by the Certification Bodies on entitlements as mentioned in the Commission's reply to paragraph 39. Moreover, section 7.2.2 of Guideline 3 specifies that FY2016 (CY2015) is the first year of the establishment of the payment entitlements, thus, the Certification Bodies' conclusion on the process of entitlements allocation was requested.

Moreover, several Member States were late with establishing the final entitlements. As the Certification Bodies have strict reporting deadlines (i.e. 15 February following the financial year in question), they could not always conclude on the accuracy of the entitlements' calculation.

First bullet: In most Member States with regional Paying Agencies and entitlements calculated at national level, it is possible to subject the entitlements calculations to the certification audit. In the case of Germany, the central body that calculated the payment entitlements was not subject to certification audit. Thus, the case of Germany (Niedersachsen) was not indicative of the Certification Bodies' work performed in other Member States.

Second bullet: The issue on entitlements for Italy is followed up through an ongoing conformity audit.

Third bullet: The issue on entitlements for France is followed up in an ongoing conformity audit.

42. The initial Commission proposal aimed at the simplification of the direct payments scheme. In fact, the original Commission proposal contained fewer options and was therefore more straightforward. However during the co-legislation process other options were added, which made the rules more complex. Furthermore, simplification is one of the main objectives in the discussions on the new common agricultural policy for post-2020.

43. While it is correct that the model of internal convergence for establishing the payment entitlement values is more complex, it is to be noted that applying this model as an alternative to the simple model of a flat-rate from the first year of implementation was an option for Member States. The choice by Member States of a specific implementation model is in line with the principle of shared management of the CAP according to which the implementation is managed directly by each Member State and

national authorities are responsible for the administration and control of direct payments to farmers in their country.

45. The Spanish authorities decided on the BPS regionalisation model based on a multitude of criteria in close cooperation with regional authorities. The implementation of the current BPS regionalisation will be assessed and taken into account for the reflection on the future CAP.

46. Extending the definition of eligible area was not obligatory for Member States. When using this possibility, it is the Member States' responsibility to assess the complexity of the system they decide to implement together with the actual need to account for specific agricultural methods in their territory.

48. The legislation provided for the possibility to limit increase of the value of payment entitlements in case such increase would lead to a windfall profit. Whether or not to apply this optional provision falls under the Member States' responsibility.

In addition, where windfall profits arise because of conditions created artificially and contrary to the objectives of the CAP, the (compulsory) circumvention clause set out in Article 60 of Regulation (EU) No 1306/2013 applies. As a result of the application of Article 60, no advantage shall be granted in favour of such natural or legal persons.

Finally, those farms obtaining high value payment entitlements by concentrating support on a smaller area made those payment entitlements subject to a higher reduction due to the internal convergence.

ECA counter-reply

The circumvention clause set out in Article 60 of Regulation (EU) No 1306/2013 and internal convergence only have a limited impact as mechanisms to reduce windfall profit.

*As repeatedly held by the Court of Justice, the application of the circumvention clause by Member States requires, first, a combination of objective circumstances in which, despite formal observance of the conditions laid down by the European Union rules, the purpose of those rules has not been achieved, and, second, a subjective element consisting in the intention to obtain an advantage by creating artificially the conditions laid down for obtaining it. In the case of windfall profits resulting from the transfer of land to other farmers (see **Box 2**), it is extremely difficult for Member States to prove that the applicant, when transferring the land, intended exclusively to obtain an advantage contrary to the objectives of BPS.*

*By 2019 internal convergence will reduce the value of BPS entitlements referred to in **Box 2** by around 25 %, which means that farmers will still benefit from 75 % of the windfall profit in that year.*

53. Similar deficiencies concerning the verification of the active farmer status of the applicants were identified during the Commission's conformity audits. The conformity procedures are on-going. Any financial risk to the EU budget will be covered through financial corrections until appropriate corrective measures will be taken by the Member State to ensure the legality and regularity of the direct payments expenditure.

54. The co-legislators granted a number of policy choices for the implementation of the active farmer provision allowing Member States to take into account their national specificities.

The Commission has provided a favourable assessment of the use of a threshold expressed in eligible hectares as an alternative criterion for the purpose of Article 9(2)(b) of Regulation (EU) 1307/2013 to prove the agricultural activity is not insignificant if this condition does not entail any incentive for farmers to produce.

55. The negative list was not part of the Commission proposal but was introduced as a result of the political compromise. While the initial proposal of the Commission was to have a single test on all claimants (DP at least 5% of the total non-agricultural receipts), the co-legislators granted a number of policy choices on the implementation of the active farmer provision allowing Member States to take into account their national specificities. Due to the existence of the negative list, it is quite probable that some entities have decided not to apply at all and this data is not available to the Commission.

Box 3 – Examples of different treatment of comparable situations

The Commission has published a Guidance document on the implementation of Article 9 of Regulation (EU) 1307/2013 (DSCG/2014/29). It is for Member States to further implement that provision in compliance with the purpose of the active farmer rule and the general principles of EU law.

As far as permanent sport and recreational grounds are concerned, the negative list aims at targeting specialised operators of permanently existing areas of land with permanent fixtures and/or permanent artificial structures for spectators that are being used for a purpose of sport and recreational activities. Germany has followed this guidance. There is an ongoing conformity clearance procedure for France.

The co-legislator provided for flexibility allowing Member States to calibrate the negative list to their specific circumstances and needs. In fact, the second subparagraph of Article 9(2) of Regulation (EU) No 1307/2013 allows Member States to add to the negative list any other similar non-agricultural businesses or activities, on the basis of objective and non-discriminatory criteria. Nevertheless, any additions to the list need to be objectively justified on the basis of the "similarity" test in Article 9(2), i.e. the businesses/activities of such entities should be similar in nature to those of entities already included in the negative list.

Likewise, the co-legislator decided to allow for optional implementation of Article 9(3) of the same Regulation.

57. As a result of the negotiation process on the so-called Omnibus Regulation³, the application of Article 9(2) of Regulation (EU) No 1307/2013 (the negative list) can be discontinued as from 2018 or any subsequent year. In contrast, Article 9(1) still continues to apply for all Member States that have areas naturally kept.

60. Defining eligibility on the basis of the characteristics of agricultural land does not exonerate farmers from exercising an agricultural activity. The characteristics should result from this activity. Where Member States define these characteristics correctly, abandoned areas would appear as such and would therefore be considered ineligible.

62. The Commission considers that for naturally-maintained areas, the minimum activity should not be completely detached from any land management, unless this is the result of Natura 2000 implementation (which also implies that the areas had a right to receive payments in 2008)⁴.

Box 5 – Minimum activities on land naturally kept in a state suitable for grazing or cultivation

The Scottish authorities did not notify to the Commission their decision to carry out an environmental assessment of the land in each calendar year instead of an agricultural activity.

It is questionable whether an environmental assessment may be considered a minimum activity on the agricultural area.

³ Regulation (EU) 2017/2393 (O.J. L350 of 29.12.2017).

⁴ Article 32(2)(b)(i) of Regulation (EU) No 1307/2013.

It is expected that the activity has an impact on the land itself (e.g. to maintain or even enhance the natural value of that grassland) and is not limited to an observation of the environmental state of the area, whose evolution is not the consequence of any action exercised by the farmer.

Box 6 – Effects of redistribution depending on the BPS model applied

The Spanish authorities decided on the BPS regionalisation model based on a multitude of criteria in close cooperation with regional authorities. The implementation of the current BPS regionalisation will be assessed and taken into account for the reflection on the future CAP.

Although the amount transferred from high value payment entitlements to low value payment entitlements expressed as a percentage of the BPS ceiling illustrates a better convergence in Italy as compared to Spain, the comparison of the aforementioned percentage does not allow to draw conclusions on the different effects of convergence between all Member States. In fact, a Member State for which this percentage is higher than for another one does not necessarily end up with a better situation at the end of the period. It is important to take also the starting situation into account, in particular the possibility of further convergence. Although the transfers of funds as a percentage of the BPS ceiling will be lower in a Member State with Payment Entitlements values close to the average already in the beginning of the convergence period, this Member State might end up with more convergent values than a Member State with a much higher percentage of transferred funds.

69. The difference in average level of BPS support is partly explained by the fact that Member States made different choices as regards the allocation of funds to the different direct payments schemes. The BPS envelope equals the amount of funds that is left after the allocation to those other schemes.

BPS is a decoupled payment by definition having a minimal effect on the production decisions of farmers and consequently on the market and competition conditions. The evaluation made by ECA relies on the theoretical assumption that farmers in different Member States are in an identical situation. Such a comparable situation would mean not only equality of production conditions but also that land prices, rents, and other factors of production are identical between two Member States.

70. The Basic Payment Scheme makes sure that all farmers receive a minimum support per hectare. Other schemes, such as the redistributive payment, the payment for young farmers, the small farmer scheme and voluntary coupled support allow for targeting of direct payments. BPS is an area based system and as a result, the total support tends to increase by farm size. However, Commission analysis shows that direct payments per hectare decrease with increasing farm size and that the unit support is higher for small farms, which on average have a lower income per worker, mainly due to the use of other direct payment schemes.

Box 7 – Examples of redistribution as a result of the 2013 reform without changes in farming pattern

ECA gives examples of farms where the support received by the farmer is increased exponentially although there is no change in the way they farm.

The Commission considers that the absolute amount of support cannot be looked at as a stand-alone figure but that it should be evaluated together with the size of the area and the support received by other farmers in comparable situations before and after the convergence exercise. Indeed, as we are in a context of convergence, a significant increase of support for a given farmer can most probably be explained by the fact that the support received by the farmer before the introduction of the BPS was considerably below the average and/or by increased area coverage of the BPS as compared to SPS. Both the increase of low value payment entitlements and larger area coverage were clear objectives of the scheme.

When looking closer at the examples highlighted by ECA the situations are not so extreme as they might seem at first sight.

For example in UK-Scotland where the support converges to a regional flat rate in 2019, the maximum support per area in claim year 2019 is fixed at EUR 161/ha for region 1 (arable land and permanent grassland), EUR 26.9/ha for region 2 (Rough grazing in non-Less Favoured Areas and in Less Favoured Area (LFA) with grazing categories B, C and D) and EUR 8.7/ha for region 3 (Rough grazing in Less Favoured Area (LFA) with grazing category A). The Commission considers that these levels of per area payment are not set at an inappropriate level.

In the example provided for IT, the average payment per hectare of the farmer in question amounts to about EUR 225, which is slightly below the average BPS Payment Entitlement value in IT for CY2015 (EUR 228/ha).

As regards DE, it is to be clarified that this Member State will evolve to a situation of a national flat rate by 2019.

71. Direct payments can be more or less capitalized into land prices according to different factors. The drivers of land values are numerous and CAP support is only one of them: agricultural commodity prices and agricultural productivity, urban pressure, different national land market regulations, duration of rental contracts, different levels of land taxes... According to Swinnen et al., *"CAP subsidies have an impact on land values but the impact varies importantly across countries and appears relatively modest compared to other factors, in particular where land prices are high"*.⁵ Moreover, in BPS Member States where entitlements can easily be traded without land, the income support is less capitalized into land prices.

72. BPS allows Member States to target support by excluding farmers that are not in a particular need for income support or by differentiating the basic payment. Further targeting of support is mainly achieved through other schemes: Redistributive payment, payment for young farmers, small farmers scheme or voluntary coupled support. Whereas some Member States show a significant degree of targeting, in other Member States targeting has been done to a smaller extent.

Moreover, the Treaty makes a link between an increase in agricultural productivity as a means to ensuring a fair standard of living for the agricultural community, in particular by increasing the individual earnings of persons engaged in agriculture. It is thus appropriate to focus on the income derived from agricultural activities, as this income is of primary importance for the CAP⁶. Finally, the costs of collecting data on farm household income may outweigh the benefits⁷.

73. The Commission Communication "The Future of Food and Farming"⁸ proposes a new Delivery Model for the CAP.

The Communication aims at greater subsidiarity allowing taking into better account the local conditions and needs against the objectives and targets. Moreover, the Commission acknowledges the importance of the CAP objective of viable food production and has tasked an evaluation on the impact of CAP measures on "viable food production".

The Impact Assessment that will underpin the Commission proposal for the post-2020 CAP will take into account all available evidence on the performance of the policy so far and will use this information when analysing specific solutions for the future.

⁵ Swinnen J. Ciaian P, Kancs d'A. (2008). Study on the functioning of land markets in the EU Member States under the influence of measures applied under the Common Agricultural Policy. Final report. Centre for European Policy Studies (CEPS).

⁶ See Commission replies (executive summary paragraph V) to the Special Report No 1/2016 of the European Court of Auditors: "Is the commission's system for performance measurement in relation to farmers' incomes well designed and based on sound data?".

⁷ See Commission replies (executive summary paragraph VI.b) to the Special Report No 1/2016 of the European Court of Auditors: "Is the commission's system for performance measurement in relation to farmers' incomes well designed and based on sound data?".

⁸ COM(2017) 713 final.

CONCLUSIONS AND RECOMMENDATIONS

74. The initial Commission proposal aimed at the simplification of the direct payments scheme. In fact, the original Commission proposal contained fewer options and was therefore more straightforward. However during the co-legislation process other options were added, which made the rules more complex.

Concerning the targeting, BPS allows Member States to target support by excluding farmers that are not in a particular need for income support or by differentiating the basic payment. Further targeting of support is mainly achieved through other schemes: Redistributive payment, payment for young farmers, small farmers scheme or voluntary coupled support. Whereas some Member States show a significant degree of targeting, in other Member States targeting has been done to smaller extent.

As regards convergence, according to Regulation EU (No) 1307/2013, Member States had three options in the application of the internal convergence (flat-rate as from 2015, full convergence by 2019 and partial convergence "tunnel mode"). Consequently, the impact and the effects of the implementation may vary from one Member State to another. Also, the application of the regionalisation played a significant role in the actual level of the convergence achieved.

75. Except for the Netherlands and UK-Scotland, the conformity audits carried out by the Commission lead to similar observation. The conformity procedures are on-going. Any financial risk to the EU budget due to errors and weaknesses in the functioning of the BPS related management and control systems will be covered through financial corrections to be applied until appropriate corrective measures are taken to ensure the legality and regularity of the BPS expenditure.

Recommendation 1

The Commission accepts this recommendation and considers it is already implementing this through the guidelines issued, monitoring done and the conformity audit procedures. When errors and weaknesses are found in the functioning of key controls, the Commission is requesting the Member States to take corrective actions and monitors their implementation by the Member States.

In addition, the Commission provides guidelines and advice to the Member States on the correct implementation of these key controls.

76. Direct Payments, as the entire EAGF expenditure, are implemented under the shared management principle between the Commission and Member States. In order to ensure the correct application of the BPS scheme, it is the Member States' responsibility to duly notify information and documents to the Commission in order to meet the obligations laid down in Regulation (EU) No 1307/2013.

The Commission provided clear and consistent guidelines and interpretation, which are available when of general interest on CIRCABC to all Member States.

77. The Commission considers that it did set out what was required from the Certification Bodies. The audit work expected from the Certification Bodies for FY2016 (CY2015) is clearly set in Guidelines 2 and 3.

Recommendation 2

(a) The Commission rejects this recommendation as, in accordance with the principle of shared management, it is the responsibility of Member States to apply the consistent interpretation of the BPS legal framework. Any interpretation and relevant information is shared with Member States in the Direct Payments Committee and relevant documents are uploaded on CIRCABC which is also available to Member States. Accordingly, the Commission considers it has made appropriate steps of disseminating information and ensuring the effectiveness of consistent interpretations among Member States and thus deems further maximising would be out of its reach.

(b) The Commission accepts this recommendation. The Commission acknowledges the importance of transmission of key information on the implementation of direct support schemes. However, the

Commission is at this stage not in a position to make specific commitments in relation to legislative proposals for the post 2020 period. Furthermore, already under the current legislation, the Commission can take various formal legal actions. Some existing provisions allow the Commission to suspend payments, to consider subsequent declarations of expenditure inadmissible and to initiate a conformity clearance procedure. In case of systemic and major non-compliance issues, the Commission can also initiate an infringement procedure, prepared, if useful, by launching an EU Pilot file, with the possibility of a sanction (lump-sum or penalty payment) to be imposed by the CJEU in case of non-execution of a first ruling. The decision on the appropriate action depends on a case-by-case assessment and the applicable legal framework.

(c) The Commission accepts this recommendation. In relation to the respective roles of the Commission and Certification Bodies, the Commission considers it implemented. as the requirements for the Certification Bodies' audit work on entitlements (review of the process of the first entitlements allocation and review of the entitlements' value calculations in the first year of allocations; and review of any new entitlements allocations, entitlements' cancellations, convergence, etc. in subsequent years) are clearly laid down in Guidelines 2 and 3 for FY2016 and onwards. In accordance with internationally accepted audit standards, there should be room for professional judgement by Certification Bodies. The main framework is provided in the guidelines (i.e. that the procedures need to be tested together with the controls embedded in the process whilst using the list of key and ancillary controls, etc.) and the Certification Body then designs and performs its own audit tests on entitlements.

The Commission takes this opportunity to clarify that where a Member State's institutional set up does not make it possible for the Certification Bodies to audit the procedures of allocation and calculation of entitlements, the work of Member State bodies (Paying Agencies, Certification Bodies or another body responsible for the entitlements' calculations) is subject to conformity audits to assess whether the applicable legal framework and the relevant guidelines are applied.

78. The initial Commission proposal aimed at the simplification of the direct payments scheme. In fact, the original Commission proposal contained fewer options and was therefore more straightforward. However during the co-legislation process other options were added, which made the rules more complex.

79. Where windfall profit arises because farmers have artificially created conditions to obtain very high payment entitlement values, Member States should apply the circumvention clause meaning that no advantage should be granted to the concerned farmers.

In addition, those farmers obtaining high value payment entitlements by concentrating the reference amount on a smaller area will be subject to a higher reduction of the value of their payment entitlements as a result of the internal convergence exercise.

ECA counter-reply

The circumvention clause set out in Article 60 of Regulation (EU) No 1306/2013 and internal convergence only have a limited impact as mechanisms to reduce windfall profit.

*As repeatedly held by the Court of Justice, the application of the circumvention clause by Member States requires, first, a combination of objective circumstances in which, despite formal observance of the conditions laid down by the European Union rules, the purpose of those rules has not been achieved, and, second, a subjective element consisting in the intention to obtain an advantage by creating artificially the conditions laid down for obtaining it. In the case of windfall profits resulting from the transfer of land to other farmers (see **Box 2**), it is extremely difficult for Member States to*

prove that the applicant, when transferring the land, intended exclusively to obtain an advantage contrary to the objectives of BPS.

*By 2019 internal convergence will reduce the value of BPS entitlements referred to in **Box 2** by around 25 %, which means that farmers will still benefit from 75 % of the windfall profit in that year.*

80. The degree of flexibility provided to Member States in e.g. extending the list of negative activities and/or applying the active farmer provision to all applicants, allows them to adjust the provision to their specificities but inevitably results in a differentiated implementation.

Furthermore, the first year of application of the active farmer clause required a one-off setting up of procedures to verify compliance with this clause. Although annual checks will still be required for Member States that continue implementing the negative list, one can reasonably expect that in subsequent years the administrative burden will level off.

82. If some very high levels of income support remain in 2019, they have however been subject to reductions compared to the 2015 level.

83. The Basic Payment Scheme makes sure that farmers receive a minimum support per hectare. Other schemes, such as the redistributive payment, the payment for young farmers, the small farmer scheme and voluntary coupled support allow for targeting of direct payments. BPS is an area based system and as a result, the total support tends to increase by farm size. However, Commission analysis shows that direct payments per hectare decrease with increasing farm size and that the unit support is higher for small farms, which on average have a lower income per worker, mainly due to the use of other direct payment schemes.

A significant increase of support for a given farmer can most probably be explained by the fact that the support received by the farmer before the introduction of the BPS was considerably below the average and/or by increased area coverage of the BPS as compared to SPS. Both the increase of low value payment entitlements and larger area coverage were clear objectives of the scheme.

84. The purpose of BPS is to improve the overall income situation of farmers. BPS support is area-based, decoupled from production and in most Member States linked to historical references. It does not focus on individual circumstances in each holding in order to avoid excessive administrative burden.

The decoupled nature of BPS ensures a market orientation and avoids creating an incentive for farmers to produce.

Recommendation 3

The Commission partially accepts this recommendation.

The Commission's Communication on "*The future of food and farming*" of 29 November 2017 proposes a new delivery model of the CAP in which the Union should set the basic policy parameters (objectives of the CAP, broad types of intervention, basic requirements), while Member States should bear greater responsibility and be more accountable as to how they meet the objectives and achieve targets that should be presented and justified in a strategic CAP plan.

The Impact Assessment that will underpin the Commission proposal for the post-2020 CAP will take into account all available evidence on the performance of the policy so far and will use this information when analysing specific solutions for the future.

In particular, the Commission will analyse the current distribution and targeting of income support by farm size and type of farming taking into account income generated by agricultural activities.

The Commission recalls⁹ that CAP supports farmers' income by supporting the agricultural activity (area-based support, a few sector-specific supports, investments, market measures, environmental activities on agricultural areas). Therefore, with regard to BPS, it is consistent to focus on the income generated from these agricultural activities.

In addition, the Commission's Communication envisages targeting "genuine farmers", understood as those who are actively farming in order to earn their living.

The duality of objectives of direct payments reflects the recognition of "jointness" in the delivery of market products and public goods, and thus the difficulties to carry out a proper economic valuation of all the public goods provided by farmers. However, other revenues generated by non-agricultural activities, based on agricultural factors (such as agri-tourism) will be taken into account when assessing the relevance of income support overall.

The impact assessment being still at the inception stage, it is not yet possible to determine whether or not it will take into consideration all the factors referred to in the recommendation.

Finally, in order not to prejudge the outcomes of the above-mentioned impact assessment, the Commission cannot accept the recommendation to link from the outset the proposed measures to appropriate operational objectives and baselines against which the performance of the support could be compared at this stage. However, in line with the Commission's Communication on "*The future of food and farming*", the way to assess the performance of types of intervention, including where appropriate, income support, will be considered.

⁹ See Commission replies (executive summary paragraphs I and V) to the Special Report No 1/2016 of the European Court of Auditors: "Is the commission's system for performance measurement in relation to farmers' incomes well designed and based on sound data?".

Event	Date
Adoption of Audit Planning Memorandum (APM) / Start of audit	29.6.2016
Official sending of draft report to Commission (or other auditee)	7.12.2017
Adoption of the final report after the adversarial procedure	7.2.2018
Commission's (or other auditee's) official replies received in all languages	6.3.2018

With an annual expenditure of around 18 billion euros, the Basic Payment Scheme, which was introduced in 2015, is the EU's biggest income support scheme for farmers. We found that the scheme was operationally on track, but that its impact on simplification, targeting and the convergence of aid levels was limited.

We make a number of recommendations to the Commission concerning the correction of farmers' payment entitlements, key controls by paying agencies, the systems for disseminating information among Member States, and the role of national certification bodies.

For the next programming period after 2020, we recommend that the Commission analyse the factors impacting income for all groups of farmers, their income support needs and the value of the public goods that farmers provide. Proposed income support measures for farmers should be linked, from the outset, to appropriate operational objectives and baselines against which their performance could be compared.



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