



Report to the Public Accounts  
Committee on the audit of  
EU funds in Denmark in 2011

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This report is submitted to the Public Accounts Committee in accordance with section 17(2) of the Auditor General's Act, cf consolidated act no. 101 of 19 January 2012.

The report concerns the following sections of the Fiscal Act: Section 7 – The Ministry of Finance, section 8 – The Ministry of Economic and Business Affairs, section 9 – The Ministry of Taxation, section 19 – The Ministry of Science, Technology and Innovation, section 24 – The Ministry of Food, Agriculture and Fisheries, and section 38 – Taxes and duties. A number of ministries have, by royal decree, changed names, and their remits have been reorganized. The following new ministries are therefore now included in the report: Section 8 – The Ministry of Business and Growth, section 14 – The Ministry of Housing, Urban and Rural Affairs, section 19 – The Ministry of Science, Innovation and Further Education.

As a consequence of the change of government in 2011, certain ministries were reorganised and remits were transferred to other ministers. Moreover, several audit cases referred to in this report have their source in previous accounting years and include issues that are referred to in the *Final report on the state accounts*. Rigsrevisionen has therefore decided not to list all the ministers in the report.

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# I. Opinion on the audit of European Union (EU) funds in Denmark in 2011

## OPINION ON THE AUDIT OF EU FUNDS IN DENMARK IN 2011

In the opinion of Rigsrevisionen, the 2011 financial statement of EU revenue and EU expenditure has been prepared in accordance with the Danish government accounting rules. The financial statement gives a true and fair view of revenue and expenditure in the financial year under review and of the financial position at the end of the financial year.

On the basis of the audit findings, Rigsrevisionen is of the opinion that, taken as a whole, the transactions underlying the 2011 financial statement of EU revenue and expenditure are legal, regular and in compliance with the provisions laid down by the European Commission (the Commission) and the Council of the European Union (the Council).

### *Emphasis of Matter*

Rigsrevisionen draws attention to issues relating to remote sensing, cross-compliance control and financial corrections:

- In its report to the Danish Public Accounts Committee on the audit of EU funds in Denmark in 2010, Rigsrevisionen concluded that the quality of remote sensing was not satisfactory, as irregularities were identified in just under half of the remote-sensing measurements that were performed by the Ministry of Food, Agriculture and Fisheries (the Ministry of Food) together with the Faculty of Agricultural Sciences at Aarhus University. In 2011, Rigsrevisionen has noted significant improvements in the organisation of the control, which is a reflection of the fact that many of the remote-sensing activities were transferred back to the Danish AgriFish Agency (AgriFish Agency) in 2011, and the improvement of the systems supporting the remote sensing activities. However, errors detected during the quality assurance performed by the AgriFish Agency in 2011 show that remote sensing needs to be further improved. An analysis made by the Agency of the causes of the errors showed that contrary to expectations and mainly due to shadowing and the angle of recording, it was not always possible to determine the limits of a parcel or determine which areas that should be excluded from the parcel on the basis of the available imagery. In particular, pastures bordering farming areas along windbreakers, woodland areas and certain types of ineligible areas (earth roads versus wheel tracks) are causing problems. Whether ineligible areas have been included in remote sensing can only be determined through physical inspection. Rigsrevisionen therefore finds it satisfactory that 97 per cent of all remote-sensing measurements were followed up by physical inspections in order to reduce the risk of financial corrections being imposed on Denmark by the Commission.

- Rigsrevisionen noted that in certain municipalities the number of cross-compliance controls performed was out of proportion to the number of cross-compliance breaches. The AgriFish Agency noted the same development and subsequently identified a number of municipalities that have consistently for several years reported very few or no farmers to the Agency for breaches of the cross-compliance requirements. The cross-compliance checks performed by these municipalities as part of the 1 per cent check of all the farms that received direct support in 2010 and 2011, have thus not triggered any penalties. The Danish authorities have decided that the majority of cross-compliance controls in the environmental area are to be performed by the municipalities. According to the Ministry of Food, this set-up prevents the ministry from supervising the cross-compliance control performed by the local authorities. In the opinion of Rigsrevisionen, the organisation of cross-compliance control needs to be re-considered to ensure that the overall responsibility for the control rests with a central authority in order to ensure consistent control.
- The Commission has – on several occasions in the past couple of years – opened proceedings against Denmark concerning exclusion of expenditure (repayment of previously received EU funding) amounting to approximately EUR 134.2 million for the period 2002-2011. The largest financial correction of EUR 101 million concerned exclusion of expenditure relating to hectare aid. The Ministry of Food did not agree with the premise of the Commission's decision and brought the case before the EU Court of Justice. The case was settled on 3 July 2012 with a dismissal of Denmark's claim and the financial correction of EUR 101 million imposed by the Commission was thus upheld. The Danish authorities have appealed the judgment on the grounds that it is based on inadequate legal reasoning and may therefore be disputed in an appeal. Moreover, the Danish authorities are of the opinion that the outcome of such an appeal could be to Denmark's advantage.

## II. Introduction

1. This report concerns the audit of EU funds in Denmark in 2011, ie the audit of revenue received from the EU (EU revenue) and contributions made to the EU (EU expenditure).

Seen from the perspective of the EU, the Danish revenue and expenditure is considered expenditure and revenue, respectively. In this report, Rigsrevisionen has decided to view matters from Denmark's perspective. The definition of revenue and expenditure is thus in compliance with the definition included in the Danish state accounts.

2. The audit performed in 2011 included EU revenue received through agricultural subsidy schemes under the Ministry of Food, Agriculture and Fisheries, the structural funds under the Ministry of Economic and Business Affairs, and EU expenditure under the Ministry of Taxation.

3. The objective of the audit was to assess whether the administration of EU funds in Denmark is generally handled in a satisfactory manner.

4. Based on an assessment of materiality and risk, Rigsrevisionen focused its audit of EU revenue in 2011 on three sub-objectives:

### *Agricultural subsidies*

- Were the EU agricultural subsidy schemes under the Ministry of Food administered in a satisfactory manner, and did the area control and cross-compliance control contribute to ensuring financially sound administration in the area?

### *Financial corrections*

- Was the action taken by the Ministry of Food to reduce the amounts of the financial corrections imposed on Denmark satisfactory?

### *The effect of local EU-subsidized projects*

- Were outcome targets defined for the European Regional Fund (the Regional Fund), the European Agricultural Fund for Rural Development (the Rural Fund) and the European Fisheries Fund (the Fisheries Fund) at Bornholm (Danish island in the Baltic Sea) and is it possible to measure the effect of subsidies received?

5. Rigsrevisionen's opinion on the audit of EU funds in Denmark in 2011 is included in chapter I. Chapter III includes an overview of the most significant conclusions that provide the basis for the opinion. Chapter IV presents a statement of EU revenue and EU expenditure as included in the Danish state accounts. The results of Rigsrevisionen's examination of the area control and cross-compliance control under the agricultural subsidy schemes are presented in chapter V. Chapter VI provides information on the financial corrections imposed on Denmark. The effect of local EU-subsidized projects is described in chapter VII, and chapter VIII briefly presents the results achieved in relation to Denmark's contributions to the EU (EU expenditure concerning taxes and levies).

6. A draft version of the report was presented to the Ministry of Finance, the Ministry of Business and Growth, the Ministry of Housing, Urban and Rural Affairs, the Ministry of Science, Innovation and Further Education, the Ministry of Food and the Ministry of Taxation, and their comments have to the widest possible extent been incorporated in the report.

7. A glossary of relevant terms and concepts is attached as appendix 1.

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### III. The most significant audit findings

#### MAIN CONCLUSION OF THE AUDIT

Rigsrevisionen performs an annual audit of EU revenue and EU expenditure, ie funds that Denmark receives from the EU or contributes to the EU budget. The greater part of the EU revenue concerns aid provided to farmers within the framework of various agricultural subsidy schemes, primarily the Single Payment Scheme. According to Rigsrevisionen's assessment, the administration of the agricultural subsidy schemes was generally satisfactory, but the administration of parts of area control and cross-compliance control was not entirely satisfactory. Rigsrevisionen's audit showed that the control exercised in these two areas was affected by errors and inconsistent quality. The audit showed that remote sensing, which is the method most frequently used to perform area control, was not entirely accurate and in some instances overstated the size of parcels compared to the control measurements performed. As regards the control of cross-compliance in the environmental area, which is performed mainly by local authorities, the number of environmental inspections performed seemed to be out of proportion to the number of cross-compliance breaches found in some of the municipalities; certain municipalities have not sanctioned any farmers on the basis of their cross-compliance checks in 2010 and 2011. The local authorities are required to check one per cent of all farmers that receive direct support from the EU.

Rigsrevisionen's examination of the financial corrections imposed on Denmark by the Commission showed that Denmark in the period 2002-2012 paid back approximately EUR 134.2 million, which corresponds to 1.2 per cent of the total agricultural aid received from the EU. Financial corrections imposed on countries that were members of the EU for this entire period, averaged 1.4 per cent of total subsidies received. At the end of August 2012, Denmark was facing 19 financial corrections. Nine of these have subsequently been closed and settled by the Commission. The Ministry of Food sought dialogue with the Commission in all these cases and, eg submitted new data or advocated its interpretation of the regulations in an effort to reduce the amount of the financial corrections.

This year Rigsrevisionen focused its attention particularly on aid provided to rural regions in Denmark through the Regional Fund, the Rural Fund and the Fisheries Fund. The objective of these subsidy schemes is to promote increased growth, employment and activities in the peripheral regions. Rigsrevisionen's audit showed that outcome targets on national and regional/local level had only to some extent been defined for the four selected subsidy schemes established within the framework of the Regional Fund, the Rural Fund and the Fisheries Fund. Rigsrevisionen recommends that the Ministry of Business and Growth and the Ministry of Housing, Urban and Rural Affairs should make a greater and more coordinated effort to define outcome targets and examine the effects of EU-funded projects established within the various subsidy schemes.

In 2011, EU expenditure totalled approximately EUR 2.5 billion of which customs duties and agricultural fees and levies accounted for approximately EUR 0.3 billion. Rigsrevisionen is of the opinion that the EU expenditure is generally administered in a satisfactory manner; yet the Danish tax authorities should continue their efforts to reduce the error rate in the customs clearance declarations.

The main conclusion is based on the following sub-conclusions:

*Were the EU agricultural subsidy schemes under the Ministry of Food administered in a satisfactory manner, and did area control and cross-compliance control contribute to ensuring financially sound administration in the area?*

The organisation and implementation of remote-sensing control improved in 2011 over 2010, but the audit findings reflect that remote sensing, as a method of control, is still – as expected – less accurate than physical inspections. This means that the size of parcels is sometimes overstated compared to the results of the physical control measurements. Particularly, pastures bordering farming areas along windbreakers, woodland areas and certain types of areas that should be excluded from the parcel are causing problems. Rigsrevisionen therefore finds it satisfactory that 97 per cent of the remote-sensing controls were followed up by physical inspections in order to reduce the risk of future financial corrections being imposed on Denmark by the Commission.

Rigsrevisionen is content that the administration of the Land Parcel Identification System has improved to the extent that Denmark in 2011 met more of the EU test criteria than in 2010. Rigsrevisionen also welcomes the fact that the Danish AgriFish Agency has launched several projects to further improve Denmark's performance.

Rigsrevisionen noted that in certain municipalities the number of cross-compliance controls performed was out of proportion to the number of cross-compliance breaches. The AgriFish Agency noted the same development and subsequently identified a number of municipalities that have consistently for several years reported very few or no farmers to the Agency for breaches of the cross-compliance requirements. The cross-compliance checks performed by these municipalities – as part of the one per cent check of all the farms that received direct aid in 2010 and 2011 – have thus not triggered any penalties at all.

The Danish authorities have decided that the majority of cross-compliance checks should be performed by local level authorities. According to the Ministry of Food, this set-up prevents the ministry from supervising the cross-compliance control performed by the municipalities. In the opinion of Rigsrevisionen, the organisation of cross-compliance control needs to be re-considered to ensure that the overall responsibility for the control rests with a central authority in order to ensure consistent control.

Rigsrevisionen's review of the project *Enhanced control* showed that several of the projects launched by the AgriFish Agency had improved the quality of area control. However, the effect of some of these projects on, for instance, the quality of remote sensing and cross-compliance control remains to be seen. Yet, Rigsrevisionen finds it satisfactory that the AgriFish Agency has developed an action plan for the areas where the performance can be further improved.

*Was the action taken by the Ministry of Food to reduce the amounts of the financial corrections imposed on Denmark satisfactory?*

At the end of August 2012, Denmark was facing 19 financial corrections. Nine of these have subsequently been closed and settled by the Commission. The Ministry of Food sought dialogue with the Commission in all the cases and, eg submitted new data or advocated its interpretation of the regulations in order to reduce the amount of the financial corrections. Rigsrevisionen is not entirely satisfied that the Commission has found reasons to impose a total of 19 financial corrections on Denmark, but has noted that the amounts of the financial corrections have decreased in the period 2002-2012.

The correction involving the largest amount concerns hectare aid and repayment of EUR 101 million received in the period 2002-2004. The Danish authorities brought the case before the EU Court of Justice with a claim for annulment, alternatively, reduction of the financial correction. On 3 July 2012, the EU Court of Justice made its ruling and upheld the Commission's decision. The Danish authorities have appealed the judgment on the grounds that it is based on inadequate legal reasoning and may be disputed in an appeal. Moreover, the Danish authorities are of the opinion that the outcome of such an appeal could be to Denmark's advantage.

*Were outcome targets defined for the European Regional Fund (the Regional Fund), the European Agricultural Fund for Rural Development (the Rural Fund) and the European Fisheries Fund (the Fisheries Fund) at Bornholm (Danish island in the Baltic Sea), and is it possible to measure the effect of subsidies received?*

In connection with the overall objective of the Regional Fund, Rigsrevisionen noted that outcome targets had not been defined for the employment effect. Moreover, the three underlying outcome targets set for the programme period in relation to innovation, the application of information and communications technology and entrepreneurship, were very broad and vague. Rigsrevisionen finds that the Danish authorities should set outcome targets for the overall expected effect on employment. More concrete and clear outcome targets should also be defined for the sub-objectives set for the programme period, and guidance material should be developed on the interpretation of the outcome requirements. Rigsrevisionen also finds that the Danish Business Agency and the regional growth forums should direct more attention to documenting effect.

Rigsrevisionen finds that the Ministry of Housing, Urban and Rural Affairs should consider how outcome targets for the various subsidy schemes can be defined and the effect measured. Furthermore, coordination of requirements determined centrally and requirements set at local level should be improved.

Finally, Rigsrevisionen sees a need for improved coordination of performance measurement activities between the Danish Business Agency and the Bornholm Growth Forum. Action is required in relation to the current practice, where both the Danish Business Agency and the Bornholm Growth Forum follow up on performance, and in relation to changes and projects implemented by the Danish Business Agency and the Bornholm Growth Forum, respectively. A coordinated effort is also required in respect of the schemes under the Rural Development Programme and the Danish Fisheries Development Programme to ensure that the effects of the programmes are adequately followed up by the Ministry of Housing, Urban and Rural Affairs and the Local Action Groups (LAGs).

## IV. EU funds as included in the Danish state accounts

8. The state accounts for 2011 includes a statement of the funds that Denmark received from the EU (EU revenue) and the contributions that Denmark made to the EU (EU expenditure). The statement is presented below in table 1.

**Table 1. EU revenue and EU expenditure in 2011  
(EUR million)**

<b>EU REVENUE</b>	
<b>Agricultural and structural funds</b>	<b>1,117.07</b>
The European Agricultural Guarantee Fund	932.42
The European Agricultural Fund for Rural Development	70.32
The European Social Fund	69.51
The European Regional Fund	32.38
The European Fisheries Fund	12.44
<b>EU programmes outside the agricultural and structural funds</b>	<b>7.15</b>
Research and innovation	5.29
Education and training	1.10
Transport infrastructure	0.76
<b>Other EU revenue</b>	<b>44.24</b>
<b>Total EU revenue</b>	<b>1,168.48</b>
<b>EU EXPENDITURE</b>	
<b>Earmarked funds</b>	<b>68.40</b>
Contributions to the European Development Fund	67.26
Contributions to the European Synchrotron Radiation Facility	0.87
Contributions to the Helsinki Commission	0.21
Contributions to the European Environmental Bureau	0.03
Contributions to the Financial Instrument for the Environment	0.03
<b>Taxes and levies</b>	<b>2,442.96</b>
Contributions calculated on the basis of the gross national income	1,717.25
Contributions calculated in accordance with the joint basis of calculation for value added tax	403.36
Share of custom duties and agricultural fees and levies less collection costs	313.80
Co-responsibility levy (milk)	8.53
<b>Total EU expenditure</b>	<b>2,511.36</b>

Note: Rate of exchange: EUR 0.7519 = DKK 1.00. Totals may not add up due to rounding.

In table 1, revenue is broken down on agricultural and structural funds, programmes outside the framework of agricultural and structural funds and other EU revenue. Expenditure is broken down on earmarked expenditure and taxes and levies. The statement included in the Danish state accounts shows that Denmark in 2011 received EU funding of approximately EUR 1.1 billion and transferred approximately EUR 2.5 billion to the EU budget.

EU revenue provided directly by the Commission to private and independent institutions and organisations is not included in the Danish state accounts and therefore not included in table 1 either.

Programmes within the framework of the *Agricultural and structural funds* are under shared management, ie the administrative authorities share the administrative responsibility with the Commission and execute the payments to the beneficiaries. *Programmes outside the framework of agricultural and structural funds* include programmes that are managed directly by the Commission, which means that the Commission executes the payments to the national beneficiaries. *Other EU revenue* concerns transfers from the Commission to Danish government institutions that do not belong to either of the categories of revenue mentioned above.

#### **EU revenue**

9. The greater part of the total EU revenue is provided within the framework of the agricultural and structural funds and amounted to a total of EUR 1,117 billion in 2011. The Danish government serves as a link for financial transfers between the EU and the final beneficiaries. Payments made through the European Agricultural Guarantee Fund (the Agricultural Guarantee Fund), the Rural Fund and the Fisheries Fund are handled by the AgriFish Agency under the Ministry of Food. The Danish Business Agency under the Ministry of Business and Growth handles payments from the Social Fund and the Regional Fund.

10. The Agricultural Guarantee Fund is in money terms the largest fund. In 2011, aid provided through this fund to a number of programmes totalled EUR 932.4 million. The most important scheme under the Agricultural Guarantee Fund is the Single Payment Scheme, which in 2011 managed funds of in total EUR 881.5 million for allocation to approximately 46,500 farmers. The Ministry of Food has informed Rigsrevisionen that the amount of revenue indicated for the Agricultural Guarantee Fund in the statement included in the Danish state accounts should be reduced by EUR 3.2 million to EUR 929.2 million. This variance is caused by the fact that a couple of institutions under the Ministry of Justice and the Ministry of the Environment have booked EU revenue of EUR 0.6 million and EUR 3.9 million, respectively, relating to the institutions' ownership of, for instance, agricultural land, whereas the Ministry of Food has included EU revenue of EUR 1.3 million from the operating account of the AgriFish Agency, which is not included in the state account statement.

11. The second-largest source of EU revenue is the structural funds, ie the Social Fund and the Regional Fund. In 2011, revenue from the structural funds totalled EUR 101.9 million with the Social Fund accounting for EUR 69.5 million and the Regional Fund accounting for EUR 32.4.

12. EU subsidies are also provided through the Rural Development Fund and the Fisheries Fund. In 2011, revenue relating to these two funds totalled EUR 70.3 million and EUR 12.4 million, respectively. Aid provided through the Rural Development Fund is mainly supporting achievement of the following three objectives:

- improvement of the competitiveness of the agricultural and forestry sector;
- improvement of the environment and landscape;
- improvement of the quality of life in rural areas and encouragement of diversification of rural economy.

The two largest schemes under the Rural Development Fund were in 2011; *Development in primary agriculture* – EUR 40.0 million and *Job creation and attractive quality of life in the rural areas* – EUR 13.9 million. The Fisheries Fund provides aid for the implementation of structural measures, etc in the fisheries sector. The Ministry of Food has informed Rigsrevisionen that the figures in table 1 concerning the Rural Development Fund and the Fisheries Fund should be increased to EUR 72.1 million and EUR 12.7 million, respectively. These corrections are caused by the fact that the statement prepared by the Ministry of Food includes EUR 1.5 million for technical assistance in connection with the administration of the rural development schemes and EUR 0.3 million for the wetland restoration projects. For the Fisheries Fund, the Ministry of Food has included technical assistance for the administration of the scheme, ie EUR 0.3 million, which amount is not included in the statement in the Danish state accounts.

13. EU programmes outside the framework of agricultural and structural funds are mainly operating on funds that have been paid directly from the EU to the final beneficiaries. It appears from the table that the EU in 2011 funded projects on *Research and innovation*, *Education and training* and *Transport infrastructure*. With a total budget of EUR 5.3 million, *Research and innovation* was the single largest project in 2011. Funds awarded to this project can be broken down as follows: The Ministry of Climate and Energy received EUR 2.3 million, the Ministry of Research, Technology and Innovation received EUR 1.3 million and the Ministry of Defence, the Ministry of Food, the Ministry of Culture and the Ministry of Children and Education shared the balance of EUR 1.7 million.

It should be noted that EU revenue relating to independent institutions like, for instance, universities, is not included in the table; the universities are included in the fiscal act as subsidized institutions, and therefore only the grant provided by the Danish government is included in the fiscal act and in the state accounts.

14. The universities have stated that they have received EUR 76.9 million from the Commission. The Commission supports a large number of mainly research-based projects under the EU subsidy programmes, and the universities under the Ministry of Research, Innovation and Further Education are the main beneficiaries. It appears from the Danish state accounts that the ministry received total funding of EUR 2.5 million in 2011. In addition, the Danish Agency for Universities and Internationalisation managed subsidies of in total EUR 14.5 million on behalf of the Commission.

15. Other EU revenue of EUR 44.3 million includes EU revenue from a broad spectre of sources. The largest amount concerns EU subsidies from the European Globalisation Adjustment Fund and totals EUR 24.0 million. Also subsidies to the Danish authorities' administration of the EU programmes (technical support) and subsidies to various EU projects are included under other EU revenue.

#### **EU expenditure**

16. EU expenditure is divided into two categories; *Earmarked expenditure* representing Denmark's direct contributions to programmes and project outside the EU general budget, and *Taxes and levies* representing Denmark's contributions to the EU budget. It appears from table 1 that EU expenditure amounted to approximately EUR 2.5 billion with taxes and levies accounting for approximately EUR 2.4 billion, or 97 per cent, of this amount.

17. The earmarked expenditure of approximately 3 per cent, or EUR 67.2 million, can mainly be referred to Denmark's contribution to development assistance, which is provided by the EU through the European Development Fund (EDF). The EDF operates with five-year programming periods and has a budget of EUR 3.0 billion for the period 2008-2013. EDF funds go to development work in countries in the African, Caribbean and Pacific countries (the ACP countries).

18. EU expenditure under section 38 – Taxes and duties – has in the Danish state accounts been broken down on three elements. As indicated in table 1, the total amount of approximately EUR 2.4 billion consists of contributions based on gross national income (GNI-based budget resources) EUR 1.7 billion; VAT-based resources of approximately EUR 403.4 million and customs duties and agricultural fees and levies of approximately EUR 313.8 million.

#### **Development of consolidated EU accounts in Denmark**

19. Rigsrevisionen and the Ministry of Finance have for a couple of years discussed the possibility of publishing a consolidated financial statement of EU funds in Denmark. Rigsrevisionen would like for the Ministry of Finance to present consolidated accounts for all EU funds included in the Danish state accounts.

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20. The consolidated accounts would include a profit and loss account, balance sheet, cash flow statement and explanatory notes. A consolidated EU financial statement would serve to shed light on the various financial aspects of the transactions between the Danish government and the EU.

21. To be able to produce consolidated EU accounts based on well-defined and clear rules, the Ministry of Finance needs to modify various internal rules and systems and further specify the government's chart of accounts. These modifications should have been implemented in the course of the autumn 2011 to allow the AgriFish Agency to make entries in the accounts in compliance with the updated rules as per 1 January 2012 and thus produce a consolidated EU financial statement for the agricultural policy area for 2012.

Early in September 2012, the Ministry of Finance informed Rigsrevisionen that the AgriFish Agency still could not make these entries, because system errors had delayed the Agency's implementation of a new financial system. Yet, the Ministry of Finance expects to elaborate a consolidated EU financial statement for the agricultural policy area for 2012.

The Ministry of Finance should also change the current governmental structure of accounting, as this is not designed to embrace the elaboration of a separate EU balance sheet. The Ministry of Finance expects to be able to produce a consolidated financial EU statement for 2013 covering all policy areas.

## V. The agricultural subsidy schemes under the Ministry of Food

In the opinion of Rigsrevisionen, the agricultural subsidy schemes are generally administered in a satisfactory manner, but the administration of parts of the area control and cross-compliance control is not entirely satisfactory.

22. The Ministry of Food accounts for approximately EUR 1 billion of the total EU revenue of approximately EUR 1.2 billion, cf. chapter IV on the information provided in the Danish state accounts on EU funds in Denmark.

23. The assessment of the administration of the agricultural schemes is based on Rigsrevisionen's audit of the Single Payment Scheme, which was the largest scheme in 2011 making annual payments to approximately 46,500 farmers who received in total approximately EUR 872.5 million.

The audit performed by Rigsrevisionen included follow-up on the remote sensing performed under the area control, which was referred to in the report to the Public Accounts Committee on the audit of EU funds in Denmark in 2010. Rigsrevisionen has also reviewed the Commission's test of the quality of the Danish Land Parcel Identification System. Furthermore, Rigsrevisionen has audited the cross-compliance control, which is also part of the area-based schemes, with focus on the control exercised by the municipalities in the environmental area. Finally, this chapter presents the outcome of the assessment of the project *Enhanced Control* that was completed in 2011. The purpose of the project was to reduce the risk of financial corrections being imposed on Denmark by the Commission.

24. Rigsrevisionen's examination of the agricultural schemes under the Ministry of Food showed the following:

- Remote-sensing control was better organized and implemented in 2011 than in 2010, but the audit evidence showed that remote sensing as a method of control is still less accurate than physical inspections on the spot. Remote sensing sometimes overstates the size of areas measured compared to the results derived from physical inspections. Pastures bordering farming areas, in particular along windbreakers, woodland areas and certain types of areas that should be excluded from the parcel (earth roads versus wheel tracks), still cause problems. Rigsrevisionen therefore finds it satisfactory that 97 per cent of all remote-sensing measurements were followed up by physical inspections in order to reduce the risk of financial corrections being imposed on Denmark by the Commission.
- Rigsrevisionen is content that the administration of the Land Parcel Identification System has improved to the extent that Denmark in 2011 has met more of the EU's test criteria than in 2010. Rigsrevisionen also welcomes that the AgriFish Agency has launched several projects to further improve Denmark's performance.

- Rigsrevisionen noted that in certain municipalities the number of environmental inspections performed was out of proportion to the number of cross-compliance breaches. The AgriFish Agency noted the same development and identified a number of municipalities that have consistently for several years reported very few or no farmers to the agency for breaches of the cross-compliance requirements. Consequently, these municipalities have not sanctioned any farmers on the basis of their part of the cross-compliance checks of all the farms that received direct aid in 2010 and 2011. The Danish authorities have decided that the majority of the cross-compliance checks should be performed by local level authorities. According to the Ministry of Food, this set-up prevents the ministry from supervising the cross-compliance control performed by the municipalities. In the opinion of Rigsrevisionen, the organisation of cross-compliance control needs to be re-considered to ensure that the overall responsibility for the control rests with a central authority in order to ensure consistent control.
- Rigsrevisionen's review of the project *Enhanced Control* shows that the AgriFish Agency has launched several projects that have improved the quality of area control. However, the effect of some of these projects on, for instance, remote sensing and cross-compliance control remains to be seen. Yet, Rigsrevisionen finds it satisfactory that the AgriFish Agency has worked out an action plan for the areas where the performance can be further improved.

#### A. Introduction to the Single Payment Scheme

25. Farmers who wish to apply for aid from the Single Payment Scheme must forward an application to the AgriFish Agency every year. The cross-compliance regulation applies to the entire farm and all the fields owned by the farmer and the farmers must therefore register all their agricultural land including land for which they do not want to claim payment.

26. Upon receipt of the applications, the AgriFish Agency will compare the data contained in the applications with the data registered in the Land Parcel Identification System. Moreover, the Agency will check whether the farmers hold the relevant entitlements.

27. In the course of the year, the AgriFish Agency performs sample-based checks to confirm the correctness of the land size information provided by the farmers in the application forms. According to the EU regulations, minimum five per cent of all farmers applying for Single Payment Scheme payments should be subjected to on-the-spot checks. In accordance with the EU regulations, the Member States may use remote sensing as a method to carry out on-the-spot checks. Satellite images or aerial photos (ortho images) provide the basis for this control. When using remote sensing for control, the Member States are required to make an assessment of the satellite or ortho images of the farmers' fields to determine the crop and measure the area. Moreover, physical inspections of the farmers' fields will be required if the assessment of the satellite or ortho imagery does not – according to the responsible authority (the AgriFish Agency) – suffice to confirm the correctness of the data provided in the applications. It is checked whether the farmers have included ineligible areas, and whether the areas meet the requirements for good agricultural and environmental condition, ie are uncultivated fields, for instance, being mown at least once every second year in the period 1 July - 15 September, and are permanent grazing areas mown minimum once every year in the period 1 July - 15 September.

In 2011, the area control of five per cent of all applications was based on remote sensing followed up by physical inspections on-the-spot. 2,844 farmers and 20,600 parcels were checked. Physical inspection of minimum one parcel was carried out at 97 per cent of the farms selected for control because the satellite or ortho images resulting from the remote-sensing control were inadequate. It is often difficult to assess satellite and ortho imagery of eligible grazing pastures, as these may be overgrown with species of plants that are not eligible like, for instance, rush and other wetland vegetation. Only three per cent of the applications could thus be finalized on the basis of remote-sensing control only.

28. Many errors were detected during the control of five per cent of the applications; in 2011, irregularities were detected in 48 per cent of the checked applications. Breaches ranged from minor errors like, for instance, inclusion of areas smaller than 0.1 ha – which are not eligible – to considerable sanctionable overstatements of areas, ie deviations of more than three per cent or deviations of more than 2 ha between area size stated in the application and the actual size of the measured area.

29. Penalties are imposed according to a tiered scale:

- Deviations in field sizes exceeding three per cent (up to and including 20 per cent or more than two ha) between the application and the measured area within one single crop group reduce aid by an amount corresponding to twice the size of the deviation.
- Deviations exceeding 20 per cent of the measured area (confirmed area) will reduce support by 100 per cent, ie the farmer will not receive any support that year for the crop group in question.
- Deviations exceeding 50 per cent will trigger refusal of the application by the Food Agency. This means that the farmer will not receive any support that year, and support provided in the subsequent three years will be reduced.

In 2011, 20.6 per cent of the remote-sensing controls that were re-checked triggered penalties. Penalties were distributed within the three above-mentioned categories as follows; 16.9 per cent, 2.2 per cent and 1.5 per cent, respectively.

Box 1 exemplifies the calculation of a penalty and its implications for the support provided to the farmer.

#### BOX 1. CALCULATION OF PENALTY IMPOSED FOR NON-COMPLIANCE

Support provided to the farmers will be reduced if they fail to meet certain requirements. If sanctioned, the farmers receive less aid than they might have expected on the basis of their application.

A farmer has stated an area size of 100 ha in his/her application. According to a control measurement, the area of the eligible land is only 95 ha. The deviation of five ha corresponds to 5.3 per cent of the measured area. The area will thus be reduced by twice the size of the deviation, corresponding to 10 ha. At a rate of EUR 299 per ha, the penalty will be EUR 2,990.

The size of the area that is providing the basis for the payment of support will thus be 85 ha (95 hectare minus 10 ha) and the farmer will therefore receive support corresponding to the measured area minus the penalty, ie EUR 25,415 (95 ha x EUR 299 minus 10 ha x 299 = EUR 28,405 minus EUR 2,990).

Cross compliance means that farmers receiving support under the Single Payment Scheme – or certain schemes under the Rural Fund – are required to comply with certain requirements concerning the environment, health, animal welfare and the agricultural condition of their land to qualify for full support.

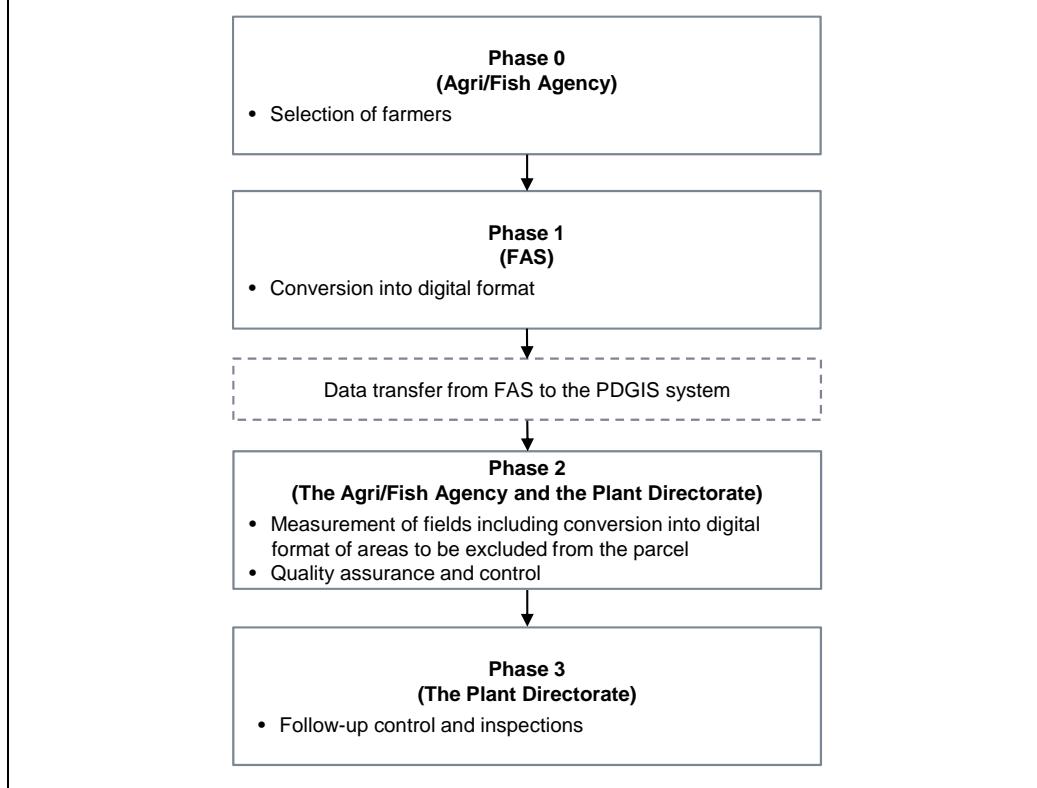
If the farmers fail to comply with the requirements, the support will be reduced. The Agri-Fish Agency is responsible for organising the cross-compliance control, whereas the local authorities and several government authorities perform the actual control.

## B. Remote-sensing control

30. Remote sensing was in 2011 performed by the Faculty of Agricultural Sciences at Aarhus University (FAS), the AgriFish Agency and the Danish Plant Directorate in combination. Remote sensing was transferred to the AgriFish Agency with effect from 2012. The AgriFish Agency was established on 1 October 2011 and is a merger of the Food Agency, the Plant Directorate and the Fisheries Agency.

31. In 2011, the remote-sensing procedure was as follows; in phase 0, the AgriFish Agency (responsible authority) selected farmers for remote sensing; the data on the selected farmers was forwarded to FAS, which prepared the satellite photos and converted the field parcel data into digital format (phase 1) which was then transferred to the AgriFish Agency and the Plant Directorate through the Land Parcel Identification System (PDGIS-system). In phase 2, the AgriFish Agency and the Plant Directorate measured the parcels and converted areas that should be excluded into digital format, and performed quality assurance and control. Finally, in phase 3, the Plant Directorate checked data through physical inspections of selected fields on-the-spot. The remote-sensing phases are illustrated in figure 1.

**Figure 1. Phases of remote-sensing control**



32. In its report to the Danish Public Accounts Committee on the audit of EU funds in Denmark in 2010, Rigsrevisionen included an emphasis of matter paragraph on remote-sensing control, because irregularities were detected in almost 50 per cent of the controls performed in collaboration with FAS. Some of the errors were caused by a mid-process change of the digitalization procedure; because the AgriFish Agency was running behind schedule and not able to submit data from the applications to FAS on time, it was decided that the Agency should perform the conversion of the not eligible areas into digital format (phase 2) before FAS performed the digital conversion of the field parcels (phase 1). This approach, however, proved ineffective and extensive correction of errors was required subsequently. The decision to transfer remote sensing in full to the AgriFish Agency was also to some extent founded on this experience.

33. The AgriFish Agency has informed Rigsrevisionen that remote sensing improved considerably in 2011 compared to 2010 and followed the usual business procedures laid down for the implementation of remote-sensing control. The AgriFish Agency was thus able to provide application data on time to FAS, and FAS was able to convert the field parcels into digital format and return the data to the Agency as planned. The Agency could thus proceed to phase 2 of remote sensing and conduct quality assurance and control, perform the actual remote sensing and convert areas that should be excluded into digital format.

According to the Agency, this development also reflects the effect of a series of activities that were launched to improve remote sensing like, for instance; enhanced guideline on remote sensing in the form of actual remote-sensing instructions, guidance on converting data in a digital format and enhanced remote-sensing technology. The latter has improved the quality of imagery and thus made it easier for the staff to assess and determine the size of eligible parcels. The introduction in 2011 of a second processing of all control cases to be performed by an unbiased member of staff has enhanced also the quality assurance of remote-sensing control. To this should be added that remote sensing is now performed by experienced staff members with relevant qualifications; they have been recruited among the members of the field mapping team and among the fixed employed agricultural inspectors, and this has raised the level of professionalism considerably.

34. The many overstatements detected during the checks of the five per cent sample make it imperative that parcels are correctly measured so that payments are made only for eligible areas. Rigsrevisionen has therefore compared the results of the quality control of remote sensing performed in 2010 and 2011.

The results of this comparison are presented below and show that the technical execution of remote sensing still causes problems in spite of the improved remote-sensing process. On the average, land size is still overstated as a result of the remote sensing and in consequence farmers may receive aid for areas that are not eligible.

35. Every year, the AgriFish Agency checks a sample of remote-sensing results; in 2011, 34 applications that had previously been approved for subsidies under either the Single Payment Scheme or the Rural Fund were subjected to quality control. The rechecks were performed on the basis of ortho imagery. If the inspectors detected errors on the basis of the ortho photos, these would be supplemented with GPS measurements that are considered more accurate.

36. In 2011, five out of 34 applications in the sample (approximately 15 per cent) changed status from eligible to not eligible due to overstatements that were not detected during the remote sensing. In 2010, five out of the 40 applications in the sample (approximately 13 per cent) changed status from eligible to not eligible due to overstatements detected during the physical inspections. The quality of remote sensing has thus deteriorated slightly.

37. The AgriFish Agency has examined why the remote sensing in some cases overstates the size of land compared to the results of the control measurements. The analysis showed that it is not always possible to determine the limits of a parcel or determine which areas should be excluded from a parcel on the basis of the available imagery – primarily due to shadowing and the angle of recording. Particularly, pastures bordering farming areas along windbreakers, woodland areas and certain types of ineligible areas (earth roads versus wheel tracks) are causing problems. It requires a physical inspection to determine whether the land area has been overstated.

38. The Plant Directorate and the internal auditors of the AgriFish Agency also rechecked the measurements of land size; the recheck included 14 farmers who had all received payments under the Single Payment Scheme.

39. The deviations detected between the results of the ordinary control and the results of the recheck were so large that they affected subsidy payments to four out of the 14 farmers (approximately 29 per cent) that were rechecked. In 2010, the recheck had financial implications for two out of 11 farmers (approximately 18 per cent). On the basis of the recheck, the internal auditors of the AgriFish Agency concluded that the total eligible areas were slightly smaller than assumed on the basis of the ordinary remote sensing.

40. During its audit visit to Denmark in May 2012, the Commission also assessed the quality of remote sensing and established that certain ineligible areas had not been excluded. In some instances these ineligible areas had not been detected by the inspectors. In its audit report, the Commission highlighted examples of incorrect remote sensing; the remote-sensing measurement of eight parcels out of 30 included ineligible areas. The sample of 30 parcels was selected on the basis of a thorough screening of ortho imagery. Rigsrevisionen notes, however, that the areas that were rechecked were quite small – the largest was 0.3 ha. The AgriFish Agency calculated the total deviation for 2010 at 0.52 ha out of a total of 1,276.5 ha (approximately 0.04 per cent) and for 2011 it was 0.1 ha out of a total of 1,432.1 ha (approximately 0.01 per cent). The Agency and the Commission are currently discussing the size of the ineligible areas.

On the basis of its findings, the Commission concluded that there were weaknesses in the physical control and inherent risk of loss of funds from the Agricultural Fund, because ineligible areas had been accepted as eligible by the inspectors.

41. Rigsrevisionen's review of the results described above shows that remote sensing on the average overstates the size of areas compared to the results of the rechecks. Taking into consideration the risk of financial exclusions, Rigsrevisionen therefore finds it satisfactory that 97 per cent of the parcels that have been measured by means of remote sensing are subjected to physical inspections before the cases are closed.

### C. The Commission's quality assurance of the Danish land parcel identification system

42. In Denmark, agricultural farmland is mapped as parcels consisting of one or more fields delimited by fixed, visible characteristics of the landscape like, for instance, roads, streams and hedgerows. The area of the fields making up a parcel is measured and the data is loaded into the AgriFish Agency's land parcel identification system. The farmers are required to register changes in the landscape that have an impact on the size of the land eligible for support to allow the AgriFish Agency to update the register. Changes in land parcels that follow from the AgriFish Agency's administrative and physical inspections are also registered in the system.

43. The Commission has introduced a new concept for quality assurance of reference parcels – the so-called Executable Test Suite (ETS). The test is designed to give the Member States an opportunity to assess the quality of reference parcels and subsequently take correction action, if required. Approximately 800 parcels in Denmark that have been randomly selected by the Commission will be subjected to the ETS. These parcels will be tested for compliance with seven criteria laid down by the Commission and the test will include, for instance, whether the AgriFish Agency has updated the land parcel identification systematically to reflect reported changes in the landscape. In 2011, Denmark met five of the seven quality criteria, ie one more than in 2010. The two criteria that Denmark did not manage to meet in 2011 concerned 1. correct updating of data in the land parcel identification system; the threshold value was 72 parcels, but 125 parcels were not updated, and 2. critical defects relating to the fact that some areas were no longer eligible for support, because a new road had been built or the land had been planted with Christmas trees, which did not appear from the ortho imagery. Defects of this nature are not allowed to affect more than 10 parcels according to the criteria, but in Denmark 16 parcels were affected.

44. The AgriFish Agency has implemented various projects to improve its future performance on the test; in the period February 2011 to January 2012, approximately 85,000 parcels out of the approximately 320,000 parcels in Denmark were updated. Late in 2011, the Agency introduced monthly mini-tests of 50 selected parcels that had been processed the month before. The investigation of the causes of irregularities occurring during the mini-test, addresses also the administrative procedure and inaccurate transfer of data, etc. The 125 parcels that turned out to be affected by errors have all been updated. All analogue field maps will be converted into digital format and from 1 January 2013, farmers applying for support under the Single Payment Scheme are no longer allowed to submit analogue field maps. This measure will contribute to ensuring more accurate measurement of parcels as will the fact that external data like, for instance, information on new roads, etc, will also be used to update the field maps. Lastly, the importance of reporting changes in land will be impressed on the farmers.

45. Rigsrevisionen welcomes the fact that that the Danish land parcel identification system now meets more of the criteria set by the Commission, and that the AgriFish Agency has launched various projects to improve Denmark's performance on future tests.

#### D. Environmental cross-compliance control

46. Rigsrevisionen has audited the environmental cross-compliance control that is primarily performed by local level authorities. The audit covered control results for 2010 and 2011.

According to the EU regulations, control of cross compliance can be performed as follows:

- as control performed at the farms selected for control (1 per cent of all farmers that have applied for aid) on the basis of a risk assessment;
- as *Other control* performed by the supervising/controlling authorities when an inspection on-the-spot, that has been arranged for other purposes, comes across breaches of the cross-compliance requirements.

##### *Results of the control performed by the local authorities in 2010 and 2011*

47. Rigsrevisionen has looked closer at the environmental cross-compliance control performed by the local authorities. Rigsrevisionen's audit included both the cross-compliance control performed at the approximately 500 farms in the 1 per cent sample, and the results of the control reported in connection with the so-called *Other control*.

Table 2 shows the results of the control performed by the local authorities in 2010 and 2011 broken down on the various cross-compliance requirements. The table includes both the results of the general cross-compliance control and the results of *Other control*.

**Table 2. Overview of penalties imposed for breaches of the cross-compliance requirements in 2010 and 2011**

Requirement	Specification of requirement	2010	2011
1.1	Substances that are potentially hazardous to the groundwater, soil and subsoil	55	29
1.2	Use of sewage sludge for agricultural purposes (nature of sewage sludge used)	1	1
1.3	Application of sewage sludge for agricultural purposes (timing of application)	0	1
1.4	Soil management and accounting requirements	6	2
1.5	Restrictions on application of sewage sludge	5	2
1.6	Hygienic restrictions for the use of sewage sludge	0	1
1.7	Building accommodation for animals kept for farming purposes	21	23
1.8	Storage of animal manure	2	7
1.9	Storage of farmyard manure	67	78
1.10	Storage of compost and farmyard manure	10	16
1.11	Storage of silage	36	19
1.12	Storage of slurry, silage water and sewage sludge	17	14
1.13	Application of animal manure and ensilage water (timing)	3	4
1.14	Application of animal manure to bare land (timing)	2	7
1.15	Restrictions for application of animal manure/restrictions for application to specific areas	28	28
1.16	Two metre protection zone along natural watercourses and lakes	250	129
1.23	Protection of natural habitats encompassed by Natura 2000	9	10
1.26	Protection of polders of the Tønder marsh encompassed by Natura 2000	0	0
4.7	Burning of grass or similar crop residue	1	0
4.10	Controlling the Giant Hogweed	18	16
4.11	Managing water resources	29	96
<b>Total</b>		<b>562</b>	<b>483</b>

It appears from table 2 that breaches fall mainly within the following five categories; 1.1) Substances that are potentially hazardous to the groundwater, soil and subsoil; 1.7) Building accommodation for animals kept for farming purposes; 1.9) Storage of farmyard manure; 1.16) Two metre protection zone along natural watercourses and lakes; 4.11) Managing water resources. Breaches of this nature make up 73 per cent of all breaches in 2011. The remaining 16 requirements thus only account for 27 per cent of the breaches found.

A number of requirements are hardly ever violated; the use and application of sewage sludge to agricultural land (1.2-1.6); application of animal manure (1.13-1.15); breaches concerning the Tønder marshland in the Wadden Sea area (1.26) and burning grass or similar crop residue (4.7).

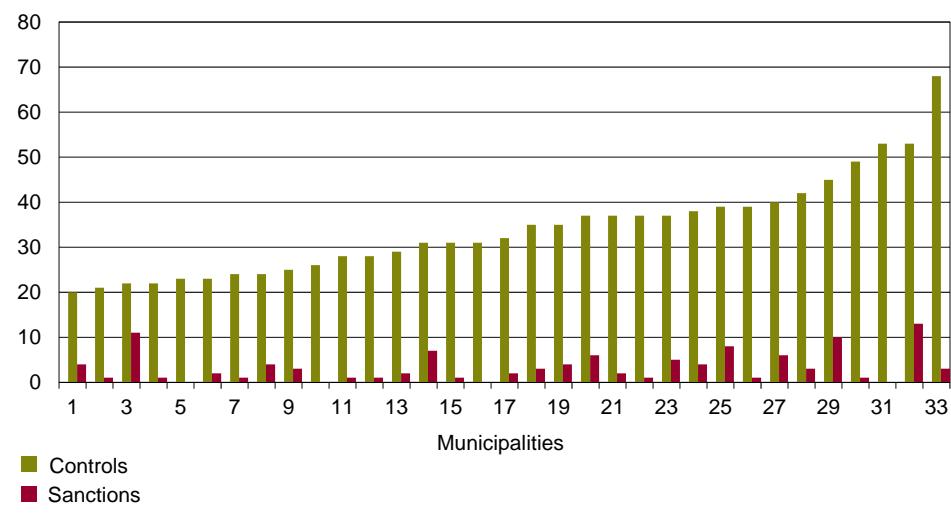
48. According to the AgriFish Agency, penalties are rarely imposed on the basis of breaches of these requirements, because they are relevant only to very few farmers and difficult to ascertain. The sewage sludge requirements are only relevant for 470 of the 50,900 beneficiaries; the requirements concerning application of animal manure (1.13-1.15) concerns restrictions for the timing of application, method of application, and areas to which the manure may be applied. Compliance with requirements of this nature can only be checked if the controlling authorities are at the farm when the activity takes place – or shortly after. Otherwise, the controlling authorities will not be able to neither establish nor document the breach and report the farmer to the relevant authorities.

49. The AgriFish Agency has informed Rigsrevisionen that although a requirement may be relevant only for a minority of beneficiaries or for a limited time, the Member States must include these requirements in their cross-compliance control.

In connection with a review of 20 cases checked by the municipalities, Rigsrevisionen found that in some of the control reports, the controlling authorities had ticked the field *OK* next to requirements that were not relevant for the beneficiary in question, whereas others had ticked the field *not relevant*. Rigsrevisionen is of the opinion that the controlling authorities should indicate why the cross-compliance requirements in question are not relevant. The AgriFish Agency's guidance on cross-compliance control states that if a single requirement is not relevant for a farmer, this requirement should be reported as being *not relevant*. Rigsrevisionen recommends that the practice of reporting should be consistent.

50. Rigsrevisionen also studied the distribution of breaches on the individual municipalities. Figure 2 shows the number of checks and penalties imposed in municipalities that performed more than 20 cross-compliance checks (the mandatory 1 per cent control) in 2010 and 2011, respectively.

**Figure 2. Number of checks and penalties imposed in municipalities that performed more than 20 cross-compliance checks in 2010 and 2011, respectively**



Apparently, there is no connection between the number of checks performed and the number of penalties imposed; some municipalities performed many checks, but did not impose any penalties, like no. 31, and others performed few checks, but imposed many penalties, like no. 3, which performed 22 checks and imposed 11 penalties.

The AgriFish Agency made the same observation and identified a number of municipalities that for several years reported very few or no farmers for breaches of the cross-compliance requirements. In May 2012, the AgriFish Agency impressed on the municipal heads of department that the regulation on cross-compliance applies also to their supervision.

51. The Agri/Fish Agency has pointed out to the municipalities the importance of reporting farmers that fail to meet the requirements, emphasizing that inadequate control increases the risk of financial corrections being imposed on Denmark.

52. Rigsrevisionen found that in certain municipalities the number of cross-compliance checks performed was out of proportion to the number of irregularities found. The Danish authorities have decided that most cross-compliance checks should be performed by the local authorities. According to the Ministry of Food, this set-up prevents the ministry from supervising the cross-compliance control performed by the municipalities. In the opinion of Rigsrevisionen, the organisation of cross-compliance control needs to be re-considered to ensure that the overall responsibility for the control rests with a central authority in order to ensure consistent control.

53. The AgriFish Agency checks whether the municipalities comply with the requirements of the Commission for the reporting of checks performed. This means that the Agency checks whether the control reports submitted by the controlling authorities address the EU requirements and are submitted on time. One per cent of the cross-compliance checks performed in the municipalities are re-checked. Rigsrevisionen has in connection with its review of the quality control performed in 2010 established that the focus of the control was mainly on the controlling authorities' compliance with the requirement to submit the control reports no later than two months after the inspection at the farm. The requirements regarding the content of the control include listing of the people present at the inspection, ie was the farmer present, who performed the control, was the farmer notified of the inspection within the prescribed notice period (14 days before the inspection visit, at the earliest). The AgriFish Agency's quality assurance identified errors in approximately 12 per cent of the control reports.

54. Rigsrevisionen welcomes the fact that the AgriFish Agency has reported back to the controlling authorities on areas with potential for improvement and errors found.

The quality assurance does not include a technical assessment of the quality of the control performed. In other parts of the agricultural policy area – the area-based schemes, for instance – rechecks are performed on the basis of the initial irregularities found. Rigsrevisionen is of the opinion that rechecks should also be implemented in connection with cross-compliance control. The purpose would be to assess whether the control performed by the inspectors is professionally sound.

55. In response to Rigsrevisionen's suggestion, the AgriFish Agency has stated that the Ministry of Food is not positioned to supervise the cross-compliance control performed by the local authorities. Through the project *Enhanced control*, however, the Agency has gained more insight into the control exercised by the local authorities, and the Agency will also in the future, at the annual regional meetings, through participation in local knowledge-sharing meetings and – upon agreement – through participation in inspections, guide the activities of the local authorities.

56. The project *Enhanced control* has provided the basis for the launch of a number of projects designed to improve coordination between the local authorities and the AgriFish Agency; most significantly, the selection of farmers to be controlled has been transferred to the AgriFish Agency. This change provides the opportunity to ensure that the sampling of farmers to be controlled takes place in compliance with the EU requirements. The local authorities are required to report their findings in a fixed template designed by the AgriFish Agency. The Agency has also updated the guideline on cross-compliance control developed for the controlling authorities to ensure that it reflects the requirements of the regulations, and at the same time addresses complex issues and cases of doubt. Lastly, the Agency has arranged training courses for the cross-compliance inspectors in the local authorities in order to upgrade their skills and secure documentation of breaches.

57. Rigsrevisionen welcomes these activities, but recommends also the establishment of a formalized collaboration between the individual municipalities, in the form of a control network; several municipalities perform only few cross-compliance checks every year and are therefore not in a position to accumulate sufficient experience with the cross-compliance requirements. The establishment of a control network would provide a good platform for knowledge sharing on complicated cases and interpretation of the cross-compliance requirements.

#### E. Follow-up on activities launched under the project *Enhanced control*

58. Rigsrevisionen has in previous reports to the Danish Public Accounts Committee on the audit of EU funds in Denmark reported on the progress of the project *Enhanced control* that was launched in December 2009 and finished in December 2011. The objective of the project was to strengthen area control in order to ensure correct payment of agricultural aid and reduce the risk of financial corrections being imposed on Denmark by the Commission. 102 activities distributed on seven areas addressed the following issues: IT structure, parcel data and remote sensing, legal quality assurance, coordination of control, physical inspections, cross compliance and project management.

59. A private consultancy firm was commissioned to evaluate the project in the spring 2012. The evaluation addressed the following eight subject areas:

- the land parcel identification system
- adaption of control process (interpretation of the law)
- selection of sample to be checked
- basis of control
- remote sensing
- physical inspections
- cross-compliance control
- structural framework.

60. Rigsrevisionen has reviewed the report elaborated by the consultancy firm and has met with the AgriFish Agency to discuss the closing of the project.

61. Rigsrevisionen is of the opinion that the project has contributed to reducing the risk of future financial corrections being imposed on Denmark. Yet, Rigsrevisionen is also of the opinion that the full effect of the project has not yet been achieved. Rigsrevisionen therefore welcomes the AgriFish Agency's decision to implement an action plan for the areas that need further improvement.

## VI. Financial corrections

In the period 2002-2012, Denmark repaid approximately EUR 134.2 million, which corresponds to 1.2 per cent of the total agricultural subsidies received from the EU. The average financial correction rate for countries that were members of the EU for this entire period, was 1.4 per cent of total subsidies received. Thus Denmark's performance is above the average and Rigsrevisionen therefore concludes that the action taken by the Ministry of Food to reduce the amounts of financial corrections was satisfactory.

62. Rigsrevisionen has examined whether the Ministry of Food has handled recently closed and pending cases concerning financial corrections imposed on Denmark in the agricultural policy area in a satisfactory manner.

The examination addressed the following issues:

- distribution of financial corrections broken down by sector in 2012;
- distribution of financial corrections among the Member States
- financial corrections imposed on Denmark and the Ministry of Food's handling of the cases.

63. The results of the examination were as follows:

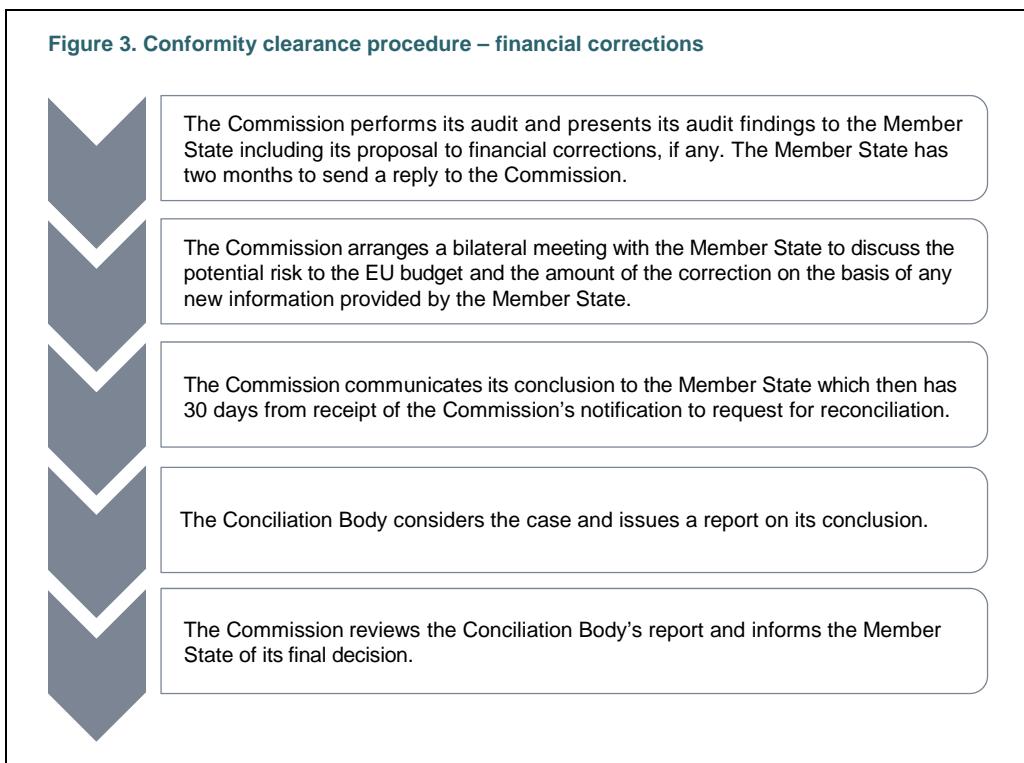
- At the end of August 2012, Denmark was facing 19 financial corrections. Nine of these have since been closed and settled by the Commission. The Ministry of Food sought dialogue with the Commission in all the cases and submitted new data or advocated its interpretation of the requirements of the regulation in order to reduce the amount of the financial corrections. Rigsrevisionen is not entirely satisfied that the Commission has found reasons to impose a total of 19 financial corrections on Denmark, but has noted that the amounts of the financial corrections have decreased in the period 2002-2012.
- The correction involving the largest amount concerns hectare aid and repayment of EUR 101 million received in the period 2002-2004. The Danish authorities have brought the case before the EU Court of Justice with a claim for annulment, alternatively, reduction of the financial correction. On 3 July 2012, the EU Court of Justice made its ruling and upheld the Commission's decision. The Danish authorities have appealed the judgment on the grounds that it is based on inadequate legal reasoning and may be disputed in an appeal. Moreover, the Danish authorities are of the opinion that the appeal may turn out at Denmark's advantage.

## A. Conformity clearance procedure for financial corrections imposed in the agricultural policy area

64. Financial corrections are imposed by the Commission to exclude expenditure that is not in accordance with applicable rules and regulations for EU funding. The Member States thus have an incentive to correct errors and improve their administration on an on-going basis.

65. All financial corrections are imposed on the basis of audits performed by the Commission.

Figure 3 illustrates the procedure for imposing financial corrections from the time when the Commission has completed its audit to the final decision on the amount of the financial correction is made.



66. The Commission detects irregularities both in relation to compliance with eligibility requirements and in relation to the organisation and implementation of internal controls. Complex rules, differing interpretation and implementation of the regulations are the main reasons for exclusions of expenditure.

## B. Financial corrections in the agricultural policy area in EU up to 2012

67. Financial corrections may comprise payments made in up to two fiscal years before the time of the audit. Experience shows that several years elapse from the time when the Commission opens proceedings against a Member State and until the case is finally settled. The cases referred to in this report therefore concern several fiscal years prior to 2011. The financial year for the European agricultural expenditure begins on 16 October and ends on 15 October the following year. This means that this report covers the period leading up to the most recent financial corrections imposed (September 2012). The principles underlying the Commission's calculation of financial corrections appear from box 2.

**BOX 2. THE COMMISSION'S CALCULATION OF FINANCIAL CORRECTIONS**

The Commission determines the amounts of financial corrections or exclusions of expenditure on the basis of an evaluation of three factors: the *nature* and *gravity* of the infringement and the *financial loss* suffered by the EU budget. Whenever possible, a financial correction will be calculated on the basis of the actual financial loss or on the basis of an assessment of the total financial loss suffered by the EU budget. If it is impossible to determine the actual financial loss, a financial correction will be calculated as a flat-rate of the total amount spent by the Member State on the scheme in question. Depending on the nature and gravity of infringements, flat-rate corrections range between two per cent to five per cent, 10 per cent or even 25 per cent of funds received under the respective scheme.

The Commission distinguishes between infringements relating to two types of checks; *key checks* or *ancillary checks*. Key checks are the physical and administrative checks that are required to verify the eligibility of the claim made by the beneficiary. Ancillary checks involve the administrative operations required to process claims correctly and include verifying, for instance, that deadlines are observed and risk analyses performed in accordance with the EU regulations. For instance, a correction of two per cent is imposed if a Member State has failed to improve the application of ancillary checks. A five per cent correction will be imposed if the Member State has implemented all key checks, but not in the number, frequency or depth required. Financial corrections of 10 per cent or 25 per cent may be imposed if key checks are gravely deficient.

**Financial corrections broken down by sector in 2012**

68. Rigsrevisionen has reviewed the Commission's documents on financial corrections that were settled by the Commission in 2012. The financial corrections are in the Commission's documents broken down by country and sector, and so far cases concerning financial corrections totalling approximately EUR 684 million have been settled.

69. In 2012, the majority of the financial corrections were imposed on the wine sector, ie EUR 255 million. The largest corrections were imposed on Spain, Italy and Greece and they were all caused by unauthorised planting of vines.

70. Portugal, Great Britain and Sweden, in combination, accounted for the second-largest amount of correction in 2012 of approximately EUR 188 million. These corrections were imposed due to weaknesses in the land parcel identification systems in the respective Member States. A similar case against Denmark is still pending.

71. In 2012, a total financial correction of approximately EUR 84 million was charged to producer organisations in the fruit and vegetable sector for shortcomings in controls. A correction may be charged also to Denmark in the fruit and vegetables sector; it is currently estimated at EUR 1 – 1.3 million and it is also imposed for shortcomings in controls.

**Total financial corrections broken down by country**

72. The Commission is not publishing statistics on the distribution of financial corrections imposed on the Member States. The Commission decisions have provided the basis for the Ministry of Food's break down of financial corrections imposed on Member States in the period 2002-2012.

73. Figure 4 shows the total amount of financial corrections imposed in the period 2002-2012 on countries that have been members of the EU since 2002.

**Figure 4. Financial corrections imposed on 15 Member States in the period 2002-2012 (EUR millions)**

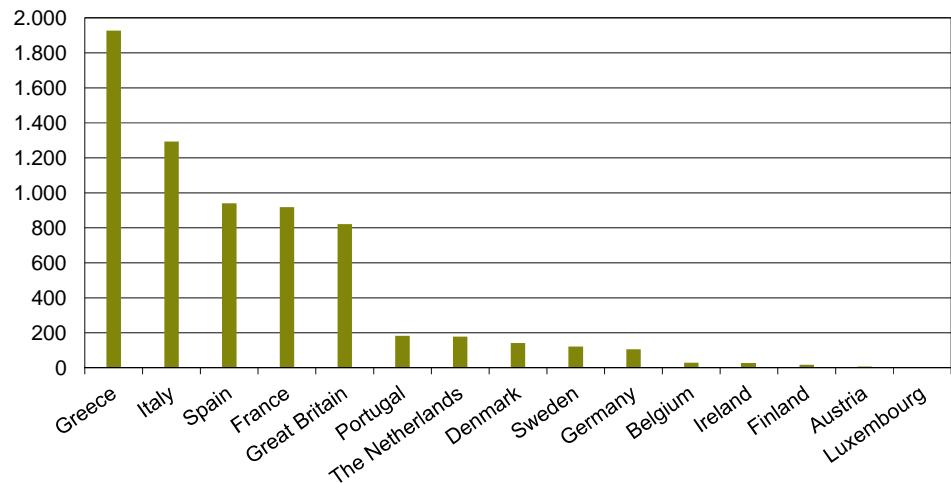


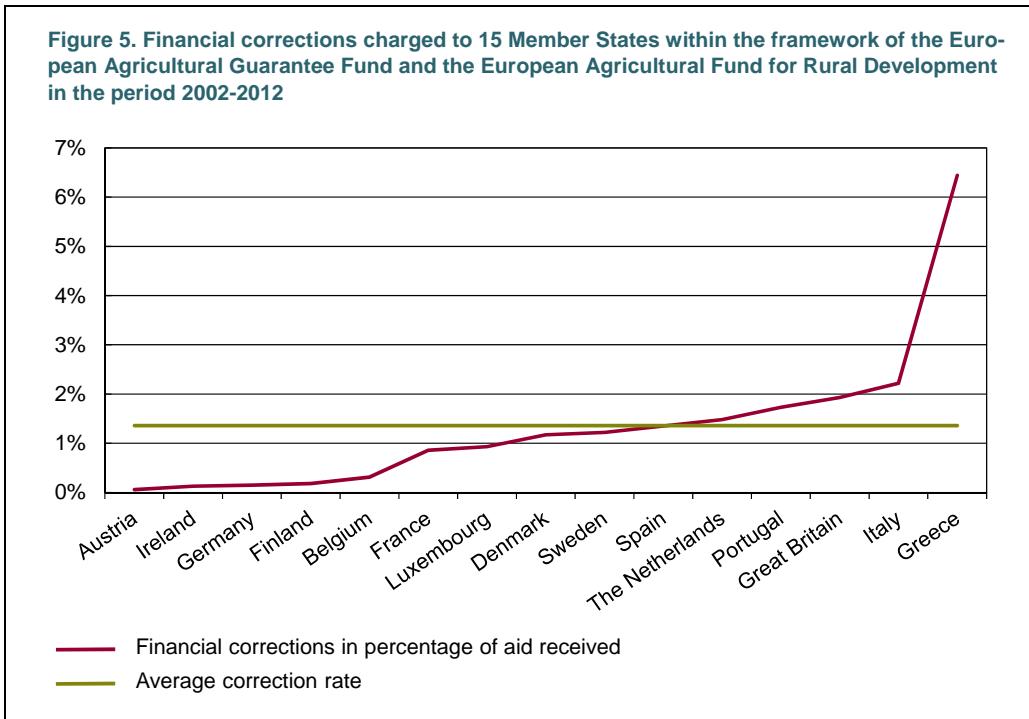
Figure 4 shows that the majority of corrections were charged to Greece, Italy, Spain, France and Great Britain, whereas hardly any corrections were imposed on Finland, Austria and Luxembourg. Denmark is positioned in the middle.

74. In the years 2002-2012, Greece received aid totalling approximately EUR 30 billion of which EUR 1.9 billion was subsequently excluded from EU financing. In 26 out of 29 Commission decisions, corrections were charged to Greece; seven of the 26 Commission decisions concerned financial corrections in excess of EUR 100 million. In comparison, Germany received aid amounting to approximately EUR 70.8 billion, of which approximately EUR 106 million was claimed back. Corrections were imposed on Germany in 23 out of the 29 Commission decisions and the largest correction amounted to approximately EUR 26.4 million.

The way in which corrections are calculated explains the deviations in terms of amounts between the corrections charged to the individual Member States and the fact that largely the same number of corrections have been charged to each Member State; when financial corrections are calculated on the basis of the actual financial loss, they will typically be considerably smaller than when the correction is calculated as a fixed correction – a so-called flat-rate – of the total amount spent by the Member State on the scheme in question. The EUR 100 million correction charged to Denmark is a flat-rate correction.

75. Denmark has received aid amounting to approximately EUR 12.2 billion in the period 2002-2012; approximately EUR 135 million has subsequently been excluded from EU financing. Corrections have been charged to Denmark in 18 out of 29 Commission decisions, with the largest single correction amounting to EUR 100 million.

76. Figure 5 shows financial corrections expressed as a percentage of aid received in the period 2002-2012 for countries that have been members of the EU since 2002. The corrections concern aid received within the framework of the Agricultural Guarantee Fund up to and including May 2012 and prepayments, etc relating to the Rural Development Fund up to 30 June 2012.



It appears from figure 5 that Denmark, in the period 2002-2012, repaid approximately EUR 134 million or 1.2 per cent of aid received. The average financial correction rate for the countries that have been members of the EU in the same period was 1.4 per cent and the percentage repaid by Denmark was thus slightly lower than the EU average.

77. The relative distribution of financial corrections alone does not provide a sound basis for an assessment of the management of EU funds in the individual Member States; the corrections are distributed on the many schemes and vary over time depending on the Commission's cycle of audits in the individual Member States and the time it takes to arrive at a final conformity clearance decision.

### C. Current financial corrections charged to Denmark and the Ministry of Food's handling of the financial corrections

78. The Ministry of Food has informed Rigsrevisionen that as per 27 August 2012, 19 specific financial corrections have been imposed on Denmark; nine of these have been settled by the Commission and 10 are still pending.

79. The Ministry of Food has in all the cases been in dialogue with the Commission and, for instance, submitted new control data or argued for its interpretation of the EU regulations. In a few cases, involving smaller amounts and where the prospects of a satisfactory outcome of reconciliation were considered marginal, the Ministry of Food has accepted the Commission's proposed financial corrections.

### **Area-based schemes**

80. The largest financial correction concerns hectare aid received in the period 2002-2004. On its control visit to Denmark in the autumn 2004 the Commission detected weaknesses in the Danish control of compliance with the regulations concerning land set aside and – to a minor extent – weaknesses in remote-sensing control. The Commission found that the Danish control had approved set-aside land that was either not managed in compliance with the regulations, had been returned to nature, or was unsuited for cultivation and was therefore used for unauthorised purposes.

81. In 1999 – in connection with the implementation of EU's *Agenda 2000* – the regulations were changed in Denmark and specific requirements concerning good agricultural condition were omitted whereas the regulations concerning management and protection of nature on agricultural land were upheld. The Danish authorities emphasised that with the implementation of *Agenda 2000*, protecting the environment took precedence over the requirement to keep the land in good agricultural condition. The Danish authorities therefore concluded that the Danish regulations concerning the management of land set-aside, which did not require mowing of sprouting plants, were in compliance with the EU regulations because the main emphasis was on environmental concerns as, for example, nitrogen-fixing vegetation and the ban on fertilization and crop-spraying.

82. The Commission demanded recovery of EUR 102 million relating to hectare aid provided in 2002, 2003 and 2004. On the basis of the Conciliation Body's report from April 2009, the Commission made its final decision and reduced the financial correction to EUR 101 million.

The Danish authorities brought the case before the EU Court of Justice with a claim for annulment, alternatively, reduction of the financial correction. On 3 July 2012, the EU Court of Justice made its ruling and upheld the Commission's decision. The Danish authorities have appealed the judgment on the grounds that it is based on inadequate legal reasoning and may be disputed in an appeal. Moreover, the Danish authorities are of the opinion that the appeal may turn out at Denmark's advantage. The Danish authorities are founding the appeal mainly on the grounds of the judgment that concern the significance of the Commission's interpretation of the issue of vegetation on set-aside land, the Court's interpretation of the land management requirement and whether the fields could be used for agricultural production.

### **Schemes that are not area-based**

83. 12 of the 19 cases are related to schemes that are not area-based. Seven of these have been settled and five are still pending. The largest correction among the settled cases concerns exclusion of expenditure totalling approximately EUR 0.3 million. Two of the cases were dropped following correspondence between the Commission and the Ministry of Food. The five pending cases concern, for instance, operation of producer organisations, eligible expenditure for demonstration projects and investment schemes within the framework of the Rural Development Fund. The risk of the financial corrections being implemented has been assessed in four of the cases.

84. All the cases that relate to area-based schemes and schemes that are not area based involve key controls and ancillary controls. The EU regulations are complex and continuously changing and therefore constantly raising questions of interpretation. Rigsrevisionen has established that disagreement over the interpretation of the EU regulations between the Commission and the Danish authorities is the cause of many of the cases. Rigsrevisionen is satisfied that the Danish authorities are pursuing on-going dialogue with the Commission in an effort to provide clarity on the interpretation of the EU regulations.

## VII. The effect of EU funds provided to the island of Bornholm

Outcome targets on national and regional/local level have only to some extent been defined for four selected subsidy schemes established within the framework of the Regional Fund, the Rural Fund and the Fisheries Fund. Rigsrevisionen recommends that the Ministry of Business and Growth and the Ministry of Housing, Urban and Rural Affairs should make a greater and more coordinated effort to define outcome targets and examine the effects of EU-funded projects established within the various subsidy schemes.

85. Rigsrevisionen has performed a cross-sectoral audit of subsidies provided through the Regional Fund, the Rural Development Fund and the Fisheries Fund to projects at Bornholm.

86. The audit included examination of the following factors:

- objectives of the funds;
- outcome targets;
- importance of the outcome targets for the recommendation of projects;
- performance measurement;
- coordination of performance measurement on national and regional/local level;
- collaboration among the funds.

The audit included 44 projects under four different subsidy schemes (one under the Regional Fund, two under the Rural Development Fund and one under the Fisheries fund). Nine of the projects were inspected on-the-spot.

87. The Regional Fund is administered by the Danish Business Agency under the Ministry of Business and Growth and includes only one subsidy scheme.

The Rural Development Fund and the Fisheries Fund, on the other hand, include several subsidy schemes, and Rigsrevisionen sampled three schemes for its audit. The Ministry of Housing, Urban and Rural Affairs is responsible for the organisation and administration of the policies governing the three schemes, whereas processing of applications, payment of subsidies, etc is carried out by the AgriFish Agency on behalf of the Ministry of Food.

88. The selection of eligible projects under all four subsidy schemes has been delegated to the regional or local level and Rigsrevisionen has therefore decided to restrict its audit to a specific geographical area, namely the island of Bornholm. The regional growth forums are responsible for selecting Regional Fund projects, whereas the Local Action Groups (LAGs) are in charge of selecting Rural Development Fund projects and the Fisheries Local Action Groups (FLAGS) select projects within the framework of the Fisheries Fund, cf box 3. At Bornholm, the latter two actions groups have been merged.

#### BOX 3. LOCAL ACTION GROUPS

The local action groups are authorized by the Ministry of Housing, Urban and Rural Affairs to exert direct influence on the development in the rural areas. The people who live and work in the rural areas should contribute to preserving the dynamics of their local area. Local insight provides the basis for an assessment of the projects' ability to contribute to creating attractive offers and jobs, and increase the quality of life in the rural areas.

Local action groups are active around the country and striving to create life and jobs in rural and fisheries areas with support from the Ministry of Food and EU. In Denmark there are

- 39 local action groups under the Rural Development Programme;
- 6 local action groups under the Fisheries Development Programme;
- 12 local actions groups working with development of rural and fisheries areas.

Figure 6 shows the relationship between the funds, the government agencies and the regional/local level.

**Figure 6. Organisation**



Growth Forum Bornholm and LAG-Bornholm recommend projects for funding to the Danish Business Agency and the AgriFish Agency. The agencies perform a compliance check of the projects and then proceed to either awarding funding or rejecting applications. Funding covers only part of the eligible expenditure of the selected projects.

89. Rigsrevisionen's examination of the effect of the EU funds provided to Bornholm showed the following:

- Rigsrevisionen noted that outcome targets had not been defined for the effect of the programme on employment. Moreover, the three underlying outcome targets set for the programme period in relation to innovation, the application of information and communications technology as well as entrepreneurship, were very broad and vague. Rigsrevisionen finds that the Danish authorities should set outcome targets for the overall expected effect on employment. More concrete and clear outcome targets should also be defined for the sub-objectives set for the programme period, and guidance material should be developed on the interpretation of the performance requirements. Rigsrevisionen also finds that the Danish Business Agency and the regional growth forums should focus more on documenting effect.

- Rigsrevisionen finds that the Ministry of Housing, Urban and Rural Affairs should consider how outcome targets for the various subsidy schemes can be defined and performance measured. Furthermore, coordination of requirements determined centrally and requirements defined at local level should be improved.
- Finally, Rigsrevisionen sees a need for improved coordination of performance measurement activities between the Danish Business Agency and the Bornholm Growth Forum. Action is required in relation to the current practice, where both the Danish Business Agency and the Bornholm Growth Forum follow up on performance, and in relation to changes and projects implemented by the Danish Business Agency and the Bornholm Growth Forum, respectively. A coordinated effort is also required in respect of the schemes under the Rural Development Programme and the Danish Fisheries Development Programme to ensure that the effects of the programmes are adequately followed up by the Ministry of Housing, Urban and Rural Affairs and the LAGs.

#### A. The objectives of the funds

90. The framework governing the two subsidy schemes – *Attractive living conditions in the rural areas* and *Creating new jobs in the rural areas* – is set out in Council Regulation no. 1698/2005 of 20 September 2005 on support for rural development by the European Agricultural Fund for Rural Development in the period 2007-2013. This regulation has been transposed into Danish legislation in act no. 316 of 31 March 2007 on development on the rural areas.

According to section 1 of the act its objective is to contribute to sustainable development of the rural areas with growth based on sustainable use of resources and local participation contributing to creating attractive living conditions and local jobs. Statutory instruments on the two subsidy schemes are available.

91. Two statutory instruments set out the framework for the Danish subsidy scheme concerning fisheries; Council Regulation no. 1198/2006 of 27 July 2006 on the Fisheries Fund and Commission Regulation no. 498/2007 of 26 March 2007 on the rules for the implementation of the regulation. The Act on Fishery Development and Aquaculture (Act no. 1552 of 20 December 2006) was issued in accordance with the two Commission Regulations. Section 1 of the act states its objective, ie to set out the framework for optimal sustainable exploitation of Danish fishery and aquaculture whilst ensuring adherence to the objectives concerning sustainability and regional development. A statutory instrument on the subsidy scheme is available.

92. Rigsrevisionen has reviewed the above-mentioned regulations, acts and statutory instruments governing the activities of the Rural Development Fund and the Fisheries Fund and found that they have been implemented in national Danish legislation in compliance with the objectives determined by the EU.

93. Rigsrevisionen has also reviewed LAG-Bornholm's development strategy and selected projects; the strategy is considered to be in compliance with the statutory instruments and grants have been awarded in compliance with the development strategy and the statutory instruments.

94. Rigsrevisionen is of the opinion that the objectives of the Regional Fund fall within the framework determined by the EU regulations. The audit included a review of applications and how they were related to the objectives of the Regional Fund and the business development strategies of the regional growth forums. Rigsrevisionen found that Growth Forum Bornholm had ensured that the applications were eligible for funding under the Regional Fund and underpinned the priorities of the business development strategy.

## B. Outcome targets

### The Regional Fund

95. Denmark has for many years awarded funds from the Regional Fund to various projects and added up, the amounts have been significant. The expenditure in 2011 for EU grants amounted to more than EUR 81 million. The overarching objective of the Regional Fund is to ensure that subsidy funds contribute to strengthening regional competitiveness and employment in Denmark.

96. On national level, the Ministry of Business and Growth has defined the following outcome targets for the programme period:

- 1,000 businesses have become more innovative;
- 200 businesses have increased their use of information and communication technology;
- 900 new entrepreneurs have entered the market.

97. On regional level, the Bornholm Growth Forum operates with 4-year business development strategies. The current strategy is focused on Bornholm as a business island, education island, adventure island and green test island. A number of strategic outcome targets have been defined for each of these areas; adding value, increasing the number of innovative businesses and increasing the survival rate of new businesses. Funds from the European Regional Fund in combination with regional development funds, which totalled EUR 6.7 million in the programme period 2007-2011, provide the financial basis for achievement of these targets.

98. The Danish Business Agency as well as the Bornholm Growth Forum collects information on estimated and actual effect of the activities. The Bornholm Growth Forum collects information twice a year through email or telephone contact, whereas the Danish Business Agency sends out a form requesting data on effects. The data collected by the Danish Business Agency is submitted to the Commission.

99. The Danish Business Agency collects data from the individual businesses on the extent to which the subsidised projects have become more innovative, whether they have increased their use of information and communication technology and whether the number of entrepreneurs in the market has increased.

100. Rigsrevisionen notes that the current targets – and the questions addressed to the businesses – are vague and too broadly formulated. The performance measurement conducted by the Bornholm Growth Forum is based on the replies provided by the businesses and the quality of the data may therefore be inadequate. The same applies to the data on growth in employment and turnover collected by the Bornholm Growth Forum.

101. Taking into consideration the amount of funds that are provided within the framework of the Regional Fund, Rigsrevisionen is of the opinion that the Danish Business Agency should supplement the information on the overall objective with information on the expected effect on the rate of employment. Moreover, the Agency should, for instance, three to five years after completion of the projects, examine the effect on national and regional/local level of the activities made to increase the employment rate and turnover.

The Danish Business Agency has informed Rigsrevisionen that this programme does not include explicit targets for number of new jobs created (in addition to the number of new businesses established) because it was set up when employment in Denmark was almost full. The primary objective of the programme was therefore to increase the productivity of the Danish business community. This should be achieved by focusing on the sources of growth that OECD, among others, has identified as essential for developing productivity, ie innovation, application of new technology, entrepreneurship and education, and which were also key elements in the growth strategies that were laid down by the then (and current) government.

Taking into consideration the current market conditions, the Danish Business Agency considers it appropriate to include job creation as an explicit target in the coming programming period 2014-2020. The Agency is also planning to tighten up the project requirements to documentation of effects, including descriptions of a clear and logical connection between the activities, output and effect of the projects. Emphasis will be on providing clearer links between the overarching programme objectives and the goals set for the individual projects. Moreover, it is the intention to measure the effect of all projects against data from Statistics Denmark, if possible.

102. Rigsrevisionen finds that the Ministry of Business and Growth should define more concrete and clear outcome targets for the sub-objectives set for the programme period, and guidance material should be developed on the interpretation of the performance requirements. This would make the outcome targets and collected information more useful for the management of the projects. Rigsrevisionen is also of the opinion that the Bornholm Growth Forum would be better positioned to validate the information if documentation of effects achieved concerning growth in employment and turnover could be provided.

103. The Danish Business Agency has informed Rigsrevisionen that collaboration has been initiated with Statistics Denmark on performance measuring; businesses receiving aid from the Social Fund are benchmarked against a similar reference group that is not receiving aid from the EU. This collaboration will facilitate evaluation of the effect of the subsidised projects in a long-term perspective. No additional administrative burden in the form of more reports will be imposed on the businesses, because existing data will provide the basis for the benchmarking.

104. Rigsrevisionen agrees that reference groups can be used for benchmarking the development of subsidised businesses against businesses that are not subsidized and thus separate the effect of the aid from other factors. However, providing a basis for comparison may be difficult, because the characteristics of the market conditions in which the businesses operate needs to be identical.

105. The Danish Business Agency has also stated that the above-mentioned benchmarking method is not applied only to Social Fund projects, but also to Regional Fund projects.

### **The Rural Development Fund and the Fisheries Fund**

106. The AgriFish Agency has defined an overall target for a number of schemes under the Rural Development Programme; the projects should lead to the creation of in total 360 new jobs.

107. On local level, LAG-Bornholm is working with a development strategy revolving around eight so-called beacons like, for instance; *Arts and crafts island*, *Local development and community participation* and *Regional quality food products*. Each beacon consists of a number of projects that support local development. The strategic objective calls for the implementation of at least one major process development project within each theme in the programming period. The development strategy is also focused on ensuring that the development work is based on networking and collaboration and includes local community participation.

108. As a result of the width and content of the strategy, many and very diverse objectives have been set for the projects; most of them are very broadly formulated, but some are well-defined, quantitative performance targets and objectives.

109. In 2011, EU subsidies of EUR 13.9 million were earmarked for two schemes under the Regional Development Fund; *Attractive living conditions in the rural areas* and *Creating new jobs in the rural areas*. Taking into consideration the amount of funds, Rigsrevisionen recommends that the Ministry of Housing, Urban and Rural Affairs in collaboration with the AgriFish Agency should consider how outcome targets can be defined for each scheme and how the effect can be measured. These considerations should include also interaction between centrally determined requirements and requirements defined on local LAG level.

110. In respect to measuring effect, the ministry and AgriFish Agency should take into consideration the very same factors that are mentioned in connection with the Regional Development Fund.

111. Rigsrevisionen appreciates that the characteristics of the schemes are such that it may be difficult to define outcome targets that are relevant for all LAGs.

112. More than 50 LAGs – with each their development strategy – have been established on national level. The strategies of these 50 LAGs differ considerably among themselves, reflecting the very broad objectives defined for the funds. It has been determined by law – and this applies to all three schemes – that the creation of attractive living conditions and local jobs must be founded on local community participation. To secure local community participation, all individuals aged 15 who reside in the community can register as members of the local action groups that are approving the development strategy prepared by the board.

113. The subsidy funds can be used to support and develop a wide variety of activities, as it appears from box 4.

**BOX 4. FOCUS AREAS OF THE SCHEMES ATTRACTIVE LIVING CONDITIONS IN THE RURAL AREAS AND CREATION OF NEW JOBS IN THE RURAL AREAS**

- Promotion of micro-enterprises in the non-agricultural sector
- Rural tourism
- Diversification into non-agricultural activities
- Basic services
- Small and medium-sized food companies
- Competence development and information campaigns to promote implementation of local development strategies
- Village renewal
- Natural and cultural heritage.

### C. The significance of outcome targets for recommendation of projects

#### The Regional Fund

114. To qualify for funding, the projects must meet the eligibility requirements of the Regional Fund and the priorities of the business development strategy, and contribute to achieving the outcome targets.

115. When selecting projects, the Bornholm Growth Forum is required to attach special importance to the anticipated effect of the projects. Rigsrevisionen found that Bornholm Growth Forum had on several occasions failed to perform an independent assessment of the effects projected by the applicant.

116. The Bornholm Growth Forum has informed Rigsrevisionen that if the projected effects seem unrealistic, the applicants will be asked to provide further information. However, it should be taken into considerations that it may be difficult to separate the direct effects of projects from the effects of external factors.

117. Rigsrevisionen finds that when the eligibility of a project depends on the validity of the projections of effect, the Bornholm Growth Forum should request additional information on the basis for the projections including underlying prerequisites. Thus the Bornholm Growth Forum would get an opportunity to assess the effect of relevant external factors.

#### **The Rural Fund and the Fisheries Fund**

118. To become eligible for support, a project must contribute to achieving the objectives of LAG- Bornholm's development strategy. Moreover, applicants must have an anticipation that their projects will contribute to improvements in minimum one centrally defined area. For instance, projects should lead to the introduction of new or improved services, create new jobs or pull new residents or tourists to the region.

119. The audit showed that outcome targets had been defined for the projects as required, and the project closing reports summarised how the projects had supported the development strategy of LAG-Bornholm, and whether they had met the objectives of contributing to improvements in minimum one centrally defined area. The objectives in terms of, for instance, the creation of a certain number of new jobs/new residents/tourists were, however, not fully achieved.

The Ministry of Housing, Urban and Rural Affairs has informed Rigsrevisionen that it also checks the effect of the projects three to five years after they are closed. Pursuant to Commission Regulation no. 65/2011, article 29, ex-post checks are carried out on investment operations to ensure compliance with the commitments pursuant to Article 72(1) of Regulation (EC) no. 1698/2005 on the durability of investment-related operations, or as detailed in the rural development programme.

#### **D. Project performance measurement**

##### **The Regional Fund**

120. It turned out that realistic and measurable targets for employment and turnover had been defined for only one of the sampled projects. The targets set for the other projects were not as well defined and the closing reports focused mainly on whether the projects had been implemented and less on the immediate effects achieved through the projects.

121. According to available information, six of the projects had increased the employment rate by the equivalent of two man-years and one project had increased the employment rate beyond that. These projects were typically targeting small businesses that were affected by the financial crisis, and according to the management of the businesses, the aid had contributed to increased growth.

122. Rigsrevisionen considers it essential that beneficiaries define measurable outcome targets for their projects.

The Danish Business Agency considers it necessary to continue the efforts to ensure measurement of the effects of the structural fund projects, and has therefore in recent years – in collaboration with the secretariats of the regional growth forums – implemented various measures to improve effect measurement and evaluation; evaluation guidance for structural fund projects was developed in 2010; a new application form with considerably more focus on effect was implemented early in 2011; evaluation courses directed at case workers were held in 2011. Finally, the six regional growth forums and the Danish Business Agency have in collaboration with Statistics Denmark worked on several projects, which have all been benchmarked against registered data and subjected to advanced performance measurement methods, including, among other things, the projects' effect on job creation.

Since autumn 2010, the Danish Business Agency has collected CVR and CPR numbers (central business register numbers and personal identity numbers) on the businesses and individuals that are affected by the structural fund projects. This data and data from Statistics Denmark have been pooled and used for measuring performance. The Agency has stated its intent to use the CVR and CPR numbers to monitor the development of businesses and individuals beyond the project period, as the effect of many of the project will probably not show till after the end of the programming period.

### The Rural Development Programme

123. The implementation of – and awarding of grants to – the three schemes; *Attractive living conditions in the rural areas* and *Creating new jobs in the rural areas* and *Sustainable development of fisheries areas* is founded on the development strategies that are worked out by the LAGs. According to the time schedule, the LAGs must start work on the development strategies for the coming programming period that starts in 2014 very soon; it is therefore essential that the LAGs are able to draw on lessons learnt from the assessment of the preceding programming period and in particular effects achieved.

124. Rigsrevisionen finds that the individual LAGs – at the end of the programming period – should perform a professional assessment of their development strategies.

### E. National and regional/local level coordination

125. Rigsrevisionen established lack of coordination between the Danish Business Agency and the Bornholm Growth Forum regarding performance measurement. This observation applies to the current set-up where both the Danish Business Agency and the Bornholm Growth Forum follow up on project development, but is also evident in relation to various changes and activities launched by the Danish Business Agency and the Bornholm Growth Forum, respectively. Rigsrevisionen assumes that also other growth forums could benefit from increasing the level of coordination.

126. The Danish Business Agency agrees that benchmarking the performance of projects against two different measuring systems is ineffective. The Agency is working closely with the regional growth forums on the performance measurement system in order to streamline the measurement methods across the regions and the central administrative authorities. The Bornholm Growth Forum partakes in this work. In connection with the structural fund programmes for 2014-2020, the Agency will seek to ensure that no projects are required to report on separate effects to the regions.

127. As regards coordination in relation to changes and activities, the Agency has informed Rigsrevisionen that a new application form was implemented early in 2011 which required applicants to indicate the success criteria of the activities, output and effect. The organisation of the administrative approach in the next programming period will take into consideration the experience gained with this new application form, as will the results of a pilot project that the Agency and the six regional growth forums have decided to implement; the Agency and the Bornholm Growth Forum are to set up kick-off meetings with businesses that have applied for grants of EUR 134,000 or more from the Regional Fund in order to guide them in defining concrete targets, including performance targets against which the performance of the project can subsequently be measured.

128. The Bornholm Growth Forum has also stated that it intends to work further on a paper on the development of a performance measurement policy – a project that was started in June 2012. In the paper, the Bornholm Growth Forum proposes a process that is started at receipt of the project application, continues for the life of the project and beyond when progress is assessed and measured. The purpose of this process is – in addition to ensuring assessment of the individual projects – to measure the effect of the development strategy laid down by the Bornholm Growth Forum.

129. The fact that the Danish Business Agency and the Bornholm Growth Forum are focused on businesses and their achievement of the targets set for their projects is welcomed by Rigsrevisionen. Yet, Rigsrevisionen also considers it essential that changes and activities are coordinated more firmly and thus supporting the efforts made to define outcome targets and conduct the relevant outcome studies.

130. The Danish Business Agency has announced that coordination will be handled by representatives of the regional growth forums and the Agency in an assessment network.

131. Rigsrevisionen finds that also the Ministry of Housing, Urban and Rural Affairs and the local LAGs should be involved in the coordination efforts to ensure adequate follow up on the outcome of the Rural Development Programme and the Fisheries Development Programme.

#### F. Cooperation between the funds at Bornholm

132. The overarching objective of the Regional Fund is to ensure that subsidy funds contribute to strengthening regional competitiveness and employment in Denmark. The EU funds operate with programming period of seven years and the current period runs from 2007 to 2013. From 2007 to 2011 inclusive, the Bornholm Growth Forum had a budget of approximately EUR 5 million.

133. The three selected LAG schemes; *Attractive living conditions in the rural areas*, *Creating new jobs in the rural areas* and *Sustainable development of fisheries areas* operated on a total budget of approximately EUR 2.7 million from 2007 to 2011 inclusive.

134. The Head of Secretariat of the Bornholm Growth Forum, the LAG coordinator and the chairman of LAG Bornholm have informed Rigsrevisionen that the Bornholm Growth Forum and LAG Bornholm collaborate to ensure coordination of the use of EU funds awarded through the Regional Fund, the Rural Development Fund and the Fisheries Development Fund.

As regards commercial projects, LAG Bornholm supports the smaller commercial and entrepreneurial environment at Bornholm and as a rule it does not award grants to individual businesses whereas the Bornholm Growth Forum handles large projects and awards grants to individual businesses. The coordination is secured through mutual representation; the Bornholm Growth Forum is represented on the board of LAG-Bornholm, and the LAG coordinator is a member of the Bornholm Growth Forum team that is responsible for recommending projects for funding.

135. The three funds have on average just under EUR 1.6 million at their disposal annually for distribution to the four schemes at Bornholm. The Bornholm Growth Forum and LAG-Bornholm have adopted a policy for awarding grants that ensures that funded projects complement each other.

136. Taking into consideration the amount of funds and the grant awarding policy, Rigsrevisionen finds that the cooperation between the Bornholm Growth Forum and LAG-Bornholm has been appropriately organised.

## VIII. EU expenditure

In 2011, EU expenditure totalled approximately EUR 2.5 billion of which customs duties and agricultural fees and levies accounted for approximately EUR 0.3 billion. Rigsrevisionen is of the opinion that the EU expenditure is generally administered in a satisfactory manner; yet the Danish tax authorities need to reduce the error rate in the customs clearance declarations.

### A. Own resources

137. Denmark and the other Member States transfer three types of own resources to the budget of the EU:

- Traditional resources, ie customs duties and agricultural duties and levies;
- VAT-based resources in accordance with the joint basis for calculation of value added tax;
- GNI-based resources in accordance with the joint basis for calculation of gross national income.

The internal auditors of the Ministry of Taxation have audited SKAT's (Danish tax authorities) settlement of Denmark's two single largest contributions to the budget of the EU in 2011; VAT-based resources of EUR 403 million and GNI-based resources of EUR 1,717 million.

138. The audit included a review of business procedures and internal controls and whether own resources had been settled in compliance with the EU's material and formal regulations and were documented and correctly recognized in SKAT's financial statement. The audit also included random checks of booking of VAT- and GNI-based resources in order to determine whether bookings were made in compliance with internal procedures. The internal auditors of the Ministry of Taxation concluded that SKAT had established procedures to ensure that transfers were correctly authorised and all payments recorded.

The internal auditors of the Ministry of Taxation also concluded that the settlement of EU's own resources relating to the tax year 2011 was satisfactory and their audit did not give rise to any qualifications. Rigsrevisionen therefore focused on the administration of customs duties and agricultural duties and levies, which has previously proved to be inadequate.

### B. Danish customs duties

139. On behalf of the EU, SKAT collects import duties on goods brought into the EU. The companies that import the goods – or shipping agents representing such companies – submit the data required for customs clearance to SKAT via SKAT's own online solution. The electronic customs clearance fulfils the business community's need for fast and flexible customs clearance routines.

140. For several years, audits and SKAT's own reviews have disclosed many errors in the customs declarations. The errors are caused by inadequate quality of the data reported by the companies. The errors are minor in terms of amounts as some companies settle too much and others too little.

141. SKAT has in recent years launched various projects to improve the quality of the customs declarations. In a memorandum of 25 February 2011 on the audit of EU funds in Denmark in 2009, the auditor general announced that he intended to follow these projects closely.

142. Rigsrevisionen's review of the projects, which was performed together with the internal auditors of the Ministry of Taxation, showed the following:

- The results of previous reviews had shown that many shipping agents, including courier companies, often made mistakes when filling out the customs declarations. SKAT therefore launched the project *Quality of customs clearance performed by shipping agents*. As part of the project, SKAT decided to approach the relevant trade organisations to hear their views on the causes of the many errors. According to SKAT this approach proved worthwhile and resulted in a good dialogue on which action to take to make the business community focus more on the quality of customs clearance. Rigsrevisionen welcomes this initiative by SKAT.
- The success criteria of the project call for a reduction of the error rate of 20 per cent. Rigsrevisionen will follow the progress of the project in this respect.
- In connection with both the project on the quality of customs clearance performed by shipping agents and the so-called *Guidance project – time waster project*, SKAT asked the businesses and shipping agents to provide concrete proposals for improvements and simplifications of the customs clearance procedures as determined by SKAT and the customs clearance system as such. SKAT is currently reviewing the many suggestions received. Rigsrevisionen welcomes these initiatives by SKAT and will monitor the effect of the project closely.
- MoFia is a national project involving sample checks of customs declarations before release of goods. MoFia set out as a time-limited project, but has since 1 January 2011 become a permanent operational activity. SKAT has informed Rigsrevisionen that it has now implemented the quality control concept for MoFia's sample checks, which Rigsrevisionen finds satisfactory.

143. SKAT has announced that it will perform sample-based checks of customs declarations, after the goods have been imported into Denmark (post events), in the period September 2012 to May 2013. The purpose of this control that is referred to as *Customs compliance* and is a repeat of a previous activity, is to assess the extent to which businesses comply with the rules. Rigsrevisionen welcomes SKAT's efforts to assess the effect of these initiatives on the quality of customs clearance.

144. Overall, Rigsrevisionen welcomes SKAT's targeted efforts to improve the quality of customs clearance and ensure correct collection of customs. Yet, SKAT needs to continue its efforts to reduce the number of errors in customs declarations.

Rigsrevisionen, 7 November 2012

Lone Strøm

/Michala Krakauer

## Appendix 1. Glossary

Area control	Area control includes administrative control as well as physical inspections. The objective of the control is to ensure compliance with the eligibility terms.
Business development strategy	This strategy describes the activities and projects pursued by the Local Growth Forums and serves as the basis for the Regional Growth Forums' management of these activities and projects.
Conciliation Body	The EU Conciliation Body has five members who are independent experts recruited among the Member States. The Conciliation Body is reconciling budgetary differences between the Commission and Member States. The conclusions of the Conciliation Body are published in a report.
Controlling authority	The cross-compliance control is exercised by the municipalities and various government authorities like, for instance the Danish Plant Directorate and the Danish Forest and Nature Agency.
Cross compliance	<p>The farmer must comply with a number of national requirements concerning the environment, health, animal welfare, and the maintenance of all agricultural land in good agricultural and environmental condition to be eligible to receive single payments and direct aid for protein and energy crops, starch potatoes, and premiums for male animals and ewe (ie support financed by the European Agricultural Guarantee Fund). The cross-compliance requirements are also applying to direct aid received under the livestock or arable area subsidy schemes that are financed by the European Agricultural Fund for Rural Development.</p> <p>This cohesion between payment of subsidies and compliance with requirements is called cross compliance.</p>
Customs compliance	Project designed to assess the extent to which businesses comply with the rules.
Development strategy for LAGs	Strategy describing the activities and projects that the LAG has prioritised and is supporting.
Direct agricultural aid	Direct agricultural aid includes the Single Payment Scheme, premiums for protein and energy crops, starch potatoes, ewe and slaughter of male animals (bulls and steers).
Financial correction	If a Member State is not complying with the EU rules, the European Commission may refuse to reimburse project expenditure.
Eligible/not eligible areas	Land used for agricultural activities (including grazing) is eligible for support under the Single Payment Scheme. The following areas are not eligible for support: fire lanes, property lines, windbreakers, natural areas like heather, areas overgrown with rush and other wetland plants, and areas that are not primarily used for agricultural activities or are planted with Christmas trees.
Enhanced Control Project	The objective of the project was to strengthen the area control. The project included 102 activities distributed on seven areas, which addressed the following issues: IT structure, parcel data and remote sensing, legal quality assurance, coordination of control, physical inspections, cross compliance and project management.
EU funds	The EU funds contributing EU revenue to Denmark are: the <u>European Agricultural Guarantee Fund</u> , the <u>European Agricultural Fund for Rural Development</u> , the European Fisheries Fund, the European Social Fund, and the European Regional Fund. The EU funds are part of the EU budget and are not funds in the traditional legal sense of the word.
EU revenue and expenditure	Revenue, which Denmark receives from the EU, is referred to as EU revenue, whereas the Danish contributions to the EU are referred to as EU expenditure.

Note: Words underlined are explained under another entry in the glossary.

The European Agricultural Fund for Rural Development	EU fund financing support granted under the Rural Development Programme.
The European Agricultural Guarantee Fund	EU fund financing <u>direct agricultural aid</u> .
The European Fisheries Fund	The EU fund financing projects under the Fisheries Development Programme.
Financial correction	The Commission generally applies a flat-rate penalty when project expenditure has been disqualified from reimbursement, which means that EU funding of the respective programme will be reduced by a fixed percentage.
Good agricultural and environmental condition	Farmers must meet the requirements for good agricultural and environmental condition of his land to be eligible for support; uncultivated lands must be mown at least once every second year in the period 1 July to 15 September, and permanent pastures must be mown once a year in the same period.
Incomplete declarations	Customs declarations that the company has started on, but not completed.
Land Parcel Identification System (LPIS)	The LPIS contains data on the size of individual land parcels.
Local Action Groups (LAGs)	Local Action Groups are made up of representatives from the local community and are meant to promote the development of the rural areas and fisheries areas. Anyone may join the group and thus make a difference and contribute to speeding up the development of commercial life, creating new jobs and good living conditions in the area. The members of the LAGs are also responsible for the allocation of the funds available to the group. Funds should be awarded to projects that contribute to achievement of the development strategy laid down for the action group.
MoFia	Project contributing to the implementation of daily control of and follow-up on customs declarations in order to reduce the error rate and eliminate other deficiencies before the declarations are approved and the good released.
Ortho imagery	The AgriFish Agency has developed digital field maps on the basis of aerial photos that have been geometrically corrected to ensure that the scale of distances, areas, etc. are as accurate as ordinary maps. These photos are referred to as ortho imagery.
"Other control"	Performed when the <u>controlling authority</u> during an inspection on-the-spot, that has been arranged for other purposes, comes across violations of the cross-compliance requirements.
Payment entitlements	To be eligible for direct aid under the Single Payment Scheme, a farmer requires payment entitlements. Entitlements for agricultural and non agricultural land were allotted in 2005. In 2008, permanent fruit and vegetables crops and nursery crops also became entitled to direct aid and entitlements were allotted accordingly. The value of the payment entitlements is included in the calculation of the size of subsidy.
Regional growth forum	Project applications for subsidies from the European Social Fund and the European Regional Fund are processed by the regional growth forums that are composed of regional politicians and representatives of the business community, knowledge and educational institutions and the parties in the labour market.
Remote sensing	Measurement of agricultural land performed by satellite.

Note: Words underlined are explained under another entry in the glossary.

Set-aside land	As a condition of receiving hectare aid for areas with corn, oil seeds and protein crops, the farmers are required to set aside part of their land to limit overproduction of corn and other produce.
Single payments	Aid paid to farmers under the <u>European Agricultural Guarantee Fund</u> .
Structural funds	The European Social fund and the European Regional Fund.

Note: Words underlined are explained under another entry in the glossary.