Reports of Cases

OPINION OF ADVOCATE GENERAL
CRUZ VILLALÓN
delivered on 1 April 2014 [1]

Joined Cases C-549/12 P and C-54/13 P

Federal Republic of Germany
v

Commission

(Appeals — European Regional Development Fund (ERDF) — Operational programme falling within Objective 1 (1994-1999), concerning the Land Thüringen and Berlin (East) (Germany) — Reduction of the financial assistance originally granted — Extrapolation method — Net financial corrections — Regulation (EEC) No 2052/88) — Regulation (EEC) No 4253/88)

1. In the context of two appeals against two judgments of the General Court dismissing actions for annulment brought by the Federal Republic of Germany against two Commission decisions reducing certain assistance from the European Regional Development Fund (ERDF), the question has arisen as to whether the case-law laid down in relation to other structural funds on the matter of the reduction of financial assistance is applicable to the present case. [2] In particular, the question arises as to whether, in the case of the ERDF, administrative errors of the national authorities constitute an 'irregularity' within the meaning of Article 24(2) of Regulation (EEC) No 4253/88, [3] and, above all, whether the Commission is entitled to make financial corrections using the extrapolation method.

I – **Legislative framework**

2. Council Regulation (EEC) No 2052/88 of 24 June 1988 on the tasks of the Structural Funds and their effectiveness and on coordination of their activities between themselves and with the operations of the European Investment Bank and the other existing financial instruments [4] lays down the regulatory framework for the ERDF, which is intended to correct the main regional imbalances in the Union.

3. Under the heading 'Financial control', Article 23 of Regulation No 4253/88 laying down provisions for implementing Regulation No 2052/88 provides as follows:

'1. In order to guarantee successful completion of operations carried out by public or private promoters, Member States shall take the necessary measures:

1 — Original language: Spanish.

2 — For example, Case C-55/91 *Italy* v *Commission* [1993] ECR I-4813; Case C-436/98 *HMIL* [2000] ECR I-10555; and Case C-344/01 *Germany* v *Commission* [2004] ECR I-2081.

3 — **Council Regulation of 19 December 1988, laying down provisions for implementing** Regulation (EEC) No 2052/88 **as regards coordination of the activities of the different Structural Funds between themselves and with the operations of the European Investment Bank and the other existing financial instruments** (OJ 1988 L 374, p. 1).

4 — OJ 1988 L 185, p. 9.

— to verify on a regular basis that operations financed by the Community have been properly carried out;

— to prevent and to take action against irregularities;

— to recover any amounts lost as a result of an irregularity or negligence …

2. Without prejudice to checks carried out by Member States, in accordance with national laws, regulations and administrative provisions … Commission officials may carry out on-the-spot checks, including sample checks, in respect of operations financed by the Structural Funds.

…'

4. Article 24 of Regulation No 4253/88, entitled 'Reduction, suspension and cancellation of assistance', provides as follows:

'1. If an operation or measure appears to justify only part of the assistance allocated, the Commission shall conduct a suitable examination of the case in the framework of the partnership, in particular requesting that the Member State or other authorities designated by it to implement the operation submit their comments within a specified period of time.

2. Following this examination, the Commission may reduce or suspend assistance in respect of the operation or measure concerned if the examinat[i]on reveals an irregularity and in particular a significant change affecting the nature or conditions of the operation or measure for which the Commission's approval has not been sought.

…'

5. In accordance with Article 1(2) of Regulation No 2988/95,[5] '"[i]rregularity" shall mean any infringement of a provision of Community law resulting from an act or omission by an economic operator, which has, or would have, the effect of prejudicing the general budget of the Communities or budgets managed by them, either by reducing or losing revenue accruing from own resources collected directly on behalf of the Communities, or by an unjustified item of expenditure.'

6. Article 8 of Regulation No 2064/97[6] provides as follows:

'1. No later than at the time of the request for the final payment and the final declaration of expenditure in respect of each form of assistance, Member States shall present to the Commission a statement … drawn up by a person or organization functionally independent of the implementing service. The statement shall summarise the conclusions of the control examinations made in the previous years and provide an overall conclusion as to the validity of the request for the final payment and the legality and regularity of the operations underlying the final declaration of expenditure.

2. If the presence of important management or control weaknesses or the high frequency of irregularities encountered does not allow the provision of a positive overall assurance as to the validity of the request for final payment and the final declaration of expenditure, the statement shall refer to these circumstances and shall estimate the extent of the problem and its financial impact.

5 — **Council Regulation (EC, Euratom) No 2988/95 of 18 December 1995 on the protection of the European Communities financial interests** (OJ 1995 L 312, p. 1).

6 — Commission Regulation (EC) No 2064/97 **of 15 October 1997 establishing detailed arrangements for the implementation of Council** Regulation (EEC) No 4253/88 **as regards the financial control by Member States of operations co-financed by the Structural Funds** (OJ 1997 L 290, p. 1).

In such a case the Commission may ask that a further control be carried out with a view to the identification and rectification of irregularities within a specified period of time.'

II – **Background**

A – *Case C-549/12 P*

7. At the request of the German Government and by Decision C(94) 1939/5 of 5 August 1994, the Commission approved the operational programme for the *Land* Thüringen falling under Objective 1 in Germany (Arinco No 94.DE.16.005) providing for a structural funds contribution of ECU 1 021 771 000, increased to EUR 1 086 827 000 by Decision C(99) 5087 of 29 December 1999, with financing by the ERDF of a maximum amount of EUR 1 020 719 000.

8. In relation to measure 2.1 concerning support for productive activities of SMEs, Decision C(99) 5087 fixed the total amount of expenditure at EUR 674 104 000 and the ERDF contribution at EUR 337 052 000.

9. The Ministry of Economy and Transport of the *Land* Thüringen was designated as the managing authority.

10. In the course of 2001, the Commission systematically examined the *Land* Thüringen's management and control systems and, on 30 January 2002, it submitted its final report including certain recommendations.

11. Once the statement referred to in Article 8 of Regulation No 2064/97 had been submitted and the German authorities had requested final payment for the programme, the Commission wound up the assistance and made the final payment at the level of the amount requested on 27 June 2003.

12. Subsequently, in the course of 2003, the Court of Auditors carried out a number of audit visits and, on 22 June 2004, sent its provisional audit report to the German authorities, which sent the Court of Auditors additional information by letters of 31 August and 13 October 2004.

13. The Court of Auditors sent its audit report to the national authorities on 17 January 2005. The report referred to specific cases of irregularities and systemic irregularities, such as the financing of undertakings which do not fall within the definition of SMEs, the declaration of ineligible expenditure (future leases, VAT, rebates), errors in the calculation of the maximum assistance and the lack of supporting evidence for certain types of expenditure such as general expenses or own funds. The report concluded that there were shortcomings in the management and control systems in relation to the assistance. The error rate of the 28 measure 2.1 projects was 31.36%.

14. On 19 October 2006, the Commission sent the German authorities the first results of its examination of the report of the Court of Auditors, inviting those authorities to submit comments.

15. By letter of 5 January 2007, the German authorities replied to the Commission, objecting to the application of extrapolated corrections while providing additional supporting evidence to show the eligibility of certain expenditure.

16. By Decision C(2008) 1690 final of 30 April 2008 ('the decision at issue'), the Commission reduced by EUR 81425825.67 the ERDF financial assistance because of the specific and systemic irregularities determined in the context of the 2.1 measure, applying Article 24 of Regulation No 4253/88. The Commission carried out an extrapolation of the error rate with regard to measure 2.1 as a whole, taking an error rate of 23.88% as the basis. It calculated a sum of EUR 1232012.70 in relation to specific irregularities and EUR 80193812.97 with regard to systemic irregularities.

17. According to the decision at issue, the systemic errors found to exist were as follows:

— funding of a non-SME company;

— final recipient not having satisfied the national criteria applicable to SMEs for 15% additional funding;

— ineligible expenditure declared in connection with leasing contracts.

B – *Case C-54/13 P*

18. By Decision C(94) 1973 of 5 August 1994, the Commission approved the operational programme for Berlin (East) falling under Objective 1 in Germany (Arinco No 94.DE.16.006) providing for a structural funds contribution of ECU 743 112 000, increased to EUR 779 154 000, with financing by the ERDF of an amount of EUR 540 886 000.

19. The Ministry of Economy, Technology and Women of the *Land* Berlin was designated as the managing authority.

20. The German authorities submitted their request for final payment on 24 March 2003.

21. Between February 2004 and March 2005, the Commission and an external audit firm engaged by it carried out a number of audit visits as part of the closing audits for the programmes co-financed by the ERDF during the 1994-1999 funding period.

22. On 31 May and 15 December, the Commission sent its audit report to the German authorities, in which a number of systemic irregularities were identified in relation to specific operations, including, in particular, the declaration of ineligible expenditure (expenditure from which products for sale were not deducted, general expenditure not actually incurred, declarations of expenditure which exceeded expenditure incurred), breaches of the rules on public procurement procedures and the lack of supporting evidence. For the 29 projects selected for assistance which were actually audited, the error rate was 7.56%. Of the 36 projects selected, seven could not be audited because of insolvency.

23. After the German authorities had submitted their comments and additional information, the Commission sent its provisional findings on 26 January 2007; the German authorities objected to those findings, claiming that there was no legal basis, objecting to the application of flat-rate and extrapolated financial corrections and submitting additional evidence of the lawfulness of the expenditure.

24. By Decision C(2008) 1615 final of 29 April 2008 ('the decision at issue'), the Commission reduced by EUR 12900719.52 the ERDF financial assistance. The Commission relied on an error rate of 3.63% for the 29 projects audited and applied an extrapolated financial correction which represented a reduction of 2.68% of the ERDF financial assistance to the overall programme.

III – **The judgments of the General Court**

25. The Federal Republic of Germany brought two actions before the General Court which were dismissed by judgments of 19 September 2012 (Case T-265/08 *Germany* v *Commission*) and 21 November 2012 (Case T-270/08 *Germany* v *Commission*).

26. The General Court rejected the pleas in law put forward by the Federal Republic of Germany supported by Spain, the Netherlands and the United Kingdom which are also involved in the appeal proceedings.

27. First, the Federal Republic of Germany submitted that the conditions required by Article 24(2) of Regulation No 4253/88 in order to reduce the assistance were not satisfied. However, the General Court found that administrative errors attributable to the national authorities could be classified as irregularities within the meaning of that article, while the concept of 'irregularity', laid down by Article 1(2) of Regulation No 2988/95, was irrelevant because it was a regulation which pursued different objectives and also had a different scope.

28. Second, the Federal Republic of Germany complained that Article 24(2) of Regulation No 4253/88 did not permit the application of the extrapolation method to calculate the amount of the reduction, to which the General Court replied that it was the most appropriate method by which to guarantee the objective pursued by the regulation, namely to enable a financial correction capable of covering all the losses sustained by the Union budget.

29. Third, the Federal Republic of Germany complained that the Commission relied on an analysis by the Court of Auditors instead of carrying out its own on-the-spot audit of the facts of the case. The General Court held that this did not amount to an infringement of Article 24(2).

30. Fourth, the General Court rejected the argument that there was an infringement of the principles of the protection of legitimate expectations, legal certainty and cooperation on the grounds that the Commission took into account the erroneous accounting of certain undertakings.

31. Lastly, the General Court rejected the claim that the application of the extrapolation method was contrary to the principle of proportionality.

32. Appeals were lodged against those judgments of the General Court, leading to the present proceedings before the Court of Justice.

IV – **The appeals**

33. The appeal in Case C-549/12 P is based on two grounds: (i) error of law in the classification of certain administrative errors as 'irregularities'; (ii) error of law in the application of the extrapolation method.

34. The appeal in Case C-54/13 P repeats the above two grounds and adds the following two: (i) error of law in the unlawful application of flat-rate financial corrections; (ii) infringement by the General Court of the duty to provide grounds for its decisions.

V – **The procedure before the Court of Justice**

A – *Case C-549/12 P*

35. The first appeal was lodged at the Court Registry on 29 November 2012.

36. By the first part of its first ground of appeal, the Federal Republic of Germany claims that the General Court erred in law in holding that administrative errors attributable to the national authorities could be classified as irregularities within the meaning of Article 24(2) of Regulation No 4253/88. In the view of the Federal Republic of Germany, the concept of 'irregularity' must be interpreted in accordance with Article 1(2) of Regulation No 2988/95. By failing to do so, the General Court breached that article and the principle of conferral of powers laid down in Article 5(2) TEU and Article 7 TFEU.

37. The Commission contends that, as regards shared management in relation to structural funds, Article 24 of Regulation No 4253/88 applies to financial corrections relating to recipients, on the one hand, and Member States, on the other, while, in the latter case, Regulation No 4253/88 and Regulation No 2988/95 are not to be interpreted in conjunction with one another.

38. By the second part of the first ground of appeal, the Federal Republic of Germany submits that the General Court erred in law in holding that infringements of national law and errors which do not affect the EU budget may, in accordance with Article 1(2) of Regulation No 2988/95, constitute irregularities within the meaning of Article 24(2) of Regulation No 4253/88.

39. The Commission contends in that connection that the concept of 'irregularity' encompasses all types of breach of the applicable rules which may entail a risk to the EU budget, and that it is clear that inappropriate expenditure constitutes a risk of that kind.

40. By the second ground of appeal, the Federal Republic of Germany argues that the General Court erred in law inasmuch as it granted the Commission the right to carry out financial corrections on the basis of extrapolation and confirmed the detailed rules for carrying out extrapolation established by the Commission in the present case.

41. By the first part of the second ground of appeal, the Federal Republic of Germany, supported by the Kingdom of Spain and the French Republic, submits that the judgment under appeal infringed Article 24(2) of Regulation No 4253/88 — the wording of which (unlike the express provisions of the legislation applicable to the next funding period)[7] permits action to be taken only in respect of operations or measures which have actually been identified as irregular — and the principle of conferral of powers.

42. The Commission contends that, in accordance with the guidelines on net financial corrections which it adopted in order to determine the detailed rules for the application of Article 24(2) of Regulation No 4253/88, where an audit establishes a general risk to the whole operational programme it must be possible to carry out an extrapolated correction in order to prevent the EU budget from meeting items of expenditure which were not incurred in accordance with the applicable legislation.

43. By the second part of the second ground of appeal, the Federal Republic of Germany, supported by the Kingdom of Spain, argues that, in any event, the General Court erred in law in finding that the Commission correctly carried out an extrapolated correction in the present case. The first reason is because, in the absence of a loss to the EU budget, the erroneous recording of specific projects cannot be the basis for an extrapolated financial correction, which is contrary to the principle of proportionality. The second reason is because the General Court accepted the classification by the Commission of certain irregularities as systemic despite the contrary view of the Court of Auditors.

7 — Council Regulation (EC) No 1260/1999 of 21 June 1999 laying down general provisions on the Structural Funds (OJ 1999 L 161, p. 1).

44. The Commission counters that it was authorised to carry out an extrapolated correction in the case of the incorrect recording of expenditure entailing a risk of loss to the EU budget and that the classification of the irregularities as systemic was based on point 5 of the guidelines on financial corrections, without being related to the legal considerations of the Court of Auditors. Moreover, in the Commission's view, the extrapolation is proportionate in so far as it transfers to the rest of the operational programme the error rate identified in a representative sample.

B – *Case C-54/13 P*

45. The second appeal was lodged at the Court Registry on 31 January 2013.

46. The first two grounds of this appeal are essentially the same as the grounds of appeal which gave rise to Case C-549/12.

47. In particular, the Federal Republic of Germany complains that the General Court confirmed the systemic irregularities established by the Commission, whereby the latter included errors linked to the rules on public procurement procedures which could only affect certain parts of the operational programme, and errors relating to very specific and uncertain cases.

48. The Federal Republic of Germany further disputes that the General Court was correct to hold that the Commission chose the appropriate sampling procedure, from which it follows that the error rate established is not representative.

49. In addition, the Federal Republic of Germany contends that the extrapolation of unrepresentative errors and errors quantified at a flat rate is contrary to the principle of proportionality, since the financial correction goes beyond compensation for financial losses actually sustained by the EU budget.

50. In response to that, the Commission argues that the irregularities identified were systemic in nature, since they were evidence of shortcomings in the management and control systems. Further, the sample was carried out in accordance with an internationally recognised technique. Finally, the Commission submits that extrapolation is of itself a proportionate method for evaluating and quantifying the risk entailed by the assistance concerned.

51. By the third ground of appeal an infringement is alleged of Article 24(2) of Regulation No 4253/88 as a result of the application of flat-rate financial corrections.

52. In that connection, the Commission contends that a flat-rate calculation is appropriate for irregularities which do not have a specific value, as in the present case, and it is also proportionate in view of the seriousness of the operations.

53. Finally, by the fourth ground of appeal it is alleged that the General Court infringed the duty to provide grounds for its decisions, since it did not deal with the arguments relating to the unlawfulness of the flat-rate financial corrections; this is disputed by the Commission.

54. The hearing in the appeals was held on 9 January 2014 and oral argument was presented by the Federal Republic of Germany, the Kingdom of Spain and the Commission.

VI – **Assessment**

55. Although I shall state my position on each of the grounds of appeal put forward by the Federal Republic of Germany, I shall focus in greater detail on the second ground, which raises the question as to whether the extrapolation method may be applied when carrying out financial corrections in the case of irregularities identified in operations financed by the ERDF.

A – *The first ground common to both appeals*

56. The Federal Republic of Germany maintains that the General Court erred in law in holding that Article 24(2) of Regulation No 4253/88 authorises the Commission to make financial corrections as a result of administrative errors.

57. In line with the Commission's approach, it is appropriate to begin by pointing out that, in addition to the general obligations arising from the principles of cooperation in good faith and procedural autonomy of the Member States, where the latter implement EU provisions in relation to EU funds or financial programmes this also triggers the reciprocal responsibilities which are incumbent on the Commission and the Member States for the purposes of implementation of the Community budget and which are set out in Article 247 EC (now Article 317 TFEU), Regulation No 1605/2002 ('the financial regulation'),[8] Regulation No 2342/2002 ('the implementing regulation'),[9] and, in the present case, the regulations on structural funds.

58. As a result, the Federal Republic of Germany received from the European Union a financial contribution which it has a duty to manage on behalf of the Union, ensuring that it is used in accordance with the applicable legislation.

59. As regards this kind of shared management of Union financial contributions, the Court of Justice has established settled case-law on structural funds, primarily the European Agricultural Guidance and Guarantee Fund (EAGGF) and the European Social Fund (ESF).[10] To my mind — and I agree with the Commission on this point — that case-law is equally applicable to the ERDF, which is, after all, also a structural fund from which contributions to the Member States can be checked only indirectly and not exhaustively by the Commission.

60. As the Commission points out, in accordance with that case-law, only 'expenditure incurred in conformity with the Community rules is to be charged to the Community budget'.[11] Admittedly, the reference to 'Community rules' could support the view, put forward by the Federal Republic of Germany, that the infringement of national rules cannot be taken into consideration. I do not believe that to be so.

61. In the case of shared management of EU funds, the Community legislation — focusing on the general rules governing the conditions for the distribution and management of subsidies financed by the Union — will inevitably be complemented by the national provisions which, by giving concrete expression to those general rules, make it possible to determine exactly the recipients of those subsidies.

8 — Council Regulation (EC, Euratom) No 1605/2002 of 25 June 2002 on the Financial Regulation applicable to the general budget of the European Communities (OJ 2002 L 248, p. 1).

9 — **Commission Regulation (EC, Euratom) No 2342/2002 of 23 December 2002 laying down detailed rules for the implementation of** Regulation No 1605/2002 (OJ 2002 L 357, p. 1).

10 — In general, Case C-199/03 *Ireland* v *Commission* [2005] ECR I-8027.

11 — *Ireland* v *Commission*, paragraph 26, citing the judgment in Case C-55/91 *Italy* v *Commission* [1993] ECR I-4813, paragraph 67. The Court held that this principle, which was originally laid down in relation to the EAGGF, was applicable to the ESF.

62. In that connection, the Community and national provisions constitute a whole for the purposes of Article 24(2) of Regulation No 4253/88, which, in referring to an 'irregularity … affecting the nature or *conditions* of the operation or measure',[12] must encompass all the rules which define, in full, the content and scope of those conditions.

63. I am now indicating my position with regard to the question raised by the German Government concerning the rule in which to seek the definition of irregularity which is relevant for the present purposes. Furthermore, my position is in line with that proposed by the Commission.

64. The Federal Republic of Germany contends that the starting point must be the definition of 'irregularity' contained in Article 1(2) of Regulation No 2988/95 on the protection of the European Communities financial interests, pursuant to which '"[i]rregularity" shall mean any infringement of a provision of Community law resulting from an act or omission by an economic operator, which has, or would have, the effect of prejudicing the general budget of the Communities …'

65. Since that provision is a *general* rule concerning the protection of the EU's financial interests, I believe that it must give way to the rule contained in Article 24(2) of Regulation No 4253/88, which is a *special* rule governing the protection of the EU's financial interests in the specific field of structural funds.

66. Accordingly, it cannot be claimed that the Commission may only cancel or reduce financial assistance if the irregularity identified is attributable to an economic operator, as provided for in Article 1(2) of Regulation No 2988/95, thereby excluding irregularities attributable to the national authority responsible for the management of Community assistance.

67. In that connection, the Court has held that 'Article 24 of Regulation No 4253/88 does not make any distinction of a quantitative or qualitative nature concerning the irregularities which may give rise to reductions in assistance.'[13] That assertion, although made in response to the observation that the irregularities identified in that case were of a technical nature, may be applied to a situation like the present one, in which the public *nature* of the authority to which the irregularity is attributed is invoked.

68. That is because, as the Commission points out, and in the words of the judgment in *Conserve Italia* v *Commission*,[14] 'Article 24(2) of Regulation No 4253/88 … constitutes the legal basis for any claim for recovery by the Commission.' Therefore, a broad interpretation of the concept of 'irregularity' within the meaning of that provision is imperative if its practical effect is not to be significantly affected, since otherwise it would not be possible to correct the irregularities attributable to the national public managing authority, which must be taken into account in the context of the shared management specific to structural funds.

69. I believe, therefore, that the General Court was right to conclude, in paragraph 40 of the first judgment under appeal, that 'the fact that the national authorities have a central role to play in the implementation of the structural funds supports a broad interpretation of the concept of "irregularity" … [since] an error committed by those authorities must be considered to be an "irregularity" within the meaning of Article 24(2) of Regulation No 4253/88, in the light of the principles of sound financial management, referred to in Article 274 EC, and of cooperation in good faith, referred to in Article 10 EC, which do not authorise immunity for the Member States, and taking into account the fact that Article 24 of Regulation No 4253/88 is the only provision which allows the amount of assistance to be reduced where the intervention did not take place as originally envisaged …'[15]

12 — Emphasis added.

13 — *Ireland* v *Commission*, paragraph 30.

14 — Case C-500/99 P [2002] ECR I-867, paragraph 88.

15 — The same view is set out in paragraph 28 of the second judgment under appeal in these proceedings.

70. Finally, I also disagree with the view that only irregularities which are prejudicial to the EU budget are important.

71. Once again, that is a condition laid down in Article 1(2) of Regulation No 2988/95 but not in Article 24(2) of Regulation No 4253/88, which takes precedence in this case and in which the relevant irregularities are those 'affecting the nature or conditions of the operation or measure for which the Commission's approval has not been sought'. It is clear that the legislature's interest in ensuring the proper implementation of financing operations and measures is ultimately explained by its interest in avoiding any loss to the Community budgets. However, without reaching that point, it is equally clear that any irregularity, including one which does not directly produce such a loss, is evidence of a shortcoming in the management of public funds which, as such, constitutes a risk to the budget. That applies irrespective of the fact that the primary aim of Article 24(2) of Regulation No 4235/88 is the sound management as such of EU funds, and, therefore, to my mind, irrespective of the fact that the irregularities identified translate into immediate financial damage.

72. Accordingly, I believe that the first ground of both appeals must be rejected.

B – *The second ground common to both appeals*

73. The Federal Republic of Germany submits that the General Court erred in law in granting the Commission the power to carry out financial corrections on the basis of extrapolation and in confirming the extrapolation actually carried out in the present case.

1. Whether use of the extrapolation method is lawful in the context of the ERDF

74. The German Government's argument, which is supported by the Spanish and French governments, is essentially textual, since it is based on the fact that Article 24(2) of Regulation No 4253/88 refers specifically to '*an* irregularity and in particular *a* significant change affecting the nature or conditions of *the* operation or measure'.[16] According to the German Government, it follows that the reduction or cancellation of assistance is possible only if a specific irregularity or change has actually been identified, and it is thus inappropriate to apply the extrapolation method in respect of operations or measures which have not been examined.

75. That is the approach adopted by Advocate General La Pergola in his Opinion in Case C-443/97 *Commission* v *Spain*,[17] in which he stated that 'the *literal wording* [[18]] of Article 24 does not allow infringements of the obligations stated in Article 23(1) to be included in the concept of "irregularity" so as to justify net reductions'.[19]

76. In addition to the foregoing, there is the fact that, unlike Article 24(2) of Regulation No 4253/88, Regulation No 1260/1999, which was applicable to the 2000-2006 period, does expressly authorise the Commission, in Article 39(3)(b), to 'make the financial corrections required' if it is established that 'there are serious failings in the management or control systems which could lead to systemic irregularities' (Article 39(2)(c)). Article 39(3)(b) goes on to provide that those corrections consist of 'cancelling all or part of the contribution of the Funds to the assistance concerned' and that, when deciding the amount of a correction, the Commission must 'take account, in compliance with the principle of proportionality, of the type of irregularity or change and the extent and financial implications of the shortcomings found in the management or control systems of the Member States.'

16 — Emphasis added.

17 — Opinion delivered on 28 October 1999 (judgment of 6 April 2000 ECR I-2415), points 18 to 24.

18 — Emphasis in original.

19 — Opinion of Advocate General La Pergola, point 21.

77. In short, the German Government maintains that it is apparent from both the wording of Article 24(2) of Regulation No 4253/88 and that of the legislation subsequently applied in this area that that article does not permit use of the extrapolation method.

78. Those arguments may be countered by the arguments which I shall develop below. First, Article 24 of Regulation No 4253/88 has to be interpreted in conjunction with the article which precedes it. Second, the subsequent development of the legislation applicable to this subject does not determine the interpretation to be given to that now at issue.

a) The system of Articles 23 and 24 of Regulation No 4253/88

79. In my view, Articles 23 and 24 of Regulation No 4253/88 make sense only if they are regarded as a system established around the concept of 'irregularity'. Article 23(1) imposes on Member States the obligation to take the necessary measures to verify that operations financed by the Community have been properly carried out, to prevent and to take action against irregularities and, as the case may be, to recover any amounts lost as a result of an irregularity or negligence.[20] In short, it is a question of establishing a financial control system capable of ensuring the correct use of the Community funds.

80. If the Member States do not comply properly with that obligation, either by failing to establish an adequate control system or by failing to apply that system correctly in a particular case, they have committed a clear irregularity. In the first situation, the reaction of EU law must take the form of an action for annulment,[21] while, to my mind, in the second situation, the relevant procedure may only be the cancellation or reduction of the assistance provided for in Article 24(2) of Regulation No 4253/88.

81. The identification of certain failings in the control system established by a Member State is one of the situations which may legitimately give rise to an uncertainty based on the justification for specific assistance allocated by the European Union. Such situations are referred to in Article 24(1) of Regulation No 4253/88, which refers to the case where 'an operation or measure appears to justify only part of the assistance allocated'. Based on that appearance, the article requires the Commission to 'conduct a suitable examination of the case in the framework of the partnership, in particular requesting that the Member State ... submit their comments within a specified period of time.'

82. Following that examination, in accordance with Article 24(2) of Regulation No 4253/88, 'the Commission may reduce or suspend assistance in respect of the operation or measure concerned if the examinat[i]on reveals an irregularity and in particular a significant change affecting the nature or conditions of the operation or measure'. In my opinion, an irregularity in the control system for EU financial assistance has a very substantial effect on the *conditions* of the operation or measure benefitting from that assistance. It is possibly the type of irregularity which most directly affects those conditions.

83. Accordingly, I can find no reason to maintain that the irregularities identified in the failure to comply with the obligations laid down in Article 23(1) of Regulation No 4253/88 cannot be included in the irregularities which justify the cancellation or reduction of assistance in accordance with Article 24(2) of the regulation. That circumstance, as we shall see, legitimises use of the extrapolation method since, owing to their very nature, irregularities in a control system are likely to affect all the operations made subject to that system and, once identified as systemic failings, they may be corrected only if they are deemed to affect all those operations.

20 — To that effect, Case C-465/10 *Chambre de Commerce et d'Industrie de l'Indre* [2011] ECR I-14081, paragraph 35.

21 — That is apparent from the Order of the Court in Case C-325/94 P *An Taisce and WWF UK* v *Commission* [1996] ECR I-3727, paragraph 22.

b) The subsequent legislation and its relevance to the interpretation of Article 24(2) of Regulation No 4253/88

84. Admittedly, as the German Government contends, the legislation applicable to the 2000-2006 period expressly authorises the Commission to 'make the financial corrections required' if it is established that there are 'serious failings in the management or control systems which could lead to systemic irregularities' (Article 39(2)(c) and (3)(b) of Regulation No 1260/1999). That does not mean, however, that, in accordance with the predecessor legislation it was not also possible to proceed in the same way, although then it was only in accordance with an authorisation which had to be regarded as implied as a result of the system established by Articles 23 and 24 of Regulation No 4253/88. [22]

85. The Court has also taken that approach, concluding that the guidelines drawn up in the Commission's document of 15 October 1997, entitled 'Net financial corrections in the context of the application of Article 24 of Regulation (EEC) No 4253/88', [23] which were applied to the present cases, express 'the general lines along which, pursuant to Article 24 … the Commission envisages subsequently adopting individual decisions whose legality may be challenged before the Court by the Member State concerned'. [24] Points 5 and 6 of that document refer explicitly to financial corrections in cases of irregularities which indicate systemic failings in management, control or audit. Due to the very nature of the failings they indicate, the risk posed by such irregularities may be quantified only in accordance with the extrapolation method.

86. That cannot be countered by the argument that, in this way, the Commission, far from interpreting the power conferred on it by Article 24(2) of Regulation No 4253/88, is assuming a power which in reality the article does not confer on it, since, again in the words of the Court in relation to the guidelines contained in the 'financial corrections' document, 'there is nothing to prevent the Commission, for the purpose of assuming fully the power referred to in the paragraph above, [[25]] from adopting internal guidelines concerning financial corrections to be made when applying Article 24 of the coordination regulation, and from entrusting the departments concerned with the task of applying them'. [26]

87. Moreover, the differences between the model applicable to the 2000-2006 period and that at issue in the present case are not so significant as far as one of the most sensitive aspects of the question is concerned, namely the ability of the Member States to defend their rights and interests.

88. The Federal Republic of Germany rightly contends that the system laid down in Regulation No 1260/1999 guarantees that a Member State has the opportunity to submit comments and to attend a hearing with the Commission if the Member State objects to the observations made by the Commission, and requires both sides to make efforts to reach an agreement 'in cooperation based on the partnership' (Article 39(2), second subparagraph). That guarantee is not excluded from Article 24 of Regulation No 4253/88, paragraph 1 of which provides that the Commission is to conduct a

22 — In its judgment in Case C-271/01 *COPPI* [2004] ECR I-1029, in paragraph 41, the Court observed that although Article 23(1) of Regulation No 4253/88 'does not provide expressly for the revocation by a Member State of financial assistance from the EAGGF …, that provision would be deprived of useful effect if a Member State could not itself adopt such measures'. The reason justifying that implied grant of power to the Member States by Article 23(1) also, in my view, supports the grant of a similar power to the Commission in Article 24(1) in the case of irregularities which have not been corrected by the Member States under Article 23(1) of the regulation.

23 — C(97) 3151 final — II.

24 — Case C-443/97 *Spain* v *Commission*, paragraph 33.

25 — In other words, the power which, pursuant to Article 24(2), authorises the Commission 'to reduce or suspend assistance in respect of the operation or measure concerned if the examination referred to in Article 24(1) of the regulation reveals an irregularity or a significant change affecting the nature or conditions for the implementation of the operation or measure for which the Commission's approval has not been sought'. *Spain* v *Commission*, paragraph 30.

26 — *Spain* v *Commission*, paragraph 31.

suitable examination of the case 'in the framework of the partnership' and based on the comments submitted by the Member State. That is what occurred in the two cases at issue in these proceedings and there is no basis at all for the claim that the national authorities were denied the opportunity to defend themselves against the conduct of the Commission.

89. It should also be pointed out that the Commission's conduct followed the guidelines laid down in the aforementioned 'net financial corrections', which are common knowledge and which the Court has stated 'contribute to ensuring that, when the Commission takes decisions pursuant to that provision, the Member States or the authorities designated by them benefit from identical treatment in comparable situations … [and] are likely to strengthen the transparency of individual decisions addressed to Member States'. [27] In short, as stated above, they indicate 'the general lines along which, pursuant to Article 24 … the Commission envisages subsequently adopting individual decisions whose legality may be challenged before the Court by the Member State concerned', [28] so that, ultimately, the right to effective legal protection of the Member State concerned will not be infringed.

90. In my opinion, therefore, the General Court did not err when it stated that 'the financial loss sustained by the budget of the European Union ... must be corrected in its entirety since any failure of implementation would constitute an infringement of the principle of sound financial management, to which the Commission and the Member States must adhere under Article 274 EC. Thus, the Commission must be able to reduce the assistance to an extent which reflects the dimension of the irregularity which it established after the hearing of those concerned under Article 24(1) of Regulation No 4253/88'. [29]

91. Nor did the General Court err in stating that, since the reduction decision must reflect the systemic dimension of the irregularities identified and in view of the fact that 'the Commission lacks the information regarding the entirety of the controls carried out by the Member State …, use of the extrapolation method is the most appropriate method by which to guarantee the objectives pursued by Article 24(2) of Regulation No 4253/88'. [30]

92. Since the Commission does not itself carry out the financial control of assistance and does not have all the information regarding the entirety of the controls carried out by the national authorities, but is nevertheless obliged to ensure the integrity of the EU's budgetary resources, it is clear that the Commission can comply with that obligation only if it employs a method, like the extrapolation method, which allows the application to all assistance of the results obtained from the selective controls which it is the Commission's responsibility to carry out. In other words, the necessarily partial and selective nature of the controls carried out by the Commission must be subject to a correction method of the same nature. As will be seen below, that is subject to the qualification that the extrapolation method must be applied with the proper guarantees in connection with the reliability of the application of its results to the assistance as a whole.

93. It is now necessary to determine whether, having accepted as a matter of principle the suitability of the extrapolation method for carrying out financial corrections in relation to the ERDF, that method was applied lawfully in the circumstances of the present cases.

27 — *Spain* v *Commission*, paragraph 32.

28 — *Spain* v *Commission*, paragraph 33.

29 — Judgment under appeal in Case C-549/12, paragraph 91; the same view is set out in paragraph 101 of the judgment under appeal in Case C-54/13.

30 — Judgment under appeal in Case C-549/12, paragraph 95; the same view is set out in paragraph 106 of the judgment under appeal in Case C-54/13.

2. Application of the extrapolation method in the circumstances of the present cases

94. The Federal Republic of Germany maintains that the General Court erred in law in holding that the corrections carried out in each case based on the extrapolation method were correct.

a) Case C-549/12

95. As regards the judgment under appeal in Case C-549/12, the German authorities maintain that, since there was no loss to the EU budget, the Commission should have disregarded the erroneous recording of specific projects, the extrapolation of which had the effect of an overcompensation in favour of the Union and was contrary to the principle of proportionality. In addition, the German Government takes the view that the Commission should not have diverged from the opinion of the Court of Auditors regarding the non-systemic nature of certain irregularities, without giving explicit and detailed reasons.

96. As concerns the first of those two complaints, it should be noted, as explained in paragraphs 51 to 53 of the judgment under appeal, that the five projects the recording of which, according to the German government, did not cause any damage to the EU budget, were eligible to be subsidised under measure 1.1 but were in fact incorrectly subsidised under measure 2.1, while the time-limit within which it was possible to amend the allocation of the projects to one or other measure had expired.

97. Admittedly, paragraph 52 of the judgment under appeal states that 'the existence of those irregularities is sufficient for the imposition of a financial correction, without specific financial damage to the Community budget being required'. That does not necessarily mean that the General Court took the view that in this case no specific damage was sustained. In fact, in paragraph 50, the General Court observes that a particular project (Tralag Landmaschinen) incorrectly received additional funding of 15%. The other four programmes would have been eligible to be subsidised if they had been allocated to measure 1.1 but were not eligible to be subsidised under measure 2.1, in accordance with which they were, however, subsidised. That irregularity meant that projects were subsidised which, although eligible to be subsidised in theory, could be subsidised in practice only if they complied with certain conditions imposed by the European Union, which the Member State had a duty to ensure were respected. In my opinion, that translates into clear damage to the Community budget from which projects which did not comply with the conditions laid down for that purpose were subsidised.

98. In any event, the finding that the projects invoked by the German Government did not entail specific financial damage does not mean that they may not be subject to extrapolation. The object of extrapolation is not, as the Federal Republic of Germany states, the financial effect of an irregularity but rather the irregularity itself. The projects in question may not have created a specific financial effect but they all entailed a serious irregularity, namely that they did not concern SMEs and, therefore, infringed one of the main conditions for the subsidy.

99. Accordingly, I agree with the General Court when it concludes in paragraph 66 of the judgment under appeal that 'the erroneous recording with regard to non-SMEs is systemic in character in so far as it reflects *insufficient management, control or audit, shortcomings which occurred a number of times and which can probably be found in a series of similar cases.* [31] The Commission was therefore correct in categorising such erroneous recording in relation to non-SMEs as systemic irregularities.'

31 — Emphasis added.

100. In that connection, I also believe that the Commission was not bound by the opinion of the Court of Auditors, since, in accordance with paragraph 65 of the judgment of the General Court, 'it is not apparent from the wording of Article 24 of Regulation No 4253/88 that, when exercising its powers under that article, the Commission is bound by the observations of that review body. On the contrary, it is for the Commission to give its own evaluation of the irregularities found to exist. Thus, the decision at issue reflects the Commission's assessment and not that of the Court of Auditors.'

101. Moreover, the Federal Republic of Germany does not strictly speaking call into question the rigour of the audit carried out by the Commission but only whether the sample used was representative, claiming that the irregularities identified in the projects, which, it also claims, did not cause any damage to the EU budget, should have been excluded from that sample. Apart from that point — which I, like the General Court, consider to be immaterial — the German Government does not detract from the merits of an audit which, based on a sufficiently representative sample, identified an irregularity which may reasonably be described as systemic, and, as such, be extrapolated to all the subsidised projects. Since an irregularity identified on the basis of a sufficiently representative sample was extrapolated, it is clear that, because of its very nature, the result of the extrapolation can only be proportionate.

b) Case C-54/13

102. As regards the judgment under appeal in Case C-54/13, the Federal Republic of Germany complains that the General Court erred in law in confirming that certain errors relating to very specific and uncertain cases were deemed to be systemic irregularities and in accepting the use of an unsuitable sampling procedure, all of which infringed the principle of proportionality by overcompensating for the financial losses actually sustained by the European Union.

103. In that connection, I believe that it is necessary to point out that the limits of the appeal proceedings do not allow the Court to review the appraisal of the facts carried out by the General Court where the appellant merely raises his personal disagreement in that regard. [32]

104. The cases which the German Government classifies as uncertain (projects no 8 and no 20) are not classified as such by the Commission and were not classified as such by the General Court which, in any event, assessed those cases together with other cases and found, based on reasons, that they were evidence of a set of systemic irregularities capable of extrapolation. In those circumstances, I do not believe that the appeal is an appropriate remedy for the mere expression of opposition by a party.

105. As concerns the suitability of the sampling procedure used in this case, after repeating that, in view of the fact that the management of the funds is shared, the European Union may only carry out spot checks based on sampling techniques, the Commission contends that an internationally recognised technique was used in the present case, namely the MUS (Monetary Unit Sampling) method, which, when applied to a selection of 36 operations (representing 32.3% of the expenditure declared in the context of the assistance in question), provides a sample which is sufficiently representative to allow a suitable extrapolation to the other co-financed operations.

106. The General Court adopted the Commission's view in paragraphs 113 to 115 of the judgment under appeal, observing, moreover, that the method in question was drawn up *ex ante* for the closing audits for the programmes co-financed by the ERDF during the 1994-1999 financing period and was applied in every audit carried out in every Member State to ensure that they all received the same treatment.

32 — To that effect, see, for example, judgment of 6 November 2012 in Case C-551/10 P *Éditions Odile Jacob* v *Commission*, paragraph 85.

107. In my opinion, the Court should not review that reasoned and reasonable assessment of the General Court.

C – *The third ground of appeal in Case C-54/13*

108. By this ground, the Federal Republic of Germany submits, again, that Article 24(2) of Regulation No 4253/88 permits corrections only in the case of actual and specific irregularities, which excludes flat-rate corrections which are of themselves imprecise and based on potential irregularities.

109. However, it is true, as the Commission claims, that the internal guidelines of 15 October 1997 refer expressly in point 7 to flat-rate corrections as a necessary method to correct '[c]ertain types of irregularity which do not have a specific financial value'. In any event, for the reasons set out in support of the dismissal of the previous grounds, nor do I believe that it is possible to uphold this complaint which is based on the premiss that Article 24(2) of Regulation No 4253/88 permits only the correction of actual irregularities.

110. Finally, as regards the alleged disproportionate character of the Commission's corrections, I believe that the arguments set out by the General Court in paragraphs 128 to 134 of the judgment under appeal do not constitute an error in law which may be reviewed on appeal.

111. In my opinion, this ground should therefore be dismissed.

D – *The fourth ground of appeal in Case C-54/13*

112. Lastly, the Federal Republic of Germany contends that the General Court did not provide reasons for its rejection of the appellant's arguments concerning the unlawfulness of the flat-rate financial corrections.

113. As the Commission has observed, the reply to both questions can be found in paragraphs 95 to 108 and 128 to 134 of the judgment under appeal.

114. After explaining, in paragraph 84 of its judgment, that the German authorities submitted that it was not appropriate to use and extrapolate flat-rate financial corrections, the General Court responds in paragraph 96 that Article 24(2) of Regulation No 4253/88 confers on the Commission 'a power of reduction and a broad discretion … without mentioning the limits with regard to the choice of the methods which … it may use to determine the amount of the reduction'. That reference to a free choice of methods means that, in the view of the General Court, the relevant legal basis for use by the Commission of the method actually used in the case in point is found in that article.

115. Admittedly, the General Court then goes on, in paragraphs 97 to 108, to examine the extrapolation method. But that does not mean that it avoided the question of the flat-rate corrections method. On the contrary, the General Court considers those corrections in paragraphs 128 to 134.

116. In that context, it is clear, in my view, that the question at issue was not the lawfulness of the flat-rate method but rather the disproportionate effects in the present case. That question was resolved by the General Court in a way which, whether one agrees with it or not, cannot be regarded as not based on reasons. Therefore, in my opinion, this ground should also be dismissed.

VII – **Costs**

117. In accordance with Article 138(1) and Article 140(1) of the Rules of Procedure, which are applicable to appeal proceedings pursuant to Article 184(1) of the Rules of Procedure, I propose that the Court order the Federal Republic of Germany to bear the costs and the Kingdom of Spain and the French Republic to bear their own costs.

VIII – **Conclusion**

118. In the light of the foregoing considerations, I propose that the Court should:

(1) Dismiss the actions.

(2) Order the Federal Republic of Germany to bear the costs.

(3) Order the Kingdom of Spain and the French Republic to bear their own costs.