JUDGMENT OF THE GENERAL COURT (Eighth Chamber)

18 June 2010 *

In Case T-549/08,

Grand Duchy of Luxembourg, represented by M. Fisch, acting as Agent, and by P. Kinsch, lawyer,

applicant,

v

European Commission, represented by A. Steiblytė and B. Conte, acting as Agents,

defendant,

* Language of the case: French.

APPLICATION for annulment of Commission Decision C(2008) 5383 of 24 September 2008 on the suspension of interim payments from the European Social Fund (ESF) to the single programming document for Community structural interventions falling under Objective 3 to the Grand Duchy of Luxembourg and Commission Decision C(2008) 5730 of 6 October 2008 on the suspension of interim payments from the Community initiative programme to combat discrimination and inequality in the employment market (EQUAL) to the Grand Duchy of Luxembourg,

THE GENERAL COURT (Eighth Chamber),

composed of M.E. Martins Ribeiro, President, S. Papasavvas and N. Wahl (Rapporteur), Judges,

Registrar: T. Weiler, Administrator,

having regard to the written procedure and further to the hearing on 4 March 2010,

gives the following

Judgment

Legal context

1 The first paragraph of Article 147 EC entrusts the administration of the European Social Fund (ESF), which was established under Article 146 EC, to the Commission of the European Communities. In accordance with the first paragraph of Article 159 EC, the ESF is one of the Structural Funds.

2 With regard to the programme period 2000 to 2006, to which the present case relates, the legal framework governing the Structural Funds, in particular the objectives, organisation, functioning and utilisation of the assistance and the role and the powers of the Commission and the Member States in that field, is determined mainly by Council Regulation (EC) No 1260/1999 of 21 June 1999 laying down general provisions on the Structural Funds (OJ 1999 L 161, p. 1).

3 In accordance with Article 9(n) of that regulation, 'managing authority' means any public or private authority or body at national, regional or local level designated by the Member State, or the Member State when it is itself carrying out this function, to manage assistance for the purposes of the regulation. Article 9(o) defines 'payment authority' as one or more national, regional or local authorities or bodies

designated by the Member States for the purposes of drawing up and submitting payment applications and receiving payments from the Commission.

4 Article 34(1)(f) of Regulation No 1260/1999 provides in particular that the managing authority is responsible for ensuring the correctness of operations financed under the assistance, particularly by implementing internal controls in keeping with the principles of sound financial management.

5 Article 38 of Regulation No 1260/1999 provides as follows:

'1. Without prejudice to the Commission's responsibility for implementing the general budget of the European [Union], Member States shall take responsibility in the first instance for the financial control of assistance. To that end, the measures they take shall include:

(a) verifying that management and control arrangements have been set up and are being implemented in such a way as to ensure that Community funds are being used efficiently and correctly;

(b) providing the Commission with a description of these systems;

(c) ensuring that assistance is managed in accordance with all the applicable Community rules and that the funds placed at their disposal are used in accordance with the principles of sound financial management;

(d) certifying that the declarations of expenditure presented to the Commission are accurate and ensuring that they result from accounting systems based on verifiable supporting documents;

(e) preventing, detecting and correcting irregularities, notifying these to the Commission, in accordance with the rules, and keeping the Commission informed of the progress of administrative and legal proceedings;

(f) presenting to the Commission, when each assistance is wound up, a declaration drawn up by a person or department having a function independent of the designated managing authority. This declaration shall summarise the conclusions of the checks carried out during previous years and shall assess the validity of the application for payment of the final balance and the legality and regularity of the transactions covered by the final certificate of expenditure. The Member States may attach their own opinion to this certificate if they consider it necessary;

(g) cooperating with the Commission to ensure that Community funds are used in accordance with the principles of sound financial management;

(h) recovering any amounts lost as a result of an irregularity detected and, where appropriate, charging interest on late payments.

2. The Commission in its responsibility for the implementation of the general budget of the European [Union] shall ensure that Member States have smoothly functioning management and control systems so that Community funds are efficiently and correctly used.

To that end, without prejudice to checks carried out by the Member States in accordance with national laws, regulations and administrative provisions, Commission officials or servants may, in accordance with systems agreed with the Member State in the framework of cooperation described in paragraph 3, carry out on-the-spot checks, including sample checks, on the operations financed by the Funds and on management and control systems with a minimum of one working day's notice. The Commission shall give notice to the Member State concerned with a view to obtaining all the assistance necessary. Officials or servants of the Member State concerned may take part in such checks.

The Commission may require the Member State concerned to carry out an on-the-spot check to verify the correctness of one or more transactions. Commission officials or servants may take part in such checks.

3. The Commission and the Member States shall on the basis of bilateral administrative systems cooperate to coordinate plans, methods and implementation of checks so as to maximise the usefulness of those carried out. They shall immediately exchange the results of the checks carried out.

At least once a year and, in any event, before the annual review provided for in Article 34(2) the following shall be examined and evaluated:

(a) the results of the checks carried out by the Member State and the Commission;

(b) any comments made by other national or Community control bodies or institutions;

(c) the financial impact of the irregularities noted, the steps already taken or still required to correct them and, where necessary, adjustments to the management and control systems.

4. Following this examination and evaluation and without prejudice to the measures to be taken immediately by the Member State under this Article and Article 39, the Commission may make observations, particularly regarding the financial impact of any irregularities detected. These observations shall be addressed to the Member State and the managing authority of the assistance concerned. The observations shall be accompanied, where necessary, by requests for corrective measures to remedy the management shortcomings found and correct those irregularities detected which have not already been corrected. The Member State shall have the opportunity to comment on these observations.

Where, following or in the absence of comments from the Member State, the Commission adopts conclusions, the Member State shall take the necessary steps within the deadline set to comply with the Commission's requests and inform the Commission of its actions.

5. Without prejudice to this Article, the Commission, after due verification, may suspend all or part of an interim payment if it finds that the expenditure concerned is linked to a serious irregularity which has not been corrected and that immediate action is needed. The Commission shall inform the Member State concerned of the action taken and the reasons for it. If, after five months, the reasons for the suspension remain or the Member State concerned has not notified the Commission of the measures taken to correct the serious irregularity, the provisions laid down under Article 39 shall apply.

6. For a period of three years, unless otherwise decided in the bilateral administrative systems, following the payment by the Commission of the final balance in respect of any assistance, the responsible authorities shall keep available for the Commission all

the supporting documents (either the originals or versions certified to be in conformity with the originals on commonly accepted data carriers) regarding expenditure and checks on the assistance concerned. This period shall be interrupted either in the case of legal proceedings or at the duly motivated request of the Commission.'

6 Article 39 of Regulation No 1260/1999, entitled 'Financial corrections', is worded as follows:

'1. The Member States shall, in the first instance, bear the responsibility for investigating irregularities, acting upon evidence of any major change affecting the nature or conditions for the implementation or supervision of assistance and making the financial corrections required.

The Member States shall make the financial corrections required in connection with the individual or systemic irregularity. The corrections made by the Member State shall consist in cancelling all or part of the Community contribution. The Community funds released in this way may be reused by the Member State for the assistance concerned, in compliance with the systems to be defined pursuant to Article 53(2).

2. If, after completing the necessary verifications, the Commission concludes that:

…

(c) there are serious failings in the management or control systems which could lead to systemic irregularities;

the Commission shall suspend the interim payments in question and, stating its reasons, request that the Member State submit its comments and, where appropriate, carry out any corrections, within a specified period of time.

If the Member State objects to the observations made by the Commission, the Member State shall be invited to a hearing by the Commission, in which both sides in cooperation based on the partnership make efforts to reach an agreement about the observations and the conclusions to be drawn from them.

3. At the end of the period set by the Commission, the Commission may, if no agreement has been reached and the Member State has not made the corrections and taking account of any comments made by the Member State, decide within three months to:

(a) reduce the payment on account referred to in Article 32(2);

or

(b) make the financial corrections required by cancelling all or part of the contribution of the Funds to the assistance concerned.

The Commission shall when deciding the amount of a correction 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.

In the absence of a decision to do either (a) or (b) the interim payments shall immediately cease to be suspended.

…'

7 In accordance with Article 3(a) of Commission Regulation (EC) No 438/2001 of 2 March 2001 laying down detailed rules for the implementation of Council Regulation (EC) No 1260/1999 as regards the management and control systems for assistance granted under the Structural Funds (OJ 2001 L 63, p. 21), the management and control systems of managing and paying authorities and intermediate bodies are to, subject to proportionality in relation to the volume of assistance administered, provide for a clear definition, a clear allocation and, as necessary to ensure sound financial practice, an adequate separation of functions within the organisation concerned.

8 Article 4 of Regulation No 438/2001 provides as follows:

'Management and control systems shall include procedures to verify the delivery of the products and services co-financed and the reality of expenditure claimed and to ensure compliance with the terms of the relevant Commission decision under Article 28 of Regulation (EC) No 1260/1999 and with applicable national and Community rules on, in particular, the eligibility of expenditure for support from the Structural

Funds under the assistance concerned, public procurement, State aid (including the rules on the cumulations of aid), protection of the environment and equality of opportunity.

The procedures shall require the recording of verifications of individual operations on the spot. The records shall state the work done, the results of the verification and the measures taken in respect of discrepancies. Where any physical or administrative verifications are not exhaustive, but performed on a sample of operations, the records shall identify the operations selected and describe the sampling method.'

9 Article 7 of Regulation No 438/2001 reads as follows:

'1. Member States' management and control systems shall provide a sufficient audit trail.

2. An audit trail shall be considered sufficient where it permits:

(a) reconciliation of the summary amounts certified to the Commission with the individual expenditure records and supporting documents held at the various administrative levels and by final beneficiaries including, where the latter are not the final recipients of funding, the bodies or firms carrying out operations; and

(b) verification of the allocation and the transfers of the available Community and national funds.

An indicative description of the information requirements for a sufficient audit trail is given in Annex I.

…'

10 Article 9 of the same regulation, entitled 'Certification of expenditure', is worded as follows:

'1. The certificates of statements of interim and final expenditure referred to in Article 32(3) and (4) of Regulation (EC) No 1260/1999 shall be drawn up in the form prescribed in Annex II by a person or department within the paying authority that is functionally independent of any services that approve claims.

2. Before certifying a given statement of expenditure, the paying authority shall satisfy itself that the following conditions are fulfilled:

(a) the managing authority and intermediate bodies have fulfilled the requirements of Regulation (EC) No 1260/1999, in particular Article 38(1)(c) and (e) and Article 32(3) and (4), and observed the terms of the Commission's decision under Article 28 of the Regulation;

(b) the statement of expenditure includes only expenditure:

(i) that has been actually effected within the eligibility period laid down in the decision in the form of expenditure by final beneficiaries, within the meaning of paragraphs 1.2, 1.3 and 2 of Rule No 1 of the Annex to Commission Regulation (EC) No 1685/2000 …, which can be supported by receipted invoices or accounting documents of equivalent probative value;

(ii) that has been incurred in operations that were selected for funding under the particular assistance concerned in accordance with its selection criteria and procedures and have been subject to Community rules throughout the period during which the expenditure was incurred; and

(iii) from measures for which all State aid has been formally approved by the Commission, where relevant.

3. So that the sufficiency of the control systems and the audit trail can always be taken into account before a statement of expenditure is presented to the Commission, the managing authority shall ensure that the paying authority is kept informed of the procedures operated by the managing authority and by intermediate bodies to:

(a) verify the delivery of the products and services co-financed and the reality of expenditure claimed;

(b) ensure compliance with the applicable rules; and

(c) maintain the audit trail.

4. In cases where the managing authority and the paying authority are or belong to the same body, this body shall ensure that procedures offering equivalent standards of control to those stipulated in paragraphs 2 and 3 are applied.'

Background to the dispute

11 On 8 August 2000 the Commission adopted Decision C(2000) 1128 approving the single programming document for Community structural assistance under Objective 3 to Luxembourg (CCI 1999LU053DO001), which provided for a total cost of EUR 93 578 900 and Community co-finance of a maximum of EUR 39 452 700. That decision was last amended by Decision C(2007) 4256 of 10 September 2007, which raised the total cost to EUR 83 289 224 and the maximum financial contribution of the ESF to EUR 35 576 935.

12 On 22 March 2001 the Commission adopted Decision C(2001) 42 approving the Community initiative to combat discrimination and inequality in the employment market (EQUAL) in Luxembourg (CCI 2000LU050PC001), which provided for a total cost of EUR 8 800 000 and an ESF contribution of EUR 4 400 000. That decision was

last amended by Decision C(2007) 3658 of 24 July 2007, which raised the total cost to EUR 8 707 522 and the ESF contribution to EUR 4 353 761.

13 By letter of 7 February 2002, the Luxembourg authorities submitted, pursuant to Article 5 of Regulation No 438/2001, a description of their management and control systems for the two assistance cases referred to in Decisions C(2000) 1128 and C(2001) 42 ('the assistance at issue').

14 Between 8 and 10 July 2002, on the basis of the description submitted by the Luxembourg authorities, the Commission services carried out a preventive audit, pursuant to Article 38(2) of Regulation No 1260/1999, in relation to the programme period 2000 to 2006 to evaluate the management and control systems which had been set up.

15 By letter of 22 August 2002, the Commission sent the final audit report to the Luxembourg authorities. In the report the Commission services found in particular, on the basis of a formal summary, that the management and control systems which had been set up by the Grand Duchy of Luxembourg offered adequate guarantees of compliance with the existing legislation and the generally accepted criteria of sound management.

16 In the course of an audit carried out on 7 and 8 July 2003 in order to make a summary of the closure procedures for the programme period 1994 to 1999, the Commission services also examined the systems set up for the programme period 2000 to 2006.

17 By letter of 4 September 2003, the audit report relating to that examination was sent to the Luxembourg authorities. In the report the Commission services found that the recommendations in the previous report had in general been followed.

18 From 14 to 16 June 2004, the Commission carried out an audit of the management and control systems for the EQUAL programme. By letter of 11 February 2005, it submitted the audit report, according to which the systems met the legal criteria, except for the so-called '5%' checks which had not then been carried out.

19 Between 11 June and 13 July 2007, the Commission services carried out several examinations in order to confirm, on the basis of random sampling, the reliability level of the management and control systems set up for the assistance at issue. The audit report was sent to the Luxembourg authorities by letter of 29 November 2007 ('the audit report of 29 November 2007'). It drew attention to material failings in the management and control systems set up for the assistance at issue concerning the separation of the functions of the managing authority and those of the paying authority, the first-level verifications carried out by the managing authority, the certification by the paying authority of statements of expenditure and the audit trail.

20 By letter of 16 January 2008, the Luxembourg authorities submitted their observations on the audit report of 29 November 2007.

21 By letter of 29 January 2008, the Commission reminded the Luxembourg authorities that it was incumbent upon them to restore sound management of the assistance at issue, particularly by virtue of the principle of sound financial management and having regard to the risks for the Community budget.

22 At the annual meeting on 29 February 2008, the Commission warned the Luxembourg authorities that, if they failed in their obligation to restore sound management of the assistance at issue, the Commission might adopt a decision to suspend the interim payments.

23 By letter of 13 May 2008, the Commission stated that it stood by its position and replied to the arguments put forward by the Luxembourg authorities in their letter of 16 January 2008. The Commission added that none of the recommendations in the audit report of 29 November 2007 could be 'brought to a close' on the basis of the information supplied. In accordance with Article 39(2) of Regulation No 1260/1999, the Commission requested the Luxembourg authorities to submit their observations within two months after receipt of the Commission's letter, together with a description of the corrective measures taken to improve the functioning of the management and control systems for the assistance at issue and the necessary financial corrections.

24 At a meeting on 20 May 2008 between representatives of the Luxembourg General Inspectorate of Finance and the Commission services, the latter gave further details of the reasons for their position with regard to the failings in the management and control systems. The Luxembourg authorities for their part stated that they adhered to their position set out in the letter of 16 January 2008. The managing authority repeated its position at a meeting on 17 June 2008 between the representatives of the Luxembourg managing authority and the Commission services.

25 By Decision C(2008) 5383 of 24 September 2008 on the suspension of interim payments from the European Social Fund (ESF) to the single programming document for Community structural interventions falling under Objective 3 to the Grand Duchy of Luxembourg and by Decision C(2008) 5730 of 6 October 2008 on the suspension of interim payments from the Community initiative programme to combat discrimination and inequality in the employment market (EQUAL) to the Grand Duchy of Luxembourg ('the contested decisions'), the Commission suspended the interim payments from the ESF relating to the assistance at issue. The Commission found

that there were serious failings in the management or control systems which could lead to systemic irregularities within the meaning of Article 39(2)(c) of Regulation No 1260/1999 with regard to the assistance at issue.

Procedure and forms of order sought by the parties

26 By application lodged at the Registry of the General Court on 16 December 2008, the Grand Duchy of Luxembourg brought the present action.

27 Upon hearing the report of the Judge-Rapporteur, the Court (Eighth Chamber) decided to open the oral procedure.

28 The parties presented oral argument and their replies to the questions put by the Court at the hearing on 4 March 2010.

29 The Grand Duchy of Luxembourg claims that the Court should:

— annul the contested decisions;

— order the Commission to pay the costs.

30 The Commission contends that the Court should:

— rule that the action is inadmissible in so far as it relates to Decision C(2008) 5383;

— dismiss the remainder of the application;

— order the Grand Duchy of Luxembourg to pay the costs.

Admissibility

Arguments of the parties

31 The Commission considers that the present action is out of time and therefore inadmissible in so far as it is directed at Decision C(2008) 5383. Under the fifth paragraph of Article 230 EC, actions for annulment must be instituted within two months of notification of the decision to the applicant. In the present case, Decision C(2008) 5383 reached the Permanent Representation of the Grand Duchy of Luxembourg to the European Union on 25 September 2008. Consequently the present action is out of time in so far as it relates to Decision C(2008) 5383.

32 The Grand Duchy of Luxembourg has made no observations on that point in its written pleadings. It did however state, in reply to a question from the Court at the hearing, that it did not deny that it received Decision C(2008) 5383 on 25 September 2008, which was formally noted in the transcript of the hearing.

Findings of the Court

33 It must be observed that, under the fifth paragraph of Article 230 EC, actions for annulment must be instituted within two months of notification of the contested decision to the applicant. Under Article 102(2) of the Rules of Procedure of the General Court, that time-limit is to be extended on account of distance by a single period of 10 days.

34 It has consistently been held that the time-limit for bringing actions is a matter of public policy and is not subject to the discretion of the parties or the Court, since it was established in order to ensure that legal positions are clear and certain and to avoid any discrimination or arbitrary treatment in the administration of justice (Case C-246/95 *Coen* [1997] ECR I-403, paragraph 21, and Joined Cases T-121/96 and T-151/96 *Mutual Aid Administration Services* v *Commission* [1997] ECR II-1355, paragraph 38).

35 In the present case, pursuant to Articles 101(1)(a) and (b) and (2) of the Rules of Procedure, the time-limit for bringing an action against Decision C(2008) 5383 began to run on 26 September 2008, the day following the date of notification of the decision to the Grand Duchy of Luxembourg.

36 Therefore the time-limit for bringing an action against that decision, which included not only the two-month period provided for in the fifth paragraph of Article 230 EC, but also the time-limit on account of distance, provided for in Article 102(2) of the Rules of Procedure, expired on 5 December 2008.

37 It follows that, in so far as the present action for annulment, which was initiated on 16 December 2008, relates to Decision C(2008) 5383, the action is out of time and must therefore be ruled inadmissible. The action is, however, admissible in so far as it relates to Decision C(2008) 5730, of which the Grand Duchy of Luxembourg was notified only on 7 October 2008.

Substance

38 In essence, the Grand Duchy of Luxembourg bases its action on two pleas. The first alleges breach of the principle of the protection of legitimate expectations. The second alleges infringement of Article 39(2)(c) of Regulation No 1260/1999 in that the Commission suspended payments relating to the assistance at issue when in fact the requisite conditions were not fulfilled.

39 With regard to the order in which the pleas raised by the Grand Duchy of Luxembourg should be examined, a question on which the parties disagree, it seems appropriate to examine the plea alleging infringement of Article 39(2)(c) of Regulation No 1260/1999 before that alleging breach of the principle of the protection of legitimate expectations.

Plea alleging infringement of Article 39(2)(c) of Regulation No 1260/1999

Arguments of the parties

40 The Grand Duchy of Luxembourg submits that the Commission infringed Article 39(2)(c) of Regulation No 1260/1999 by suspending the assistance at issue although the conditions required by that provision had not been fulfilled. The finding that there were serious failings which could lead to systemic irregularities is manifestly erroneous. Even assuming that irregularities had been found, they would have been minor and not systemic.

41 First, regarding the organisation of the managing authority and the paying authority, neither Article 3 of Regulation No 438/2001 nor any other provision of that regulation prevents those two authorities from belonging to the same body. That is the situation envisaged by Article 9(4) of the same regulation and there is nothing to prevent the managing authority and the paying authority from carrying out their verifications jointly. In requiring such a degree of functional separation, the Commission erred in law. In the reply, the Grand Duchy of Luxembourg adds that, although the auditors of the two authorities carry out the verification at the same time in relation to the same final beneficiary, that does not give rise to a risk of complicity between the auditor and the person subject to the audit because of the different ethical rules applying within the Luxembourg civil service.

42 Second, with regard to the verification at first level by the managing authority and the certification of expenditure by the paying authority, the Grand Duchy of Luxembourg

submits that the certification of expenditure *en cascade*, that is to say, the choice made by the national managing authority to declare expenditure as to which doubt exists, but which has not been legally classified as ineligible at the date of the declaration, conforms with Article 4 of Regulation No 438/2001. Likewise, the Grand Duchy of Luxembourg claims that the exclusion of only the doubtful item from so-called 'partly ineligible' expenditure and not the full amount of the expenditure does not contravene that provision. This leaves the national authorities with a margin of discretion with regard to the functioning of their management and control systems, provided that those systems provide for procedures for verifying the delivery of co-financed products and services and for verifying that the declared expenditure was actually incurred, and ensure compliance with the conditions laid down in the respective decisions of the Commission. According to the Grand Duchy of Luxembourg, the working document of 21 December 2005 on sound practice concerning the management verifications to be made by the Member States on projects co-financed by the Structural Funds and by the Cohesion Fund, upon which the Commission relies in support of its interpretation, did not command observance at the time when the programmes were being carried out. In short, because of the subsequent checks carried out by the Luxembourg authorities, the European Union's financial interests were safeguarded.

43 Third, the Grand Duchy of Luxembourg considers that the findings of the audit report of 29 November 2007 concerning the audit trail, which are repeated at paragraphs 30 to 32 of the contested decisions and according to which the files kept by the managing authority are incomplete and do not include certain essential information for proving the eligibility and legality of expenditure, are incorrect. This point was referred to by the Luxembourg authorities in their observations of 16 January 2008, which pointed out that it was perfectly possible to find all the information relating to the detailed budget and the results to be achieved in the application document for each project financed. Finally, in the rejoinder, the Grand Duchy of Luxembourg stresses that the information which is allegedly missing was never requested by the Commission from the national authorities.

44 The Commission disputes all the arguments of the Grand Duchy of Luxembourg. It points out that, contrary to the Grand Duchy of Luxembourg's submission, in the

present case it is not a question of minor irregularities, but a number of serious failings concerning the organisation, the first-level verifications by the managing authority, the certification of statements of expenditure by the paying authority and the audit trail, which are key elements of the management and control systems, and each of those failings would have justified the suspension of interim payments.

Findings of the Court

45 First of all, it must be observed that it is clear from the case-law that the rule that only expenditure incurred by the national authorities in conformity with the Community rules is to be charged to the Community budget applies equally to the grant of financial assistance under the ESF (Case C-199/03 *Ireland* v *Commission* [2005] ECR I-8027, paragraph 26).

46 Under Article 39(2)(c) of Regulation No 1260/1999, the Commission is to suspend interim payments if, after completing the necessary verifications, it concludes that there are serious failings in the management or control systems which could lead to systemic irregularities. Article 39(3) of the same regulation states that the Commission may then, if necessary, make the financial corrections required by cancelling all or part of the Fund's contribution to the assistance concerned.

47 In accordance with the requirement of sound financial management underlying the use of the Structural Funds and having regard to the responsibilities of the national authorities in using the Funds, the obligation of the Member States to set

up the management and control systems referred to in Article 38(1) of Regulation No 1260/1999, the detailed rules for which are set out in Articles 2 to 8 of Regulation No 438/2001, is crucial.

48 In the present case, it is necessary to determine whether the Commission was right to suspend the interim payments relating to the EQUAL programme to the Grand Duchy of Luxembourg in view of the failings which it identified and which are connected with, first, the organisation of the managing authority and the paying authority, second, with the verification at first level by the managing authority and the certification of expenditure statements by the paying authority and, third, the audit trail.

49 First, regarding the organisation of the managing authority and the paying authority, the Commission states, at paragraph 3.1.1.5 of the audit report of 29 November 2007, that 'it appeared that the persons responsible for carrying out the verifications provided for in Article 4 [of Regulation No 438/2001] and those provided for in Article 9 [of the same regulation] for the purpose of certifying expenditure carried out those functions jointly'.

50 From that finding the Commission concluded, in recital 18 of Decision C(2008) 5730, that 'the organisation of the managing authority and the paying authority [could] not be regarded as appropriate and did not meet the requirements of Article 3 of Regulation No 438/2001 (clear definition, clear allocation and adequate separation of functions; guarantee that functions are carried out satisfactorily)'. The Grand Duchy of Luxembourg claims in substance that, contrary to the conclusion reached by the Commission, the joint checks by the managing authority and the paying authority respectively in relation to the assistance which is the subject of Decision C(2008) 5730 ('the EQUAL assistance') are not contrary to Regulation No 438/2001.

51 On that point, it must be observed that Article 3(a) of Regulation No 438/2001 provides that 'the management and control systems of managing and paying authorities and intermediate bodies shall, subject to proportionality in relation to the volume of assistance administered, provide for a clear definition, a clear allocation and, as necessary to ensure sound financial practice, an adequate separation of functions within the organisation concerned'.

52 Although, as the Grand Duchy of Luxembourg pointed out, Article 9(4) of the regulation does not prevent the managing authority and the paying authority from belonging to the same body, there must still be a 'clear allocation' and an 'adequate separation' of functions within the organisation concerned.

53 In the present case, it is clear from the reasoning of Decision C(2008) 5730 on that point that it is not so much the irregularities in the checks carried out by those authorities as their lack of reliability that was highlighted by the Commission. In the Commission's opinion, the joint performance of the duties of management and payment gives rise to a degree of doubt as to the impartiality of the persons responsible for the checks in view of the proximity and the 'complicity' that such joint duties entail. In particular, recital 17 of Decision C(2008) 5730 states that 'the verifications provided for by Article 4 of Regulation No 438/2001 and the checks provided for by Article 9 of the same Regulation cannot … be carried out jointly in view of the risk of distorting the judgment of the authority responsible for certifying demands for payment'.

54 That conclusion must be endorsed. As the managing authority and the paying authority are required, by the legislation applying to assistance financed by the ESF, to carry out different checks at different stages, the simultaneous performance of the functions of those authorities creates a significant risk of coordination, or even the merging, of those checks and is therefore such as to give rise to doubt concerning their reliability.

55 Therefore, without the need to refer to the information in the working document on sound practice concerning the paying authority's duty of certification, presented by the Commission services to the Member States and cited by the Commission, the Commission was right in finding that the organisation of the Luxembourg managing and paying authorities contravened Article 3 of Regulation No 438/2001.

56 Second, with regard to the failings in the first-level verifications by the managing authority and the certification of expenditure by the paying authority, the Grand Duchy of Luxembourg contends, in substance, that the Commission, in criticising the system of first-level verification and certification in relation to the EQUAL assistance, disregarded the fact that no ineligible expenditure was taken into account in the subsequent checks and that, ultimately, the financial interests of the Community were safeguarded.

57 However, it must be pointed out that, in the audit report of 29 November 2007, the Commission found that there were certain items of expenditure in relation to which not only had the managing authority failed to carry out a first-level verification, or carried out an inadequate verification, contrary to Article 34 of Regulation No 1260/1999 and Article 4 of Regulation No 438/2001, but also the paying authority had not certified that expenditure in accordance with Article 38(1)(d) of Regulation No 1260/1999 and Article 9 of Regulation No 438/2001. In certain cases those authorities declared expenditure with regard to which they were doubtful. More precisely, the managing authority had carried out incomplete verifications of declared expenditure. Moreover, the irregularities which may have been found in first-level verification were not systematically taken into account by the paying authority at the stage of certifying the statements of expenditure.

58 Such shortcomings are serious failings in the management and control systems which may lead to systemic irregularities. At both the stage of first-level verification by the managing authority and that of certification by the paying authority, which are guarantees of sound financial management, the national authorities must, before the event, completely satisfy themselves that the expenditure in question was incurred and was duly incurred. Contrary to the Grand Duchy of Luxembourg's argument, it is not sufficient for the national authorities to carry out verification after the event and then make financial corrections if necessary.

59 Third, those considerations also apply to the following of the audit trail which is the subject of Article 7 of Regulation No 438/2001. In that respect the Grand Duchy of Luxembourg has not shown that mere reference to the application documents relating to the EQUAL assistance could on its own provide all the specific information required by Article 7(2) and (3) of the regulation.

60 On that point, it must be stressed that Annex I to Regulation No 438/2001, entitled 'Indicative description of information requirements for a sufficient audit trail', gives very specific details with regard to the obligations of national authorities. It states clearly that they must maintain and keep accounting records at the appropriate management level and a body of information for each co-financed operation.

61 Therefore the Commission rightly found that there were serious failings in the management and control systems which could lead to systemic irregularities and, consequently, the Commission suspended the interim payments for the EQUAL assistance.

In that connection, it must be observed that the obligation of applicants and beneficiaries of Community funding to ensure that they provide the Commission with sufficiently specific information for the management and control system put in place to ascertain whether the conditions for the grant of funding are fulfilled to be able to function correctly is inherent in the system of ESF assistance and is essential for it to function properly (see, by analogy, judgment of 6 June 2007 in Joined Cases T-251/05 and T-425/05 *Mediocurso* v *Commission*, not published in the ECR, paragraph 67, and the case-law cited).

62 Therefore the present plea cannot succeed.

Plea alleging breach of the principle of the protection of legitimate expectations

Arguments of the parties

63 The Grand Duchy of Luxembourg considers that the Commission breached the principle of the protection of legitimate expectations because it had expressly found, in the preventive audit reports submitted on 22 August 2002 and 4 September 2003 respectively, that the management and control systems for the assistance at issue offered very satisfactory safeguards. Consequently the conclusions reached by the Commission on those audits were diametrically opposed to those in the contested decisions.

64 First, the preventive audits of 2002 and 2003 pursuant to Article 38(2) of Regulation No 1260/1999 were the only ones in the programme period in question and, second, the contested decisions were made only as a result of a later audit, that is to say, when it was no longer possible to modify the management and control systems in question. In the present case, the Luxembourg authorities had no reason not to rely on the assessment in those reports with regard to the compliance of their management and control systems.

65 The Grand Duchy of Luxembourg adds that, in previous audits, the Commission services had expressly approved the organisation of the managing authority and the paying authority, as well as the audit trail and the procedure for the certification of expenditure *en cascade*, used by the Luxembourg authorities.

66 Regarding the working documents on sound practice to which the Commission refers, they were in all probability drawn up at the end of 2005, that is to say, long after the beginning of the assistance falling within the relevant programme period.

67 As for the report of 7 February 2005, which followed the additional audit of June 2004, which was produced by the Commission as an annex to its statement in defence, it confirms that the Commission services were generally satisfied with the system for selecting projects and declaring expenditure, and the control system.

68 The Grand Duchy of Luxembourg considers that, contrary to the position taken by the Commission, the audits of July 2002, July 2003 and June 2004 did not have a limited scope. An objective reading of the three reports relating to them shows that they followed a detailed examination for the purpose of, first, determining whether the

procedures actually put in place were indeed those notified to the Commission and conformed with the relevant legislation and, second, verifying whether the systems could actually be validated by means of sampling for specific promoters. On that point, it cannot be alleged that the sample of operations checked in the course of those audits was limited and, therefore, not representative, nor can the Grand Duchy of Luxembourg be criticised for that.

69 Consequently the Commission was perfectly informed and approved entirely the Luxembourg management and control systems.

70 The Commission disputes the arguments of the Grand Duchy of Luxembourg. It submits, in essence, that the audit reports are not such as to create legitimate expectations and that, in any case, they did not create legitimate expectations in the present case.

Findings of the Court

71 It has consistently been held that three conditions must be satisfied in order to claim entitlement to the protection of legitimate expectations. First, precise, unconditional and consistent assurances originating from authorised and reliable sources must have been given to the person concerned by the Community authorities. Second, those assurances must be such as to give rise to a legitimate expectation on the part of the person to whom they are addressed. Third, the assurances given must comply with the applicable rules (see Case T-347/03 *Branco* v *Commission* [2005] ECR II-2555,

paragraph 102, and the case-law cited, and Case T-282/02 *Cementbouw Handel & Industrie* v *Commission* [2006] ECR II-319, paragraph 77).

72 In the present case, the question arises as to whether the assessments in the audit reports of 2002, 2003 and 2005 concerning the projects co-financed by the ESF were such as to create a legitimate expectation on the part of the national authorities, which are responsible in the first place for the management and control of the assistance.

73 On that point, it is clear from settled case-law that a breach of the protection of legitimate expectations may not be relied upon by a person who has committed a manifest infringement of the rules in force (see, to that effect, Case 67/84 *Sideradria* v *Commission* [1985] ECR 3983, paragraph 21; order of 25 November 2004 in Case C-18/03 P *Vela and Tecnogrind* v *Commission*, not published in the ECR, paragraphs 117 to 119; and Case T-217/01 *Forum des migrants* v *Commission* [2003] ECR II-1563, paragraph 76, and the case-law cited).

74 The case-law makes it clear that the principle of the protection of legitimate expectations cannot prevent the suspension of Community funding where the conditions laid down for the grant of the funding have manifestly not been fulfilled (see, to that effect, Case T-126/97 *Sonasa* v *Commission* [1999] ECR II-2793, paragraph 39, and judgment of 14 December 2006 in Case T-162/04 *Branco* v *Commission*, not published in the ECR, paragraph 123, and the case-law cited).

75 In the present case, it is clear from the examination of the first plea that there was no manifest error of assessment on the Commission's part when it found in Decision C(2008) 5730 that there were 'serious failings in the management or control systems' which could lead to systemic irregularities and that, consequently, the interim payments relating to the EQUAL assistance should be suspended.

76 Irregularities of that kind, just as in cases where the applicant manifestly failed to comply with the requirements governing the grant of Community funding or with the provisions of a decision granting funding (see, to that effect, *Sonasa* v *Commission*, paragraphs 35, 36 and 39, and order in *Vela and Tecnogrind* v *Commission*, paragraphs 117 and 118), must be described as manifest infringements of the legislation in force.

77 The possible existence of irregularities which have not been investigated or brought to light previously can under no circumstances give rise to a legitimate expectation (see, to that effect and by analogy, Case C-339/00 *Ireland* v *Commission* [2003] ECR I-11757, paragraph 81). Consequently there is nothing to prevent the Commission from drawing financial conclusions after detecting faults in the course of a specific investigation. The national authorities, which are responsible in the first instance for the financial control of assistance (see Article 38(1) of Regulation No 1260/1999), cannot escape liability by pointing to the fact that the Commission found no irregularities during an earlier investigation (see, to that effect, Case C-28/94 *Netherlands* v *Commission* [1999] ECR I-1973, paragraph 76).

78 Therefore, as serious failings under the relevant legislation have been shown to exist, the Grand Duchy of Luxembourg cannot contend that the assessments in the 2002 to 2004 audit reports gave rise to justified expectations that the management and control system in the present case complied with the Community legislation and, therefore, that the payments made in respect of the EQUAL assistance would be finally granted.

79 In any case, as the Commission pointed out at the hearing, the audit reports prepared by its services in connection with setting up operations financed by the Structural Funds are not, in principle, such as to give rise to legitimate expectations within the meaning of the case-law cited at paragraph 71 above that the management and

control systems to be set up by the Member States comply with the requirements. Such reports are generally prepared by means of sampling on the basis of information, which is representative but not exhaustive, relating to the assistance and the reports are limited to the situation observed at the date when the audit was carried out. In addition, the reports reflect only the professional opinion of the officials responsible for the control operations on the spot and not the opinion of the Commission, which is manifested at a later date following a procedure closely involving the Member State concerned.

80 That consideration is all the more relevant to the present case as the documents in the file do not show that the findings in the audit reports prepared before that of 29 November 2007 provided the Luxembourg authorities with any specific assurance whatever such as to justify expectations that the management and control systems for the EQUAL assistance satisfied the requirements and, therefore, that the Commission would not suspend the Community funding for that assistance.

81 The earlier audit reports manifestly did not have the same purpose or the same scope as that of 29 November 2007. First, the report on the preventive audit carried out from 8 to 12 July 2002 clearly states that its purpose is to draw up a 'general summary of the characteristics of the management, payment and control system relating to the assistance". In the words of the report, that audit had merely 'enabled it to be shown that the management and control system set up by the Member State offered adequate guarantees' on the basis of a 'formal summary'. Second, the report of 4 September 2003 on the audit conducted in July 2003 states that, apart from the summary of the closure procedures for the programme period 1994 to 1999, it aimed to 'take stock of the follow-up to the 2002 audit report'. Third, the report of 7 February 2005 relating to the June 2004 audit had the purpose of taking stock of the situation on the basis of various aspects of the legislation mentioned by the auditors (see Part I, point 6, of the report).

82 Consequently those audits were intended to carry out certain verifications of the management and control systems set up for the EQUAL assistance. Only the audit report of 29 November 2007, which states that its purpose is 'to monitor projects on the basis of random sampling in order to confirm the reliability level of the management and control systems for the programme period 2000 to 2006', was such as to confirm the reliability level attributed to the systems in place at the time of the previous audits (see point 1 of the report). The Commission cannot be blamed for the fact that the final audit report was not drawn up until after the programme period referred to in the present case, that is to say, 2000 to 2006, because that is inherent in the financial control system arising from Regulation No 1260/1999.

83 On those grounds, this plea of the Grand Duchy of Luxembourg must be dismissed and, with it, the action as a whole.

Costs

84 Under Article 87(2) of the Rules of Procedure, the unsuccessful party is to be ordered to pay the costs if they have been applied for in the successful party's pleadings. Since the Grand Duchy of Luxembourg has been unsuccessful, it must be ordered to pay the costs, in accordance with the Commission's pleadings.

On those grounds,

THE GENERAL COURT (Eighth Chamber)

hereby:

1. Dismisses the action;

2. Orders the Grand Duchy of Luxembourg to pay the costs.

Martins Ribeiro Papasavvas Wahl

Delivered in open court in Luxembourg on 18 June 2010.

[Signatures]