JUDGMENT OF THE COURT (Fifth Chamber)
1 October 1998 *

In Case C-242/96,

Italian Republic, represented by U. Leanza, Head of the Department for Legal Affairs in the Ministry of Foreign Affairs, acting as Agent, assisted by M. Fiorilli, Avvocato dello Stato, with an address for service in Luxembourg at the Italian Embassy, 5 Rue Marie-Adélaïde,

applicant,

v

Commission of the European Communities, represented by E. de March, Legal Adviser, and P. Ziotti, of its Legal Service, acting as Agents, with an address for service in Luxembourg at the office of C. Gómez de la Cruz, of its Legal Service, Wagner Centre, Kirchberg,

defendant,

APPLICATION for the annulment in part of Commission Decision 96/311/EC of 10 April 1996 on the clearance of the accounts presented by the Member States in respect of the expenditure for 1992 of the Guarantee Section of the European Agricultural Guidance and Guarantee Fund (EAGGF) and in respect of certain expenditure for 1993 (OJ 1996 L 117, p. 19),

* Language of the case: Italian.

THE COURT (Fifth Chamber),

composed of: C. Gulmann, President of the Chamber, M. Wathelet (Rapporteur), J. C. Moitinho de Almeida, J.-P. Puissochet and L. Sevón, Judges,

Advocate General: S. Alber,
Registrar: L. Hewlett, Administrator,

having regard to the Report for the Hearing,

after hearing oral argument from the parties at the hearing on 4 February 1998,

after hearing the Opinion of the Advocate General at the sitting on 24 March 1998,

gives the following

Judgment

1 By application lodged at the Court Registry on 11 July 1996, the Italian Republic brought an action under the first paragraph of Article 173 of the EC Treaty for the annulment in part of Commission Decision 96/311/EC of 10 April 1996 on the clearance of the accounts presented by the Member States in respect of the expenditure for 1992 of the Guarantee Section of the European Agricultural Guidance and Guarantee Fund (EAGGF) and in respect of certain expenditure for 1993 (OJ 1996 L 117, p. 19, 'the contested decision'), in so far as it related to Italy.

2 The application seeks the annulment of that decision in so far as the Commission declared that the following amounts could not be charged to the EAGGF:

— ITL 7 104 000 000 in respect of public storage costs on the ground that the tender procedure for beef was unlawful;

— ITL 54 927 174 194 in respect of costs of public storage of beef on the ground that checks were inadequate and ineligible goods were bought in;

— ITL 34 175 522 595 in respect of the ewe premium on the ground that management and control were inadequate;

— ITL 10 082 336 246 in respect of public storage of cereals on the ground that the system was deficient and checks inadequate;

— ITL 2 169 762 753 on the ground that the setting aside of land given over to the growing of crops in Sicily was unlawful;

— ITL 391 281 020 in respect of the reimbursement of costs of public storage of sugar on the ground that checks were inadequate.

The correction with regard to the unlawful tender procedure

3 The basic rules for the common organisation of the market in beef and veal are contained in Regulation (EEC) No 805/68 of the Council of 27 June 1968

(OJ, English Special Edition 1968 (I), p. 187). Article 6 of that regulation authorises the Commission to intervene with a view to maintaining prices on the Community markets. Regulation No 805/68 was amended in particular by Council Regulation (EEC) No 571/89 of 2 March 1989 (OJ 1989 L 61, p. 43), the version as thus amended (hereinafter 'Regulation No 805/68') being that applicable to the relevant period in the present case (1992).

4 Until 1989, there was a system of automatic intervention buying when prices fell below certain thresholds, with the result that very large quantities were purchased by the intervention agencies at prices exceeding the market price.

5 In order to remedy that unsatisfactory situation, the system was reformed in 1989. Whilst preserving automatic buying-in in the event of a very large fall in prices, a system of buying-in by tendering procedures was introduced with a view to ensuring that the quantities bought in and the prices paid out did not go beyond what was required for reasonable support of the market.

6 Thus, under Article 6(2) of Regulation No 805/68, the Council sets the intervention price each year. When market prices in the Community fall below certain percentages of the intervention price, the intervention agencies in one or more Member States may buy in certain categories, qualities or quality groups of beef and veal originating in the Community, under the conditions laid down in Article 6.

7 The buying-in is organised under tender procedures. Under Article 6(1), such purchases may not exceed a quantity of 220 000 tonnes per year for the entire Community.

8 However, under Article 6(5), in the event of a very steep fall in prices a procedure is implemented whereby all offers at or below 80% of the intervention price are then accepted and are not counted against the maximum quantity referred to in Article 6(1) (the 'safety-net' procedure).

9 Under Article 6(6), tender procedures must ensure equality of access for all persons concerned and those procedures are opened on the basis of specifications.

10 In accordance with Article 6(7), the procedures implementing the intervention system are adopted by the Commission, which also decides on the opening and suspension of tender procedures after consulting a management committee. During the period to which the present case relates, those procedures were defined by Commission Regulation (EEC) No 859/89 of 29 March 1989 laying down detailed rules for the application of intervention measures in the beef and veal sector (OJ 1989 L 91, p. 5).

11 Article 7 of Regulation No 859/89 provides that the decision to open buying-in by invitation to tender is to be published in the *Official Journal of the European Communities* on the Saturday or the Tuesday before the first deadline for the submission of tenders. Under Article 8, during the period in which the invitation to tender is open, the deadline for the submission of tenders is 12 noon (Brussels time) on the second and fourth Wednesday of each month.

12 Article 9 of Regulation No 859/89, which lies at the centre of the dispute, provides:

'1. Tenderers may take part in the invitation to tender only if they undertake in writing to comply with all the provisions relating to the tender concerned.

2. Interested parties may participate in the invitation to tender issued by intervention agencies of the Member States in which this is opened either by lodging a written tender against a receipt or by any other written means of communication accepted by the intervention agency, with advice of receipt; they may submit one tender only per category in response to each invitation to tender.

3. Tenders shall specify:

(a) the name and address of the tenderer;

(b) the quantity tendered for, expressed in tonnes, of the products and categories specified in the notice of invitation to tender;

(c) the price tendered per 100 kilograms of products of quality R3 ...;

(d) the intervention centre or centres to which the tenderer intends to deliver the product.

...'

13 Under Article 9(4)(c) of that regulation, tenderers must prove that they lodged a security for the tender by the final date for submission of tenders and, in accordance with Article 9(5) and (6), tenders may not be withdrawn after the deadline for their submission and are to be confidential.

14 It follows from Article 7 of Regulation No 859/89 that, at the opening of the invitation to tender, a minimum price may be fixed below which tenders are not accepted and from Article 8 that intervention agencies are to notify the Commission of the tenders they have received within 24 hours of the expiry of the time-limit for their submission.

15 Article 11(1) of Regulation No 859/89 provides that, in the light of the tenders received in response to each invitation to tender and after consultation of the management committee, the Commission is to fix a maximum buying-in price; a different price may be set to reflect average market prices for individual Member States or regions within a Member State if special circumstances so require. According to Article 11(2), a decision may also be taken not to proceed with the invitation to tender and, under Article 11(3), if the total of the quantities tendered at a price at or below the maximum price exceeds the quantities to be bought in, a reduction coefficient may be applied to the quantities awarded.

16 Article 12 of Regulation No 859/89 provides that tenders are not to be accepted if the price proposed is higher than the maximum price laid down and Article 10(2) provides that the security is to be released entirely if the tender is not accepted.

17 According to Article 13 of Regulation No 859/89, if the tender is accepted, the security is to be released entirely if the quantity delivered represents at least 95% of the quantity tendered. If the quantity delivered comprises between 85% and 95% of the quantity tendered, the security is to be forfeited to the intervention agencies

in proportion to the quantities lacking, except in cases of *force majeure*. In all other cases, it is to be forfeited to the intervention agencies entirely, except in the event of *force majeure*.

18 The requirement that a security be lodged was introduced in order to put an end to the practice of inflated tenders.

19 Article 12(2) of Regulation No 859/89 provides that rights and obligations arising from the invitation to tender are not to be transferable. Under Article 15 the intervention agency is to pay the successful tenderer the price indicated in his tender.

20 After the facts in the present case arose, Regulation No 859/89 was repealed and replaced by Commission Regulation (EEC) No 2456/93 of 1 September 1993 laying down detailed rules for the application of Regulation No 805/68 as regards the general and special intervention measures for beef (OJ 1993 L 225, p. 4). In place of Article 9 of Regulation No 859/89, there was a new detailed provision concerning the persons eligible to submit tenders, Article 11 of Regulation No 2456/93, which provides that:

'1. Only the following may submit tenders:

(a) slaughterhouses for bovine animals approved in accordance with Directive 64/433/EEC, and not enjoying a derogation under Article 2 of Directive 91/498/EEC, whatever their legal status, and

(b) livestock or meat traders who have slaughtering undertaken therein on their own account and who are entered in a public register under an individual number.

2. In response to invitations to tender, interested parties shall forward tenders to the intervention agencies of the Member States in which they are opened, either by lodging a written bid against a receipt or by any other written means of communication accepted by the intervention agency, with advice of receipt.

Separate tenders shall be submitted for each type of invitation to tender.

3. Interested parties may submit only one tender per category in response to each invitation to tender.

The Member States shall ensure that tenderers are independent of each other in the terms of their management, staffing and operations.

Where there are serious indications to the contrary or that tenders are not in line with economic facts, tenders shall be deemed admissible only where the tenderer presents suitable evidence of compliance with the second subparagraph.

Where it is established that a tenderer has submitted more than one tender, all the tenders from that tenderer shall be deemed inadmissible.

4. ...'

21 Finally, Article 8(1) of Regulation (EEC) No 729/70 of the Council of 21 April 1970 on the financing of the common agricultural policy (OJ, English Special Edition 1970 (I), p. 218) requires Member States to satisfy themselves that transactions financed by the EAGGF are executed correctly and are actually carried out, to prevent and deal with irregularities and to recover sums lost as a result of irregularities or negligence. Article 8(2) provides that the financial consequences of irregularities or negligence attributable to administrative authorities or other bodies of the Member States are not to be borne by the Community.

22 Between 1990 and 1992, as a result of a combination of various circumstances (mad cow disease (BSE), the reunification of Germany, the Gulf War, developments in relations with Eastern Europe, etc.), the Community beef market underwent an unprecedented crisis which, as from the financial year 1991, led to a consistent increase in Community budgetary expenditure. Community beef intervention purchases rose from 540 000 tonnes in 1987 to 1 030 000 tonnes in 1991, an increase of 90.7% in the space of four years.

23 According to the Commission, a number of undertakings had submitted several tenders in the context of a single tender procedure. In its 1992 Summary Report it stated:

'Italy

The EAGGF encountered an adjudication procedure not observed in any other Member State. Trade operators in the Italian beef market are grouped into three associations (consorzio) through which offers to sell into intervention are lodged,

i. e. the association receives offers from its members and submits them all at the same time to AIMA, the paying agency.

The Italian authorities, when criticised by the EAGGF on this point, volunteered the information that an association may even submit in its own name an overlapping global offer on behalf of those of its members which had not submitted individual offers.

Such practices are contrary to Article 9(6) of Regulation No 859/89 requiring Member States to guarantee the confidentiality of offers and negates the expected advantages of a genuine adjudication because it clearly reunites the interests of the supposed competitors.

The EAGGF also established in several instances links between tenderers by comparing the standard information (e. g. names, addresses, bank accounts, signatures, etc.).

Financial corrections are proposed at a flat rate of 2% applicable to expenditure declared for 1992.'

24 According to the Commission, those practices were expressly prohibited by the applicable Community rules and totally incompatible with the purpose of the intervention scheme. In its summary report, it found that, apart from failure to observe Article 9(6) (obligation to ensure the confidentiality of tenders), there had been infringement of Article 9(2) (submission of a single tender per tenderer in response to each invitation to tender), Article 12(2) (non-transferability of rights and obligations arising from the invitation to tender), Article 9(4)(c) (lodging of a security by the tenderer himself) and Article 15(1) (payment of the price to the tenderer) of Regulation No 859/89.

25 The Commission concluded that this practice had been adopted by tenderers in order to sell the greatest possible amount of meat into intervention at the highest possible prices, while significantly reducing the risk of losing their security. According to the Commission, where the quantity actually delivered was lower than that which should have been delivered, the splitting of one tender into several made it possible in fact to honour at least some of the tenders and therefore to recover the relevant securities.

26 The Commission draws a distinction between the term 'tenderer' as used in Article 9(1) of Regulation No 859/89 and the concept of 'interested parties' as used in Article 9(2). Whereas the tenderer is merely the person submitting a tender, the term 'interested party' covers a wider circle. In its view, the prohibition laid down in Article 9(2) of the regulation precluding tenderers from submitting more than one tender per category in response to each invitation to tender would be rendered redundant if it were possible for the same interested party to make several tenders through tenderers who are *de jure* separate but *de facto* connected.

27 The Italian authorities objected that Regulation No 859/89 did not authorise them to intervene where tenders were made by separate legal entities.

28 The Italian Government submits that the practice of accepting tenders from any legal entity during the relevant period was lawful. There was no legal basis in 1991 and 1992 for the national intervention bodies to reject offers made by separate legal entities on the ground that those entities were not independent of other tenderers.

29 The first point to be borne in mind here is the need to ensure legal certainty, which means that rules must enable those concerned to know precisely the extent of the obligations which they impose on them (see, to that effect, Case 348/85 *Denmark* v *Commission* [1987] ECR 5225, paragraph 19). The Commission thus cannot choose, at the time of the clearance of EAGGF accounts, an interpretation which

departs from and is not dictated by the normal meaning of the words used (see, to that effect, Case 349/85 *Denmark* v *Commission* [1988] ECR 169, paragraphs 15 and 16).

30 In this regard, the last sentence of Article 9(2) of Regulation No 859/89 merely provides that interested parties may submit one tender only per category in response to each invitation to tender. That wording cannot therefore provide any support for the interpretation claimed by the Commission that, on account of the difference in meaning between the words 'interested party' and 'tenderers', the latter may submit one tender only in response to an invitation to tender where they are part of a single group.

31 It is only since the entry into force of Regulation No 2456/93 that the Community rules have contained provisions on interconnections between tenderers. To uphold the interpretation of Article 9(2) of Regulation No 859/89 suggested by the Commission would be tantamount to applying Article 11 of Regulation No 2456/93 retroactively.

32 However, the contested decision does not fall to be annulled on the basis of the plea in law put forward by the Italian Government, since it contains other factual and legal grounds which provide it with a sufficient statement of reasons.

33 The EAGGF's 1992 Summary Report stated, first, that Italian trade operators were grouped into three associations through which offers to sell into intervention were lodged and submitted to the tendering authority and, secondly, that those associations were able to submit an overlapping global offer on behalf of those of its members which had not submitted individual offers. The EAGGF rightly considered that such practices were contrary to Article 9(6) of Regulation No 859/89, which requires the confidentiality of tenderers to be ensured.

34 Moreover, the EAGGF found that there had been an infringement of more than Article 9(2) of Regulation No 859/89. It also referred to the prohibition on the transfer of rights and obligations arising from the tender procedure (Article 12(2)) and the tenderers' obligation to lodge a security (Article 9(4)(c)) and to receive payment personally (Article 15).

35 The EAGGF was thereby alleging that Italian tenderers had breached the rule that tenders must be independent, an essential requirement for the validity and effectiveness of any tender procedure. Although that rule does not prevent several companies belonging to one group from taking part at the same time in one tender procedure, it does preclude those same companies from agreeing on the terms and conditions of the tenders which they each submit, if the tender procedure is not to be distorted.

36 In view of the foregoing considerations, the present plea in law must be rejected.

The corrections with regard to the public storage of beef

37 As noted above, the basic rules governing the intervention system are defined in Article 6 of Regulation No 805/68 and the detailed rules for the application of that system were contained, at the material time, in Regulation No 859/89. The beef eligible for buying-in in Italy was that included in the category defined in Article 3(1) of Council Regulation (EEC) No 1208/81 of 28 April 1981 determining the Community scale for the classification of carcases of adult bovine animals (OJ 1981 L 123, p. 3), that is to say, meat from uncastrated young male animals of less than two years of age.

38 The provisions of Article 4(2) and (3) of Regulation No 859/89 specify the conditions under which meat could be bought in. In particular, those applicable in the present case concern Community origin, compliance with health regulations, presentation in accordance with Annex III to the regulation, classification in accordance with the Community scale provided for in Regulation (EEC) No 1208/81 and markings.

39 Under that article, failure to comply with any one of the requirements relating to presentation, or a classification which is not in accordance with the Community scale, entails refusal to buy in the product.

40 Article 6(4) of Regulation No 859/89 provides that bone-in meat is to be wrapped in polyethylene or polypropylene suitable for wrapping foodstuffs and in cotton (stockinettes) or a synthetic material sufficiently resistant, in such a way that the meat is entirely covered by the said wrappings.

41 Article 22 of Regulation No 859/89 provides that boned cuts are to be packed in cartons containing a maximum net weight of 30 kilograms and Article 24 that boning, trimming and packing operations must be completed within eight working days following slaughter, although Member States may set shorter time-limits.

42 Article 20 makes the intervention agencies responsible for the supervision of all boning operations either by permanent physical control or by unannounced inspections of the boning operation not less than once per day and random examinations of the cartons of cuts before and after freezing.

43 Finally, account must be taken of the Commission's Belle Group Report, which lays down guidelines to be followed when financial corrections must be applied to a Member State. In addition to three principal calculation techniques, the Belle Group Report also sets out three categories of flat-rate corrections for difficult cases:

'A.2% of expenditure — where the deficiency is limited to parts of the control system of lesser importance, or to the operation of controls which are not essential to the assurance of the regularity of the expenditure, such that it can reasonably be concluded that the risk of loss to the EAGGF was minor.

B.5% of expenditure — where the deficiency relates to important elements of the control system or to the operation of controls which play an important part in the assurance of the regularity of the expenditure, such that it can reasonably be concluded that the risk of loss to the EAGGF was significant.

C.10% of expenditure — where the deficiency relates to the whole of or fundamental elements of the control system or to the operation of controls essential to assuring the regularity of the expenditure, such that it can reasonably be concluded that there was a high risk of widespread loss to the EAGGF.'

44 The guidelines further provide that, where there is doubt as to the correction to be applied, the following points are to be taken into account as mitigating factors:

'— whether the national authorities took effective steps to remedy the deficiencies as soon as they were brought to light;

— whether the deficiencies arose from difficulties in the interpretation of Community texts'.

45 It appears from the summary report on the results of inspections concerning the clearance of the EAGGF Guarantee Section accounts for 1992 and of certain expenditure for 1993 that the investigation carried out in 1990 and 1991 into the public storage of beef and veal in Italy showed that there were serious deficiencies in the organisation. It also appears from that report that the Azienda di Stato per gli Interventi nel Mercato Agricolo (the State intervention agency in the agricultural sector, hereinafter 'the AIMA') had in practice delegated responsibility for checks to the Associazione Italiana Allentori (Italian cattle breeders' association, hereinafter 'the AIA'), a trade association, without ascertaining whether the delegated responsibilities were properly carried out. The Commission inspectors also found that responsibility for boning operations had been entirely delegated to the intervention centres, without monitoring.

46 Those deficiencies were confirmed by the numerous anomalies detected both during the course of the inspections and upon certain meat products leaving storage as part of the humanitarian aid operation for Bulgaria and sales to the former Soviet Union and Brazil: removal of the health stamp from the quarters examined — which led to the conclusion that the goods were not of Community origin — purchase of products which were ineligible on account of their category, conformation class or degree of fat cover, numerous instances of reclassification of the goods by falsifying the classification of origin, acceptance of non-compliant goods, inadequate freezing, inadequate dressing, etc.

47 In those circumstances and taking into account the fact that it was impossible to determine with any certainty the quantum of the damage suffered by the EAGGF, the Commission decided to apply a flat-rate financial correction of 10% of the expenditure financed by the EAGGF in respect of 1990 and 1991.

48 The Italian Republic disputes the allegations made and considers that the correction applied is excessive.

The existence of the conduct complained of

49 The Italian Government points out first of all that the purchasing operations are monitored by employees of the relevant provincial offices of the AIA and by classifiers approved by the Comitato Bovini ('beef' committee) of the Ministry of Agriculture and Forests, who work directly with the AIA. Moreover, both are required to follow clear rules and are directly answerable to the AIA and the Comitato Bovini.

50 The Italian Government explains that monitoring of the boning operations is carried out, in accordance with the law, by the relevant health authorities, through official veterinary surgeons of the Unità Sanitarie Locali (local health units), who are required to check, in particular, the health documents which accompany the meat products, the health stamps, the origin, the category to which they belong and the purchase stamps affixed by the AIMA.

51 It formally denies that the AIA delegated responsibility for storage and deboning to private operators referred to as 'intervention centres'. The legal relationship between the AIA and the firms which operate the cold storage depots and boning centres is contractual in nature. Moreover, it is the AIA itself which has full use of such facilities, since they are entered in the AIMA storekeepers' register as AIA centres.

52 The Italian Government maintains that the generalisation made in the summary report with regard to the anomalies found by the Commission's staff during the inspections at various intervention centres is unacceptable, since, it states, they in fact relate to isolated cases which had no impact on the Community budget. It is moreover of the view that the sample tested in 1990 and 1991 by the Commission's inspectors was not representative of the product stored in intervention since it concerned only 0.15% of the meat in storage.

53 It is surprised by the EAGGF's findings (bruising, absence of the health stamp of origin, presence of veal, ineligible conformation, falsification of the original classification etc.), given that the Italian authorities have never found any such irregularities. It adds that purchasers never complained about the inadequacy of the dressing of quarters or about soiling.

54 The Italian Government also complains that the findings and assessments made by the Commission rely, in part, on purely subjective parameters (the presence of pelvic fat, inadequate jugular trimming, muscle development, degree of fat cover etc.). It submits that the national authorities had not found any of the irregularities complained of or, at least, not on the scale described by the Commission.

55 So far as concerns the inadequacies in wrapping, the Italian Government observes that Article 6(4) of Regulation No 859/89 does not describe the characteristics of the 'stockinettes'. In any event, the use of too light a stockinette or no stockinette at all would be detrimental for the AIMA, the AIA and the approved centres inasmuch as it would exacerbate the reduction in weight of the meat by nearly 0.5%. Given that the penalty provided for by the EAGGF for a reduction in weight beyond the tolerated level is more than twice the cost per kilo of the stockinette, the need to minimise the purchase price is largely cancelled out by the need to use a sufficiently resistant material.

56 Next, with regard to the irregularities found upon the removal from storage of goods intended for export to Bulgaria, the former Soviet Union and Brazil, the Italian Government contends that the sales in question were never formally objected to either by the recipients of the aid or by the purchasers.

57 Finally, the Italian Government complains of the EAGGF's delay (of more than two years) in notifying it of the irregularities found during the investigation.

58 As the Court has already observed, only intervention undertaken in accordance with the Community rules within the framework of the common organisation of agricultural markets is to be financed by the EAGGF (see Case C-48/91 *Netherlands* v *Commission* [1993] ECR I-5611, paragraph 14). In that context, it is for the Commission to prove an infringement of the rules on the common organisation of the agricultural markets (see Case 347/85 *United Kingdom* v *Commission* [1988] ECR 1749, paragraph 16; Case C-281/89 *Italy* v *Commission* [1991] ECR I-347, paragraph 13; Case C-55/91 *Italy* v *Commission* [1993] ECR I-4813, paragraph 13; and Case C-48/91, cited above, paragraph 18). Accordingly, the Commission is obliged to give reasons for its decision finding an absence of, or defects in, inspection procedures operated by the Member State in question (Case C-8/88 *Germany* v *Commission* [1990] ECR I-2321, paragraph 23).

59 The Member State, for its part, cannot rebut the Commission's findings by mere assertions which are not substantiated by evidence of a reliable and operational supervisory system. If it is not able to show that they are inaccurate, the Commission's findings can give rise to serious doubts as to the existence of an adequate and effective series of supervisory measures and inspection procedures (see, to that effect, Case C-8/88 *Germany* v *Commission*, cited above, paragraph 28).

60 In this connection it should be pointed out in the first place that the Commission has stated that it checked all the intervention centres in 1990 and inspected 15 out of 35 in 1991, a statement which has not been challenged by the Italian Government. The Commission claims to have found the same shortcomings at all those centres.

61 Secondly, the Italian authorities have not provided any evidence of any instructions given by the AIMA in order to ensure that the intervention operations were fully in accordance with Community rules. Neither have they stated whether on-the-spot inspections were made in order to verify the methods employed by the AIA in carrying out and administering buying-in operations or, if so, how many, how frequently or on what criteria those inspections were carried out. They have made no mention of the measures implemented to ascertain whether the product was properly stored. Finally, they have provided no particulars concerning the results of such monitoring.

62 Since with regard to many of the allegations the Italian Government has confined itself to stating that inspections were carried out, and in certain cases has not even denied the allegations (in particular with regard to the affixing of counterfeit stamps) or relies on the fact that no complaint was made, the first plea in law must be rejected.

Infringement of the guidelines laid down in the Belle Group Report

63 By its second plea in law, the Italian Government claims that, if the Commission had made proper use of its discretion, it would have decided upon a reduction of only 5%.

64 First, the checks carried out by the Commission are not representative. Secondly, the Italian Republic made improvements to the system, which are moreover

acknowledged in the summary report, and the guidelines provide that, when setting the correction to be applied, account should be taken of the improvements made by the Member State to the system as soon as deficiencies are brought to light.

65 It must be observed first of all that, where the Commission, instead of rejecting all the expenditure affected by the infringement, has endeavoured to establish the financial impact of the unlawful action by means of calculations based on an assessment of what the situation on the relevant market would have been if the infringement had not occurred, the burden of proving that those calculations are not correct rests on the Member State (Case 347/85 *United Kingdom* v *Commission*, cited above, paragraph 15).

66 In this connection, it should be pointed out that what counts is not the number of random inspections carried out by the Commission but the frequency and effectiveness of the inspections for which the Italian Republic is responsible. As the deficiencies, which are numerous, concern the system as a whole — since the AIMA was not able to show that it monitors the tasks it has entrusted to the AIA — a 10% reduction appears justified pursuant to the Belle Group Report guidelines.

67 The improvements relied upon by Italy were not introduced until 1993, and thus could not be taken into consideration when clearing the accounts for 1992.

68 In view of the foregoing considerations, the second plea in law must be rejected.

The corrections with regard to the ewe premium

69 Article 5 of Council Regulation (EEC) No 3013/89 of 25 September 1989 on the common organisation of the market in sheepmeat and goatmeat (OJ 1989 L 289, p. 1) provides for the granting of a premium to sheepmeat and goatmeat producers to the extent necessary to offset an income loss in the Community during a marketing year.

70 The summary report analyses in detail the deficiencies found by EAGGF staff, in the course of inspections to verify the applications for premiums in respect of 1992 in the control procedures introduced by the Italian authorities with a view to ensuring the proper application of the system. In particular, the EAGGF found that the application files were inadequately checked, certain inspection files were unreliable and that there was no cross-checking of data contained in the applications with the findings arising from on-the-spot inspections.

71 Those inspections followed the audits conducted in Italy from 1988 and entailing, in previous years, significant financial corrections applied to the expenditure charged to the Community budget (up to 30% of national expenditure for 1991).

72 The deficiencies in the administrative and control procedures resulted, also in respect of 1992, in the payment of premiums in many cases where the applications lodged by producers should have been wholly or partly refused.

73 For those reasons the Commission decided, when clearing the accounts, to apply a flat-rate financial correction of 10% of the national expenditure for the 1992 marketing year.

74 The Italian Government denies the EAGGF's allegations. Similar complaints had already been made in previous Commission inspections, which prompted the Italian authorities to be more rigorous from 1992 and to modify the whole system radically in 1993. According to the Italian Government, those initiatives should have led the Commission to propose the minimum 2% flat-rate correction instead of the maximum rate of 10%.

75 It must be observed first of all that, where the Commission, instead of rejecting all the expenditure affected by the infringement, has endeavoured to establish the financial impact of the unlawful action by means of calculations based on an assessment of what the situation on the relevant market would have been if the infringement had not occurred, the burden of proving that those calculations are not correct rests on the Member State (Case 347/85 *United Kingdom* v *Commission*, cited above, paragraph 15).

76 So far as concerns any increased rigour demonstrated by the national authorities from 1992, it should be noted that, as the Advocate General rightly observed at point 119 of his Opinion, such improvements are to be taken into account only where there are doubts concerning the three flat-rate corrections to be applied. In this case, however, there was no such uncertainty. Because of the seriousness and scale of the irregularities found, and of the extent to which supervision was largely ineffective, the EAGGF remained, in all events, exposed to a serious financial risk.

77 The reforms referred to by the Italian Government were introduced only as from 1993, and may thus not be taken into account in the context of the clearance of the accounts for 1992.

78 Since the 10% correction decided upon by the Commission does not therefore appear unjustified, the present plea in law must be rejected.

The correction with regard to public storage of cereals

79 Regulation (EEC) No 2727/75 of the Council of 29 October 1975 on the common organisation of the market in cereals (OJ 1975 L 281, p. 1) lays down the basic rules for the intervention scheme.

80 The procedure and conditions for the taking-over of cereals by intervention agencies were contained in Commission Regulation (EEC) No 1569/77 of 11 July 1977 (OJ 1977 L 174, p. 15). That regulation was repealed by Commission Regulation (EEC) No 689/92 of 19 March 1992 (OJ 1992 L 74, p. 18), which entered into force on 1 July 1992.

81 According to the summary report, the EAGGF commenced an audit of public storage arrangements for cereals in Italy as part of the 1991 accounts clearance, supplemented by an inquiry concerning intervention stocks in 1993. That inspection revealed serious shortcomings in the administration and control system put in place to that end by the national authorities, which were essentially attributable to the fact that all the cereal purchase and storage operations were entrusted to 'organismi assuntori', private undertakings under contract to the AIMA; however, the intervention agency exercised no control over their activity or over proper performance of the contract. The inspections also brought to light the inadequacies of control of stocks which were kept in what proved to be often poor conditions, resulting in storage costs being charged to the EAGGF to no purpose. Finally, the summary report points out that collaboration between the AIMA and the other competent national authorities was almost non-existent.

82 In those circumstances, the Commission applied a financial correction of 10% of the expenditure declared as technical costs and financial charges and 5% of the expenditure declared as other costs, amounting to ITL 10 082 336 246.

83 The Italian Government observes that, since it does not have its own facilities for storing products delivered into intervention, the Ente per gli Interventi nel Mercato Agricolo (the amended designation of the Italian intervention agency in the agricultural sector, hereinafter 'the EIMA') called on external operators to carry out intervention operations. It entered into a specific contract with them laying down the conditions for the provision of storage services.

84 The register of storage bodies includes, for each commercial sector, the names of operators recognised, after checking their technical, financial and administrative capability, as capable of carrying out the tasks and missions provided for by the Community rules on behalf of the intervention agency.

85 The Italian Government acknowledges that the undertakings did not always correctly fulfil the tasks entrusted to them, and that even, 'in certain cases, serious administrative irregularities were found which led the EIMA to amend the rules governing the storage contracts'. None the less, in view of the new rules on the implementation of intervention measures adopted in June 1994, the Italian Government considers the application of a financial correction of 10 and 5% to be excessive. It submits that, in previous similar cases, the Commission had always applied considerably lower reduction percentages.

86 For the same reasons as those set out in paragraphs 75 to 77, the correction does not appear unjustified.

87 This plea in law must therefore be rejected.

The correction with regard to set-aside of arable land

88 The aid scheme to encourage the set-aside of arable land was introduced by Article 1a of Council Regulation (EEC) No 797/85 of 12 March 1985 on improving the efficiency of agricultural structures (OJ 1985 L 093, p. 1), as inserted by Council Regulation (EEC) No 1094/88 of 25 April 1988 (OJ 1988 L 106, p. 28). Under that provision, the scheme covers all arable land, irrespective of the crops grown, provided that the land has in fact been cultivated for a reference period to be determined. The measure therefore consists in withdrawing from cultivation agricultural land previously used as arable land.

89 The detailed rules for the application of the scheme are contained in Commission Regulation (EEC) No 1272/88 of 29 April 1988 (OJ 1988 L 121, p. 36). Article 2(1) provides, in particular, that arable land should be taken to mean the types of land listed in section D of the Annex to Regulation (EEC) No 571/88 of 29 February 1988 on the organisation of Community surveys on the structure of agricultural holdings between 1988 and 1997 (OJ 1988 L 56, p. 1) with the exception of land intended to be laid fallow (point D/21 of the Annex). In addition, under Article 3 of Regulation No 1272/88, the reference period during which arable land was effectively cropped — outwith which the land cannot benefit from the aid to encourage the set-aside of arable land — was to span not less than one marketing year between 1 July 1985 and 30 June 1988. For Italy, that period was the 1987/88 marketing year.

90 The rules introduced by Regulation No 797/85 were replaced by those contained in Council Regulation (EEC) No 2328/91 of 15 July 1991 on improving the

efficiency of agricultural structures (OJ 1991 L 218, p. 1) which consolidated the numerous amendments to Regulation No 797/85.

91 It is apparent from the summary report that the EAGGF checks found that, in Sicily, a large number of areas withdrawn from production in pursuance of the multiannual set-aside scheme was in fact land subject to traditional fallow practices. The inspection also showed that the Italian authorities had failed to check that aspect of the eligibility of the land. The aim of the scheme, to reduce production, was therefore only partly met.

92 In view of the deficiencies of the Italian authorities' control system the Commission applied, in respect of the 1992 financial year, a financial correction of 5% — instead of 10% as it had proposed — of the expenditure declared for Sicily, the region in which the irregularity had been found. The proposed correction was reduced in order to take account of the conclusions of the Conciliation Body consulted pursuant to Commission Decision 94/442/EC of 1 July 1994 setting up a conciliation procedure in the context of the clearance of the accounts of the European Agricultural Guidance and Guarantee Fund (EAGGF), Guarantee Section (OJ 1994 L 182, p. 45). Those conclusions concerned, in particular, the rigour of the controls concerning the other procedures for the implementation of the scheme.

93 The Italian Republic challenges the lawfulness of the financial correction. It argues that the traditional practice of laying land fallow was replaced, with effect from the reference marketing year, by the practice of 'green fallow'. That practice, which is associated with such autumn/spring early crops as leguminous plants grown as a forage, broad beans, chickpeas and potatoes, consists in keeping the land under cultivation for limited periods and then as usual preparing the ground by ploughing in the crops produced (green manuring of fallow ground).

94 It should first of all be observed that the Italian Republic does not deny having failed to check whether the land allegedly set aside had in fact previously been cultivated or, at least, whether it had been cultivated in the context of bastard fallow.

95 Furthermore, it did not adduce any evidence that the traditional fallowing practice had been replaced by 'green fallow'.

96 On the contrary, the data collected through the network for the collection of farming accountancy data at Community level (Regulation No 79/65/EEC of the Council of 15 June 1965 setting up a network for the collection of accounting data on the incomes and business operation of agricultural holdings in the European Economic Community (OJ, English Special Edition, 1965-66, p. 70)) show that that was still the practice in 1986 and 1987. Moreover, according to a letter from the EAGGF dated 2 August 1994, during farm inspections the farmers directly concerned had contradicted, at least in so far as concerns Sicily, the Italian authorities' claim that traditional fallowing was no longer farming practice.

97 The present plea must therefore be rejected.

The correction with regard to the reimbursement of costs of public storage of sugar

98 The common organisation of the markets in the sugar sector is covered by Council Regulation (EEC) No 1785/81 of 30 June 1981 (OJ 1981 L 177, p. 4). Article 8 of that regulation provides for a compensation system for storage costs in respect of certain types of sugar products manufactured from beet or cane of Community

origin. Those costs are to be reimbursed to the organisation storing the product at a single, flat rate throughout the Community; the system is to be financed by means of a levy imposed on sugar producers in respect of the quantities produced by each of them, also at a single rate throughout the Community.

99 The rules are laid down in Council Regulation (EEC) No 1358/77 of 20 June 1977 laying down general rules for offsetting storage costs for sugar and repealing Regulation (EEC) No 750/68 (OJ 1977 L 156, p. 4). Article 2 of that regulation specifies who is to be reimbursed and Article 3 provides that reimbursement is to be made by the Member State in whose territory the sugar is stored: those concerned are any sugar manufacturer to whom a basic quota has been allocated, any intervention agency, and also any specialised and approved sugar refiner, manufacturer of powdered, lump or candy sugar or sugar trader. Reimbursement is made to them provided that they are the owners of the sugar or of the syrups held in store. Moreover, since reimbursement cannot be granted unless some measure of control is possible, Article 3 provides for the prior approval of the stores by the State in which they are located.

100 Articles 4 and 5 of Regulation No 1358/77 specify the manner in which the reimbursement is to be calculated and fixed: in particular, the calculation must be carried out based on monthly returns of quantities in store, established by calculating the arithmetic mean of the quantities held in store at the beginning and at the end of the month in question; the amount of the reimbursement is then fixed, financing, insurance and specific storage costs being taken into consideration.

101 In accordance with the principle of financial neutrality which underlies the system (see the third recital in the preamble to Regulation No 1358/77), Article 6(1) of that regulation provides that the levy to be collected from each sugar manufacturer in respect of the quantities produced is to be so fixed that, for any sugar marketing year, the estimated total of the levies should be equal to the estimated total of the reimbursement. Article 6(2) provides that, when, for any sugar marketing year, the total of levies collected is not equal to the total of the reimbursement made, the

difference is to be carried forward to a subsequent sugar marketing year. Finally, Article 6(3) specifies the method for calculating the amount of the levy: the total estimated reimbursement for the sugar marketing year in question is to be increased or decreased as the case may be by the amounts carried forward under Article 6(2); the result is to be divided by the estimated quantity of sugar which will be marketed during that marketing year and produced within the maximum quotas.

102 On the basis of those principles, Commission Regulation (EEC) No 1998/78 of 18 August 1978 laying down detailed rules for the offsetting of storage costs for sugar (OJ 1978 L 231, p. 5) laid down new implementing rules.

103 That regulation made reimbursement subject to certain conditions, in particular the 'substantial participation in storing' (second recital) of manufacturers, refiners, manufacturers of powdered, lump or candy sugar and specialised sugar traders. Because of the complexity of the mechanism, it was also necessary to provide for supervisory measures and procedures for it to work properly, in particular by restricting the approval of stores depending on facilities for accounting and supervision, since sugar of different origins may be stored on the same premises (Articles 14 and 14b) or by providing that the product is ineligible for reimbursement when certain operations (flavouring, colouring or mixing) are carried out.

104 It should also be observed that Article 12 provides that the levy is to be incurred by manufacturers at the moment of disposal. For the purposes of Article 12(1)(a) to (f) 'disposal' means: exit of the sugar from the factory or from the approved warehouse of the manufacturer; transfer of the property rights to the sugar without exit of the sugar from the approved warehouse of the manufacturer; processing of the sugar in various ways; and denaturing of the sugar.

105 Finally, Article 19 requires Member States to take all measures necessary for the application of the regulation. In particular, they are to establish all the necessary control measures.

106 The monitoring missions, in particular the on-the-spot inspections, carried out by the EAGGF in 1994 to check the systems applied in Italy in the context of the measures for reimbursement of storage costs for sugar, revealed that, until 31 December 1992, the competent organisations in Italy (in particular the communes) had not carried out any checks on specialised traders or other approved independent stores. Moreover, the EAGGF also found that no checks on those beneficiaries had been carried out by the AIMA.

107 In view of the high degree of risk for the Community budget, the Commission applied a financial correction of 10% to the payments to operators in those categories in respect of the 1991/92 marketing year, amounting to ITL 391 281 020.

108 The Italian Government claims first of all that the periods to which the Commission's financial corrections refer — that is to say 1992, but also 1993, which does not fall within the scope of the contested decision — were special transitional stages. From March 1991 the AIMA took over all the administrative aspects of the system, which until then had been the responsibility of the Cassa Conguaglio Zucchero, and, from 1 January 1993, after the abolition of the tax on manufacture, the supervisory function which had been carried out by the Uffici Tecnici Imposta di Fabbricazione (UTIF).

109 That being the case, the Italian Government observes that an administrative control system had been introduced in respect of specialised traders. Though not applied on the spot, it should be considered particularly intensive and relevant for the quantification of sugar stocks.

110 Next, on the basis of the overall operation of the common organisation of the market in the sugar sector, the Italian Government denies that the sugar sector in Italy was 'high risk'. It relies, first, on the limits imposed on traders in the sector by the manufacturing quotas and, secondly, on the link between the amounts of the levy paid by the sugar manufacturers and the reimbursements made in respect of storage costs.

111 It argues that, as result of that link, acceptance that the levy accounts are reliable automatically implies that the reimbursements have also been properly accounted for and paid. To call into question the storage costs accounts would therefore conflict, in the Italian Government's view, with the acceptance of the levy accounts. The accounts for specialised traders are also affected by that close link between manufacture, disposal and storage.

112 Finally, the Italian Government argues that, to the extent that Community legislation does not specify either the frequency or the method of control, it is difficult, unless actual economic damage is proved, to state with any certainty that the controls instituted are not effective.

113 It should be observed first of all that, by failing to carry out on-the-spot checks on specialised traders during the period scrutinised by the Commission, the Italian Republic has failed to fulfil its supervisory obligations under Community rules.

114 It cannot be contended that such an obligation is not expressly laid down in the relevant regulations. The Court has consistently held that it is apparent from Article 8(1) of Regulation No 729/70 that Member States are under a general obligation to take the measures necessary to satisfy themselves that the transactions financed by the EAGGF are actually carried out and are executed correctly, even if the specific Community act does not expressly provide for the adoption of particular supervisory measures (see Case C-8/88 *Germany* v *Commission*, cited above,

paragraphs 16 and 17, and Case C-2/93 *Exportslachterijen van Oordegem* v *Belgische Dienst voor Bedrijfsleven en Landbouw* [1994] ECR I-2283, paragraphs 16 to 18).

115 That requirement is, moreover, reiterated in Article 19 of Regulation No 1998/78.

116 Those provisions must be viewed in the light of the duty to cooperate in good faith with the Commission, established by Article 5 of the EC Treaty, which, with particular regard to the utilisation of Community resources, requires Member States to set up comprehensive administrative checks and on-the-spot inspections, thus guaranteeing the conformity of financial operations with Community law. Consequently, if, as in the present case, no comprehensive system exists or if the system introduced gives rise to doubts as to compliance with the conditions imposed for eligibility for the reimbursement of the expenditure concerned, the Commission is entitled to disallow certain expenditure incurred by the Member State in question (see Case C-8/88 *Germany* v *Commission*, cited above, paragraphs 16 to 21).

117 The argument which the Italian Government seeks to derive from the link between the amounts of the levy paid by the sugar manufacturers and the reimbursements made in respect of storage costs must also be rejected.

118 Although the compensation system is indeed based on the principle of financial neutrality in that the levies collected must be equivalent to the reimbursement paid, as is evident from Article 6(2) of Regulation No 1358/77 and the case-law of the Court of Justice (see Case 121/83 *Zuckerfabrik Franken* v *Hauptzollamt Würzburg* [1984] ECR 2039, paragraph 26), that balance must be achieved at Community level and not at the level of the Member State or the undertaking concerned as the Advocate General has indicated at points 138 and 140 of his Opinion.

119 Traders who pay the levy are not, moreover, necessarily the same as those who receive the reimbursement. The latter include specialised traders who are not liable for the levy. Moreover, even so far as concerns manufacturers, the two amounts, fixed according to the manufacturing quota allocated to them and to the duration of storage respectively, do not automatically coincide.

120 That is why the Member States must introduce adequate inspection procedures in order to check whether the storage costs eligible for reimbursement have actually been incurred. The absence of such procedures, or deficiencies therein, could allow certain traders to obtain reimbursement for fictitious costs, which would obviously lead to distortions of competition, to the detriment in particular of traders in other Member States where the control system does conform to the requirements of the Community rules.

121 The objection raised by the Italian Government that no damage to the Community has been established fails to take account of the rules concerning the onus of proof.

122 As the Court has consistently held, Articles 2 and 3 of Regulation No 729/70 permit the Commission to charge to the EAGGF only sums paid in accordance with the rules laid down in the various sectors of agricultural production, leaving the Member States to bear the burden of any other sum paid, and in particular any amounts which the national authorities wrongly believed themselves authorised to pay in the context of the common organisation of the markets (Case 11/76 *Netherlands* v *Commission* [1979] ECR 245, paragraph 8; Case 18/76 *Germany* v *Commission* [1979] ECR 343, paragraph 7; and Case C-48/91 *Netherlands* v *Commission*, cited above, paragraph 14).

123 Although it is therefore for the Commission to prove an infringement of the Community rules, the Member State concerned must demonstrate that the Commission committed an error as to the financial consequences to be attributed to it (see, to this effect, Case 49/83 *Luxembourg* v *Commission* [1984] ECR 2931, paragraph 30).

124 Moreover, as the Court has consistently held, the Commission, instead of seeking to establish the financial impact of the failure of the Italian monitoring authorities to fulfil their obligations, could have rejected the entire expenditure tainted by the infringement (see Case 347/85 *United Kingdom* v *Commission*, cited above, paragraph 13).

125 The correction adopted by the Commission thus does not appear to be unjustified.

126 In those circumstances, in view of all the foregoing considerations, the application brought by the Italian Republic must be dismissed.

Costs

127 Under the first sentence of Article 69(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 Italian Republic has been unsuccessful, it must be ordered to pay the costs.

On those grounds,

THE COURT (Fifth Chamber)

hereby:

1) Dismisses the application;

2) Orders the Italian Republic to pay the costs.

Gulmann Wathelet Moitinho de Almeida

Puissochet Sevón

Delivered in open court in Luxembourg on 1 October 1998.

R. Grass C. Gulmann

Registrar President of the Fifth Chamber