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Archwilydd Cyffredinol Cymru
Auditor General for Wales

Managing the Impact of Brexit on the Rural Development Programme for Wales

WALES AUDIT OFFICE
SWYDDFA ARCHWILIO CYMRU

This report has been prepared for presentation to the National Assembly under the Government of Wales Act 1998.

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Mae’r ddogfen hon hefyd ar gael yn Gymraeg.

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Summary report

Summary

1 The European Union's Common Agricultural Policy (CAP) provides funding to support farmers, the countryside and rural communities. It has two 'pillars'. Pillar 1, called the European Agricultural Guarantee Fund (EAGF), is a direct payment to subsidise farmers amounting to approximately £211 million[1] annually. Pillar 2, called the European Agricultural Fund for Rural Development (EAFRD), is delivered through a Rural Development Programme designed by each UK administration and approved by the European Commission (EC). This report focuses on this element of 'Rural Development funding' under the Welsh Government's Rural Communities - Rural Development Programme (RDP)[2].

2 Since 2000, Wales has been eligible for €1,143m (approximately £972 million) of EU Rural Development funding. Wales is eligible for around £522 million under the current round which forms the 2014-2020 Rural Development Programme, although EU rules mean Wales would actually have until 2020 to commit[3], and until 2023 to spend and claim the funding[4]. The Welsh Government currently plan to contribute an additional £252 million of 'co-financing'[5] taking the the overall value of the current programme to £774 million.

1 For the purposes of this report we have used GBPs throughout. Where values were only available in Euros we have used the Welsh Government's current planning exchange rate – 0.85 GBP to 1.00 Euro. Exchange rates will have varied over time, and so there may be variations in the same values quoted elsewhere.

2 **gov.wales/docs/drah/publications/170705-wales-rdp-2014-2020-document.pdf**

3 For this report, we mean that the funding is committed to a specific project following approval by the Welsh Government and signed acceptance of the grant offer letter by the project sponsor.

4 The RDP includes annual allocations of funding across the programme period (2014-2020), which total the full value of the EAFRD funds. The annual allocations cannot be exceeded but the Welsh Government have a further three years (known as N+3 or decommitment principle) from each allocation within which they can commit, spend and claim the funds. N+3 targets are cumulative and rise each year to 100% of funding which must be spent by 2023.

5 'Co-financing' is the domestic funding provided by the Welsh Government to deliver the Rural Development Plan in Wales. EC Regulations stipulate a maximum and minimum percentage of funding that can come from the EC depending on the type of funding, the type of scheme and the location of the beneficiary of funding. Within these parameters, the exact percentage of domestic and EC funding is put forward by the UK administration, agreed by the EC and set out in their Rural Development Programme.

3 The EU has set six overall priorities for the funding. These are underpinned by generic EU 'focus areas' and 'measures' through which the priorities will be achieved (Box 1). The Welsh Government produces a Rural Development Programme document which sets out how it will use the funding to achieve these priorities. The Welsh Government sets up a range of schemes, which farmers or organisations can apply to. Each successful application becomes a project for the purposes of the EU rules. Part 2 of this report sets out the process in more detail.

Box 1 – Rural Development Programme 2014-2020 structure	
EU Priorities	Member States and regions draw up their rural development programmes based on the needs of their territories and ensuring that at least four of the following six common **EU priorities** are addressed: • fostering knowledge transfer and innovation in agriculture, forestry and rural areas; • enhancing the viability and competitiveness of all types of agriculture, and promoting innovative farm technologies and sustainable forest management; • promoting food chain organisation, animal welfare and risk management in agriculture; • restoring, preserving and enhancing ecosystems related to agriculture and forestry; • promoting resource efficiency and supporting the shift toward a low-carbon and climate-resilient economy in the agriculture, food and forestry sectors; and • promoting social inclusion, poverty reduction and economic development in rural areas.

Box 1 – Rural Development Programme 2014-2020 structure	
Focus Areas	The rural development priorities are broken down into 'focus areas'. For example, the priority on resource efficiency includes focus areas 'reducing greenhouse gas and ammonia emissions from agriculture' and 'fostering carbon conservation and sequestration in agriculture and forestry'. Within their RDPs, Member States or regions set quantified targets against these focus areas. They then set out which measures they will use to achieve these targets and how much funding they will allocate to each measure.
EU Measures	The RDP sets out a selection of measures drawn from the Rural Development Regulation to address the EU priorities and focus areas. A measure is a set of specific activities or investment, eg investment in physical assets.
Welsh Government Schemes	Schemes are devised by the Welsh Government (or other member state or region) to satisfy the EU measures. A scheme is essentially a framework of activities set by the Welsh Government designed to achieve the generic EU measures. These are translated into 'scheme rules' advertised to individuals or organisations to apply for funding under the specific scheme.
Applicants' Projects	Applications for specific projects are submitted to the Welsh Government who assess the proposed activities against the scheme rules and accept or reject the project.

Exhibit 1 – key facts about the 2014-2020 Rural Development Programme

EUROPEAN AGRICULTURAL FUND FOR RURAL DEVELOPMENT

EU FUNDING = £522 MILLION

DOMESTIC CO-FINANCING = £252 MILLION

Priority	Total Expenditure	EU Grant	Focus areas
Knowledge transfer and innovation*			Innovation and cooperation; Links with research and innovation; Lifelong learning and vocational training
Competitiveness	£97M	£65M	Farms performance, restructuring and modernisation; Entry of skilled/younger farmers
Food chain and risk management	£87M	£53M	Agri-food chain integration and quality
Ecosystems management	£329M	£250M	Biodiversity's restoration, preservation and enhancement; Water management; Soil erosion and soil management
Resource efficiency and climate	£68M	£40M	Energy use efficiency investment; Renewable energy and waste management investment; Greenhouse gas and ammonia emissions reduction; Carbon conservation and sequestration
Social inclusion and local development	£165M	£97M	Diversification and job creation; Improved services/infrastructure; Improved ICT
Technical assistance	£31M	£17M	Audit and controls; Evaluation and monitoring

*Note: This priority is considered cross cutting.
The allocation under priorities 2-6 contributes to the achievement of Priority 1 targets.

Figures based on first modification of RDP extant at time of publication, converted at an exchange rate of €1: £0.8

Source: Welsh Government website

4 On 23 June 2016, the UK voted in a referendum to leave the European Union. In March 2017, the UK Government served notice of its intention to leave the EU. In line with the two-year timetable set out under EU law, the UK will leave the EU at 11pm on 29 March 2019.

5 The impact of Brexit on the EU Rural Development Funding depends on whether the UK leaves the EU with a 'deal' or not. EU law allows for the UK and EU to agree a 'Withdrawal Agreement' which sets out the terms of the UK's departure. In March 2018, the UK and EU published a draft Withdrawal Agreement. The draft Withdrawal Agreement set out a range of areas where the UK and EU agree as well as some key areas of disagreement. Among the areas of agreement are that the UK will continue to participate in the 2014-2020 EU Rural Development Programme until its end.

6 On 14 November 2018 the UK and EU published a revised draft Withdrawal Agreement. However, at the time of drafting the revised agreement has not been formally approved by the EU or the UK, and there remains a chance that the UK will leave the EU without a Withdrawal Agreement. In a no deal scenario, Wales will have to rely on a UK Government guarantee, announced in October 2016[6], to replace EU funding for projects that have been 'signed before the UK leaves the EU'. During drafting of this report, in late July 2018, the UK Government announced that it was then extending its guarantee of EU funding to cover Rural Development Programme contracts signed before the end of December 2020. Exhibit 2 sets out at a high level the two key scenarios – 'deal' and 'no deal'.

6 In August 2016, the UK Government announced an initial guarantee to fund projects signed before the Chancellor's Autumn Statement. The October 2016 announcement preceded the Autumn Statement and extended the guarantee to all projects signed before the UK leaves the EU.

Exhibit 2 – UK/EU Withdrawal agreement – latest deal and no deal scenarios for Rural Development Programme in Wales

7 This report considers whether the Welsh Government is effectively managing the risks and opportunities for the Rural Development Programme posed by Brexit.

8 Appendix 1 sets out our audit methods. This report focuses at a high level on the key risks. We have not reviewed the overall management of the programme in depth. Nor have we reviewed the Welsh Government's broader response to the risks and opportunities of Brexit.

9 The report is structured around the key risks to EU funding and opportunities as a result of Brexit. Exhibit 3 sets out the key risks and opportunities and our conclusions in relation to how the Welsh Government is managing them.

Exhibit 3 – key risks and opportunities related to EU Rural Development Funds in Wales as a result of Brexit

Risk/ opportunity	Conclusion
Key risk: that Wales loses out substantially on funding.	The Welsh Government faced financial risk had the UK Government not amended the terms of its post Brexit funding guarantee.
Key risk: that the Welsh Government does not have robust governance and control arrangements in place to effectively manage the Rural Development Programme through Brexit.	The Welsh Government has checks and balances to ensure that it complies with strict EU rules, but needs to strengthen scrutiny and risk management of the overall RDP.
Key opportunity: to apply lessons learnt from years of managing the EAFRD fund in Wales to any replacement scheme.	The future of agricultural funding post-Brexit is unclear but the Welsh Government are trying to shape debate and have set out what they want future arrangements to look like.

10 We make the following key recommendations for the Welsh Government:

a The current scrutiny arrangements for the management and delivery of the RDP should be improved. A scrutiny forum should allow sufficient attention for the detailed consideration of the programme by informed and engaged members based on clear and accurate information. In particular, the reporting and consideration of 'commitments' should be clear.

b Risk management arrangements for the RDP should be clarified and documented so that officers and departments understand their responsibilities and to ensure that all risks with the RDP, and in particular in the context of Brexit, are appropriately identified and managed.

11 In addition to the recommendations made above, there are also some key issues for the Department to continue to manage even with the extension of the guarantee:

a keeping in view wider economic changes, including in relation to Brexit, and adapting the programme where necessary in response;

b Increasing the rates of commitment, working with potential project sponsors to address concerns, including around the availability of match-funding;

c Increasing the rate of spending by encouraging projects to submit their claims for EU funding more promptly;

d Working with beneficiaries to minimise project underspends that could result in funding being lost to Wales;

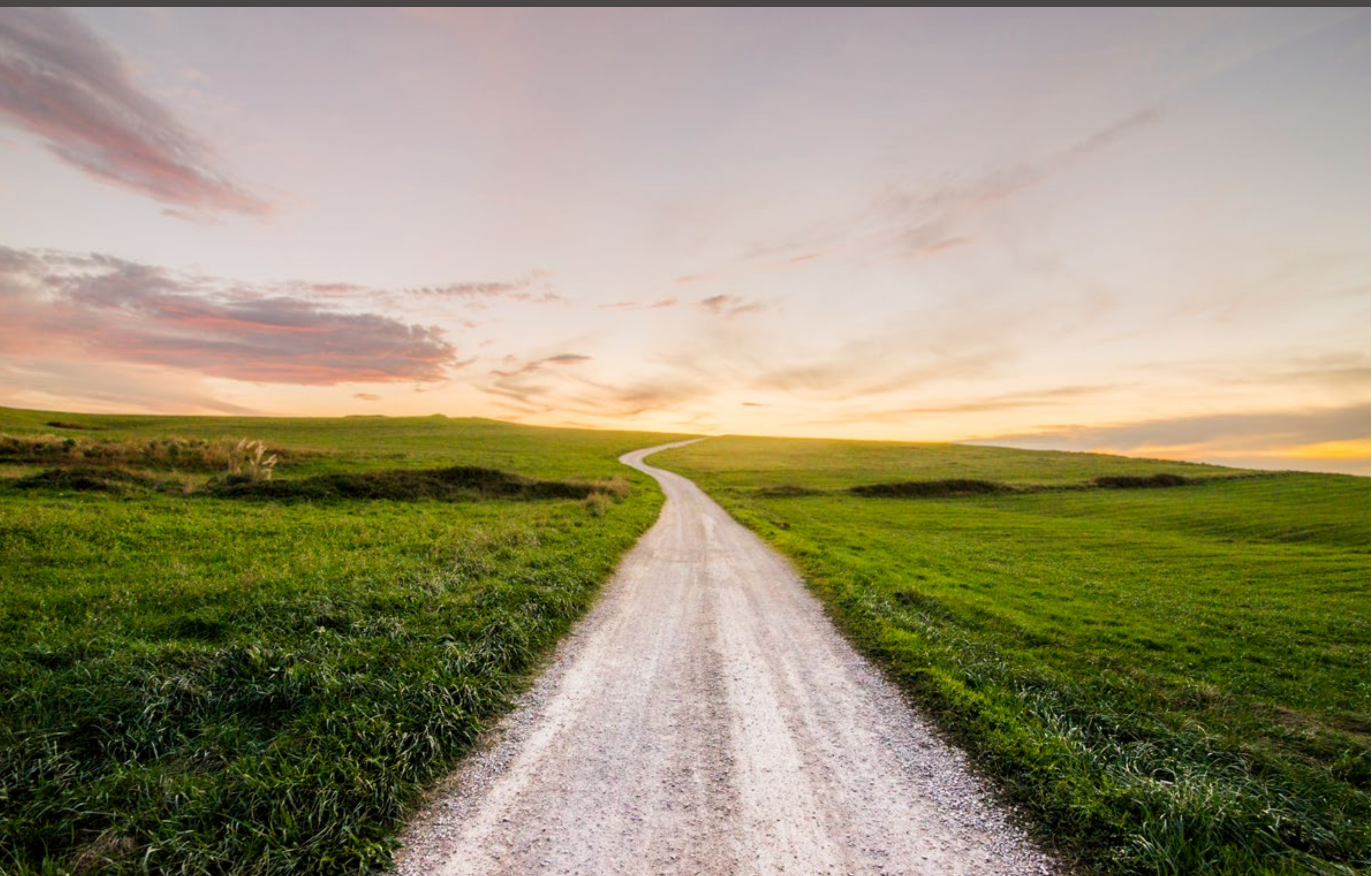
e Recruiting and retaining staff at a time where there is significant uncertainty about some of the roles within the Department, and potentially increased workload as a result of an increase in the pace of project assessments;

f Sustaining robust checks and balances; and

g Ensuring that during the transition to any replacement for rural development funds, the Department's expertise is retained either in the replacement programme or in the wider Welsh public service.

Part 1

The Welsh Government faced financial risk had the UK Government not amended the terms of its post-Brexit funding guarantee



1.1 This part of the report looks at how the Welsh Government has been managing the risk that Wales loses EU funding as a result of Brexit. In particular it looks at the deal or no deal scenarios for Brexit. In the deal scenario we consider the impact of the draft Withdrawal Agreement and any residual risks to EU funding. In the no deal scenario, we look at the risks associated with the UK Government's previous guarantee to fund projects that have been signed at the point of Brexit (29 March 2019), and the consequences of the 24 July 2018 UK Government announcement extending the guarantee to cover the full allocation. In the no deal scenario, we also look at the wider UK funding position and the risk that the UK has to fund projects that could have been claimed from the EU by the Welsh Government.

The Welsh Government initially took steps to speed up the programme to maximise EU funding but later relied on the UK funding guarantee

1.2 Under EU rules the Welsh Government has until the end of December 2023 to spend and claim the full allocation of £522 million in EU funding. The Welsh Government originally planned to commit all funding to signed projects by December 2020 so that it then had the three years between 2020 and 2023 to spend and claim it back from the EU.

1.3 Following the EU referendum in July 2016, the Welsh Government sped up the pace of commitment in order to claim as much EU funding as possible by the time of Brexit in March 2019. They did this by opening more schemes and increasing the percentage of EU funding for some schemes.

1.4 Under EU rules, the Welsh Government can set some of the rates for the proportion of EU funding. The maximum EU funding that can be used on schemes ranges from 53% to 90% dependent on the location of the beneficiary, the type of funding and the activity being funded. Rather than set different funding rates for each scheme, at the start of the programme the Welsh Government initially set a flat-rate of 43% funding from the EU across all schemes funded by mainstream EAFRD. After a 'lessons learned' exercise following the previous programme it considered a flat-rate to be a lower risk option, given that the EU can impose significant financial penalties across the whole programme if the funding rates as set are not adhered to. In 2016, in response to the referendum result, the Welsh Government increased the flat-rate EU funding rate from 43% to 53%. This was the highest rate that could be applied to all claims. Higher rates for certain measures and beneficiaries are allowable within EC regulation, but continuation of a flat-rate was considered preferable by the Welsh Government to reduce the risk of it applying the incorrect rate and having financial penalties applied by the EC.

1.5 In October 2016 the UK Government announced its funding guarantee. This pledged to replace EU funding for all projects committed to by the Welsh Government at the point of Brexit. The Welsh Government could have continued to open more schemes and increase EU funding rates further in order to draw down EU money at a faster rate, but chose not to. The Welsh Government's preference was that the RDP should run over the time frame as it was originally planned and to rely on the UK government guarantee to fund it. The Welsh Government considered that there were difficulties with expediting the programme to claim more EU funding. These difficulties are set out in Box 2 below.

Box 2 – factors that the Welsh Government state limited their ability to further expedite the Rural Development programme
A potential reduction in the size of the RDP The Welsh Government considered that increasing EU co-financing rates further would have reduced the size of the overall programme. That is, by claiming EU funding at a higher rate, the EU pot would have been exhausted more quickly. While the value of the EU pot would have remained the same, the co-financing element by the Welsh Government would have been smaller because it would have contributed a smaller proportion to each claim paid. The overall impact of this would have been less money spent on the RDP. However, the Welsh Government did not consider whether there were other ways that they could have spent the same amount of money outside of the RDP in order to both maximise EU funding and maintain the same level of benefit for rural development in Wales.
Risk of weakened controls The Welsh Government considered that there was an increased risk of internal financial controls being compromised and schemes being less robust or claims ineligible. This in turn could have led to financial penalties and clawbacks by the EU.
Limited staff resource A lack of capacity within the Welsh Government's Scheme Management Unit has stifled the ability to open and administer more schemes. As at March 2018 there was a backlog of 132 projects still in appraisal stage.
Competition limitations Given the regulatory requirement for the programme to be competitive, the Welsh Government does not have any projects held under consideration which can be called upon in order to quickly commit funds.

Box 2 – factors that the Welsh Government state limited their ability to further expedite the Rural Development programme

Planning of co-financing

All of the co-financing in the programme comes from the Welsh Government. However, it does not commit to its co-financing budget for the lifetime of the programme (including N+3 years). Co-financing is set on an annual basis, alongside the wider Welsh Government budget. The amount of co-financing available tends to be the same from year-to-year and does not match the known patterns of the programme, with spend lower in the early years and rising at later points. As such, the co-financing has tended to be underspent early in the programme but becomes a potential barrier later in the programme. The Welsh Government has been reluctant to open new schemes that would cover future years, without certainty that the necessary co-financing will be available.

1.6 As of March 2018, the Welsh Government had committed almost two-thirds of the EU funding (£378 million).

Exhibit 4 – position of the 2014-2020 EU funding for the RDP at end of March 2018

1.7 The Welsh Government had plans to take it to what it considered to be 100% commitment by March 2019 a maximise the UK funding guarantee. All EU funding was allocated to Intermediate Bodies. Intermediate bodies are internal departments of the Welsh Government that take managerial responsibility for delivering a series of schemes under the RDP. The Intermediate Bodies had a pipeline of schemes worth £109 milion of which £83.9 million would not be committed to signed projects before March 2019. The Welsh Government did not seek to clarify whether such a commitment to an internal department without an underlying signed project would fit the terms of the UK Governments funding guarantee until November 2017.

1.8 It is too early to judge the likely impact of the funding in terms of the benefits it achieves and whether the original expectations or targets will be met. The Welsh Government measures and reports progress against a wide range of detailed measures. Exhibit 5 sets out the key performance measures that the Welsh Government reports having achieved by the end of March 2018.

Exhibit 5 – the Welsh Government's key indicators for the EAFRD programme as at 31 March 2018

	Progress	Target
Physical area supported	689,186 hectares	688,000 hectares
People in training	6,400	13,000
Agricultural holdings supported	882	3,773

Source: Welsh Government data

If there is a Withdrawal Agreement, EU funding will continue largely unchanged so there is a limited risk of Wales losing out substantially

1.9 If the draft Withdrawal Agreement is agreed between the UK and EU, then under the terms of the draft Withdrawal Agreement, Wales will continue to be able to participate in the 2014-2020 programme until its end. In accordance with EU rules the Welsh Government has plans in place to commit all EU funding to signed projects by December 2020 and to spend and claim all funding by the end of the programme in 2023.

1.10 Even with a Withdrawal Agreement in place, Wales could lose out on some funding if projects underspend. The Welsh Government has the option to mitigate this risk by overcommitting funds. Given the uncertainty of future funding the Welsh Government may need to be more cautious about over-commitment, thereby increasing the risk that it is unable to balance out and redistribute underspends. For each 1% of the value of the EU funding underspent, Wales would lose around £5.2 million.

There was a significant risk of Wales losing out on funding in a no deal scenario until the UK Government very recently extended its guarantee

Under the previous terms of the UK Government guarantee, there was a significant risk of Wales losing funding if there is no Withdrawal Agreement in March 2019

1.11 If the UK leaves the EU without a deal in March 2019, EU funding to Wales will stop. The UK Government's guarantee in October 2016 said that it would replace funding for 'all structural and investment projects' that have been 'signed before the UK leaves the EU'. As previously drafted, the guarantee only covered funding for projects approved by 29 March 2019.

1.12 The Welsh Government had allocated all EU funding to Intermediate Bodies, which it expected to be covered by the UK Government guarantee. Of this, £83.9 million would not be committed to individual projects by March 2019. As reported above the Welsh Government did not begin to seek clarification on whether the terms of the guarantee would include the use of Intermediate Bodies until November 2017. The UK Government produced a draft guidance note on the detail of the guarantee in June 2018 and this confirmed that the intermediate body commitment would not fall within the scope of the guarantee. As a result there was a significant risk that Wales would have lost the £83.9 million unless the Welsh Government could have rapidly developed new schemes or signed-up projects in a very short space of time.

1.13 There could also have been losses to Wales due to a lack of flexibility to move funds around between projects and schemes afer Brexit. In a programme of this size, some projects and schemes will inevitably spend less than they planned. Under EU rules, the Welsh Government has some flexibility to redirect underspends at a scheme or project level to other projects and schemes up to the end of the programme period. However, it was not clear that the UK Government guarantee, which was specifically related to approved projects, would allow such flexibility to move funding beyond the point at which the projects had been approved and the funding guaranteed. Therefore, any underspends could have been lost to Wales.

The UK Government has recently extended the guarantee with the new terms significantly reducing the risk of Wales losing funding in a no deal scenario

1.14 In February 2018, the UK Government's Department for Environment, Agriculture and Rural Affairs produced a White Paper on the future of agriculture after Brexit. The White Paper referred to a Conservative Government manifesto commitment and stated that 'we will maintain the same cash total funding for the sector until the end of this parliament: this includes all EU and Exchequer funding provided for farm support under both Pillar 1 and Pillar 2 of the current CAP. This commitment applies to each part of the UK'. Taken literally, the White Paper appeared to offer a blanket guarantee that Wales would get the full allocation under the current RDP. However, Welsh Government officials confirmed with the UK Government that it only related to new funding after 2020, not the current round. Therefore, at that point the UK Government guarantee to fund projects approved by March 2019 still stood.

1.15 On 24 July 2018, the UK Government announced that it was extending its guarantee of EU funding to cover all projects signed before end of December 2020. As drafted, this extension of the guarantee significantly reduces the risks associated with both not committing funding and underspends in a no deal scenario. However, the precise impact will become clearer as the UK Government sets out further details on how the guarantee will work in practice.

1.16 The Welsh Government Rural Development division along with the Welsh European Funding Office (WEFO) attempted to try to clarify the UK Government's interpretation of the guarantee. Box 3 sets out the areas where WEFO on behalf of the Welsh Government had asked for further detail. The UK Government intends to produce updated guidance on the extended guarantee in the near future, which we understand will address some of the issues that were raised. Ultimately, the scope of the guarantee is a decision for the UK Government.

Box 3 – key areas where WEFO has sought clarity over the UK Government guarantee
Project/scheme variation flexibility Will the UK Government permit variations to agreed projects committed at 29 March 2019 and still regard varied commitments to be covered by the guarantee?
Impact on other funding Can the UK Government confirm the guarantee will not impact on any other funding earmarked for Wales?
Overall value of guarantee How and when will the UK Government determine whether there is a Sterling value of the ceiling on its guarantee?
Regulations What existing EU regulations does the UK Government expect to retain and what audit and inspection process will be required post Brexit?
Cut-off point Will the UK Government meet any amounts that are in the system at the point of Brexit?
Technical assistance Will the UK Government continue to fund WEFO staffing and other training, advice and support costs under the guarantee?

There is a wider risk to the UK funding position in a no- deal scenario

1.17 Although this report focuses on the risks to Wales, there is a wider risk to the UK funding position in a no- deal scenario. In a no- deal scenario, the gap in funding the programme would be covered by the UK Government. The size of that gap depends in part on the amount of EU funding that Wales (and other parts of the UK) can draw down from the EU before Brexit. To draw down funding from the EU, projects first need to spend the money then submit a claim to the Welsh Government. The Welsh Government then pay the claimant and draw down the funding from the European Union.

1.18 At the start of the programme the EU set out their overall funding budget to the Welsh Government in annual allocations from 2015 to 2020. These allocations are the maximum amounts that Welsh Government can draw down in that year. The N + 3 rule then allows the allocation to be claimed up to three years after. Beyond the three years that funding is lost. To date the Welsh Government have met all N + 3 targets and no funding has been lost.

1.19 In a typical programme it is usual for annual allocations not to be fully used within the year, and for member states to make use of the N + 3 periods to claim their full funding. However, given Brexit, and in the event of a no-deal scenario this timetable for claiming EU funds will shorten considerably to March 2019. At the end of 2018, the Welsh Government intends to have claimed £192 million (43%) of the £445 million cumulative EU allocations available to them by that date. It is therefore almost certain that three months later Wales will not have been able to draw down the total EU allocation available to them before Brexit in March 2019.

1.20 In paragraph 1.5 above we report the Welsh Government's view that there were logistical difficulties and risks in expediting the programme in order to maximise the funding coming from the EU prior to Brexit. These included potential limitations in Welsh Government resources to deliver more schemes or the availability of Welsh Government co-financing.

1.21 It is difficult to be sure exactly how much more the Welsh Government could have spent had it chosen to accelerate the programme, but it is clear that in a no deal scenario the amount of funding that will need to come from UK, rather than EU sources, is likely to be higher as a result of the Welsh Government's decision not to expedite the programme.

Part 2

The Welsh Government has checks and balances to ensure that it complies with strict EU rules, but needs to strengthen scrutiny and risk management of the overall RDP

2.1 This part of the report considers the arrangements in place to:

a ensure that projects only use money in line with EU rules; and

b monitor progress with the overall programme.

The Welsh Government has checks and balances to ensure that it complies with strict EU rules

2.2 The Rural Development Programme document sets out how the Welsh Government matches its priorities to those of the EU funding programme. In developing the Rural Development Programme, the Welsh Government chooses which EU 'measures' it will adopt and how much of the available funding it will allocate to each. Once the Rural Development Programme document is approved by the EU, the Welsh Government sets up specific schemes to deliver the activities outlined in the RDP. Each scheme must directly match at least one EU measure. Several of the schemes, such as Glastir, are well established and have been run under previous funding rounds. All schemes are subject to Ministerial approval and must demonstrate that they are aligned to both the EU priorities and the Welsh Government's own objectives.

2.3 Each scheme has its own set of criteria. For most schemes farmers or organisations need to apply through an expression of interest. Officials then review the applications to determine whether they meet the criteria. The Welsh Government has streamlined the application process and provides clear instructions and guidance to applicants. The Welsh Government also offers considerable administrative support to potential applicants.

2.4 The Welsh Government has sought to learn and apply lessons from previous programmes. Following the completion of the last RDP 2007-2013, the Welsh Government met with a number of stakeholders and carried out a public consultation to gather views on the strengths and weaknesses of the programme. This identified areas of good practice to continue, and areas for improvement which were factored into the design of the current RDP arrangements. This included the creation of a specific 'Scheme Management Unit' (SMU) to streamline the set up and administration of applications and claims, and a simplification of the financial structure of the programme to make the administration of funding clearer and easier.

2.5 Under EU Regulations, the Welsh Government must comply with a series of control standards. These standards cover a range of issues, including ensuring that EU funding is only awarded and spent on things that the EU deems eligible. The Wales Audit Office reviews the Welsh Government controls over Rural Development Funding every year to provide assurance over the compliance with the required standards[7]. The controls are also subject to periodic review by the EU. If the Welsh Government cannot demonstrate that its controls meet the required EU standards, it could result in financial penalties being imposed by the EU.

2.6 The Wales Audit Office concluded in 2015, 2016 and 2017 that in general, the Welsh Government complied with the EC control standards. In 2016 and 2017 the Wales Audit Office reported one area for improvement where officers were making administrative mistakes in interpreting scheme rules and determining the eligibility of claims for funding. In response to the Wales Audit Office findings, the Welsh Government implemented an action plan of training and guidance for officers. Our 2018 audit will follow up whether this action plan has been successful.

There is scope to strengthen oversight and risk management of the overall RDP

2.7 Risk management arrangements in relation to the RDP are not coordinated, with responsibilities divided within the Welsh Government. The Rural Development Division is tasked with managing operational risks, the Brexit liaison team manage the risks associated with the Brexit interface with UK government, and the Welsh Government Finance Department consider financial risks. No central risk management arrangements are in place to bring all risks associated with the RDP and Brexit together and our work identified that the arrangements are not fully understood by officials. As such, there is a possibility that key risks are not captured and considered. For example, whilst the Welsh Government officers understood some of the risks associated with the UK Government's guarantee, the detailed considerations of the risks to the Welsh Government's financial position and the delivery of the RDP is not documented on any of the relevant risk registers.

7 Article 5(3) and 6 of Commission Implementing Regulation (EU) No 908/2014 sets out the requirement for member states to appoint a 'Certification Body' to audit their annual agricultural fund accounts and internal controls and report their findings to the EC. The Wales Audit Office work in a consortium of UK auditors to provide this Certification Body function to the UK member state. The Wales Audit Office deliver the Welsh Government element of the audit.

2.8 The Programme Monitoring Committee (PMC), which comprises independent members and officials from the EU, oversees the overall programme alongside the EU Structural Funds programme. We found that the level of scrutiny of the Rural Development Funding at the PMC is limited in comparison to EU Structural Funds.

2.9 PMC members have themselves expressed concern over their lack of detailed understanding of the Rural Development Funding. The financial and management information regarding the progress of the RDP that the Welsh Government provides to the PMC is unclear and sometimes inaccurate. For example, the term ‘commitment’ is used to describe three scenarios:

- commitments made to scheme EOI windows and other activities;
- commitments to projects underpinned by a signed contract with a beneficiary; and
- commitments to projects underpinned by a signed contract with a beneficiary with the exception of annual payments where only the current year’s payment is included once the claim has been received (the definition used for some EC returns).

2.10 The Welsh Government recognises some of the limitations of PMC to offer robust scrutiny of the management and delivery of RDP and has taken some steps to improve matters. It has offered training to PMC members to help them better understand the rural Development Funding but take up by PMC members has been limited. They have also recently made PMC papers available to members in advance of meetings to give them more time consider the progress of the RDP.

Part 3

It is not yet clear what will replace European Union agricultural funds post-Brexit but the Welsh Government is trying to shape debate

3.1 This part of the report looks at emerging plans for replacing EU agricultural funds post-Brexit. This section does not comment on the merits of the plans. At the time of drafting this report, the Finance Committee of the National Assembly for Wales is holding an inquiry into the replacement of EU funds, and the Welsh Government has published a Green Paper consultation document, 'Brexit and our land: Securing the future of Welsh farming'[8]. We have set out the position of the UK Government and the Welsh Government on the future of agricultural funds at the time of drafting. Ultimately, the question of which tier of government is responsible for any replacement scheme is a political and constitutional matter to be resolved between the UK Government and the devolved governments.

The UK Government has set out a broad vision for agriculture in England and a transition phase but recognises that devolved governments will decide their own priorities

3.2 In February 2018, the UK Government published a consultation paper[9] setting out its ambitions for the future of farming and the environment after the UK leaves the EU. This consultation paper included reference to a Conservative government manifesto commitment to provide devolved administrations with an annual budget for farm support equal to the annual average cash total for farm support under both pillars across the 2014-2020 programme. It will be for the UK Government and devolved administrations to determine how to spend that money.

3.3 The paper does not comment on the level of funding after 2022. Evidence presented by the Minister for Agriculture to the House of Commons Welsh Affairs Committee in May 2018[10] also made it clear that the total level of UK funding for agricultural support post-2022 has yet to be confirmed.

8 Welsh Government, **Brexit and our land: Securing the future of Welsh farming**, July 2018

9 Department for Environment, Food and Rural Affairs, **Health and harmony: the future of food, farming and the environment in a Green Brexit**, February 2018.

10 House of Commons Welsh Affairs Committee, **Brexit: priorities for Welsh agriculture**, July 2018

3.4 The UK Government's consultation closed on 8 May 2018 and it has subsequently introduced an Agriculture Bill that sets out its vision for Agricultural policy that distinguishes it from the European Union's Common Agricultural Policy. The Bill had its second reading in the House of Commons on 10 October 2018. Whilst the UK Government's position is that its vision for future Agricultural policy could work for the whole of the UK it recognises that devolution provides Wales with the powers to decide its own priorities. However, the consultation paper also referred to the possible establishment of common frameworks where necessary in order to enable a well-functioning internal market across the United Kingdom, compliance with international obligations and protection of common resources.

3.5 In addition to the Agriculture Bill, the UK Government intends to develop a UK Shared Prosperity Fund. This may apply to non-agricultural schemes currently funded from the RDP. Further details around the UK Shared Prosperity Fund and the Welsh Government response to this are included in our recently published report, Managing the impact of Brexit on EU Structural Funds.[11] The Welsh Government has set out its vision for agricultural policy in Wales post Brexit and wants full control and funding to be devolved.

3.6 In February 2018, the Cabinet Secretary for Environment and Rural Affairs outlined a vision for future land management in Wales, to address economic realities, help prepare for Brexit and integrate land use with the Welsh Government's broader ambitions in the Well-Being of Future Generations and Environment Acts. They are summarised in a set of five principles (Box 4) to underpin reform in Wales.

Box 4 – the Welsh Government's principles for change

- keep farmers, foresters and other land managers on the land
- food production is vital
- a need for a prosperous and resilient Welsh land management industry whatever the nature of Brexit
- future support will focus on delivering additional public goods
- all land managers should be able to access new schemes

Source: Welsh Government

11 **Managing the impact of Brexit on EU Structural Funds**, paras 3.2- 3.5.

3.7 Building on these principles, in July 2018, the Welsh Government set out its own proposals for agricultural policy after the UK leaves the EU in **Brexit and our land: Securing the future of Welsh farming**. The proposals seek views on:

- a new land management programme consisting of an economic resilience scheme and a public goods scheme to replace the CAP; and
- how the specific schemes that will deliver the support should be designed.

3.8 The paper sets out the Welsh Government's objection to any reduction in funding as a result of the UK leaving the EU, which would jeopardise its ability to support the activities that are currently funded through EAFRD and EAGF. The Welsh Government is calling for a new, rules-based system of replacement funding, which ensures the allocation of resources within the UK is based on relative need and not the Barnett Formula[12].

3.9 In setting out its thinking on the future of agricultural funding, the Welsh Government has sought to learn lessons from its experience of managing agricultural funds for rural development and proposes a phased transition plan to move from old to new schemes by 2025. The Welsh Government's policy paper is clear that the EU's common agricultural policy does not do enough to deliver the required outcomes for Wales and outlines a case for bespoke support in Wales. The paper also outlines that future UK frameworks (paragraph 3.3) must recognise that Wales' land is different and that its communities and sectors are different and allow flexibility to make policies reflecting the unique context in Wales.

3.10 The Welsh Government is engaging with stakeholders to obtain views on its proposals through an online consultation and a series of open meetings being held until 30 October 2018. It intends to bring forward details proposals by spring 2019 and publish legislation by the end of the Assembly term.

12 The Barnett formula is a system for allocating grants to Northern Ireland, Scotland and Wales. A full explanation can be found in our **Guide to Welsh Public Finances**, July 2018

Appendices

Appendix 1 – Audit methods

Appendix 2 – List of schemes

Appendix 1 – Audit methods

Document review and data analysis

We reviewed a wide range of documentation including:

- Welsh Government guidance documents
- Independently commissioned reviews of the Programmes
- European Commission audits
- Wales Audit Office external audits of Agricultural Funds accounts and control systems
- Financial and performance data provided by the Welsh Government
- Ministerial briefings
- Minutes from various meetings including the Programme Monitoring Committee

Interviews

We have discussed the administration of the programmes with Welsh Government senior officials and held a series of interviews to discuss emerging findings and clarify key aspects of the programmes.

Observations

We attended and carried out observations at the December 2017 and May 2018 Programme Monitoring Committee meetings.

Appendix 2 – List of schemes

Scheme	Purpose
Farm Business Grant Scheme	Helps farmers to improve economic and environmental performance of their agricultural holdings. The grant provides a financial contribution towards capital investments in equipment and machinery.
Sustainable Production Grant Scheme	Helps farmers develop more sustainable, profitable and resilient farm businesses. The grant provides a financial contribution towards capital investments in equipment and facilities that relate to: • Animal health and welfare • Crop storage • Production housing and handling • Renewable energy production • Soil and crop management
Food Business Investment Scheme	Provides support to primary producers of agricultural products and businesses that do first and/or second stage processing activities in Wales.
Cooperation and Supply Chain Development Scheme	Supports the development of new products, practices, processes and technologies in the agriculture, forestry and food sectors.
Sustainable Management Scheme	Supports collaborations aimed at improving natural resources and benefits they provide including reducing greenhouse gas emissions and improving business and community resilience to the impacts of climate change.
Rural Community Development Fund	Grants primarily to community-based organisations for a wide range of activities to help meet local needs and strengthen communities.

Scheme	Purpose
Timber Business Investment Scheme	Supports improvements in value of forests, for example by enabling woodland management activities, timber harvesting and/or in-forest or small-scale timber processing.
Co-operative Forest Planning Scheme	Supports a range of activities aimed at encouraging planning and creation of broadleaved and conifer woodland.
European Innovation Partnership Wales	Supports the development of research and innovation in agriculture and woodlands.
LEADER	Supports local development and capacity building in rural communities.
Knowledge Transfer and Innovation Scheme	Supports the development of a more professional, profitable, diverse and resilient land based sector targeting farming and forestry businesses.
Rural Business Investment Scheme	Support projects that off clear benefits to the food and drink industry.
Glastir	Scheme designed to deliver specific environmental goods and services aimed at combating climate change, improving water management & maintaining and enhancing biodiversity.

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