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REPORT FROM THE COMMISSION

ANNUAL REPORT ON THE COHESION FUND (2003)

(SEC(2004) 1470)

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The information set out in this report is presented in greater detail in the Commission staff working document (SEC(2004) 1470).

ANNUAL REPORT ON THE COHESION FUND (2003)

This report is presented in accordance with Article 14(1) of Regulation (EC) No 1164/94 establishing a Cohesion Fund. It covers the activities of the Cohesion Fund during 2003.

1. BUDGET IMPLEMENTATION

The final amount, after indexation, of the resources of the Cohesion Fund for 2003 was EUR 2 839 million, including around EUR 1 million for technical assistance.

99.8% of commitment appropriations were implemented in 2003. Only EUR 3.37 million was carried forward to 2004 and no commitment appropriations were cancelled.

Implementation of commitment appropriations in 2003 (in euro)

Commitment appropriations	Initial	Movements	Final resources	Implementation	Cancelled	Carryovers to 2003
2003 budget	2 839 000 000	0	2 839 000 000	2 835 622 004	0	3 377 996
Appropriations carried over from 2002	0	0	0	0	0	0
Appropriations made available again	31 096 007	0	31 096 007	29 680 316	0	0
Repayments	0	0	0	0	0	0
Totals	**2 870 096 007**	**0**	**2 870 096 007**	**2 865 302 320**	**0**	**3 377 996**

Payment appropriations worth EUR 104.8 million were transferred from the Cohesion Fund to the Solidarity Fund and EUR 350 million was transferred to Objective 1 to cover payment requests from the Member States. Taking account of these transfers, all the payment appropriations were implemented.

Implementation of payment appropriations in 2003 (in euro)

Payment appropriations	Initial	Movements	Final resources	Implementation	Cancelled	Carryovers to 2003
2003 budget	2 650 000 000	-454 789 000	2 195 211 000	2 195 123 861	87 139	0
Appropriations carried over from 2002	0	0	0	0	0	0
Appropriations made available again	0	0	0	0	0	0
Repayments	0	0	0	0	0	0
Totals	**2 650 000 000**	**-454 789 000**	**2 195 211 000**	**2 195 123 861**	**87 139**	**0**

During the year, Spain committed appropriations in excess of its allocation, thereby making up for the fact that Greece did not consume all the appropriations allocated to it.

Budget implementation of appropriations in 2003 by Member State

Commitment appropriations 2003

Member State:	Environment		Transport		Mixed	Total	
	Amount	% Envir	Amount	% Transport	Amount	Amount	%
Spain	717 645 122	46.5	825 490 749	53.5		1 543 135 871	54.4
Greece	176 404 253	33.3	353.054.898	66.7		529 459 151	18.7
Ireland	39 875 213	34.0	77 447 367	66.0		117 322 580	4.1
Portugal	374 662 746	58,1	270.140.540	41,9		644 803 286	22.7
Technical assistance	-	-	-	-	901 115	901 115	0
Total	**1 308 584 335**	**46.2**	**1 527 037 669**	**53.8**	**901 115**	**2 835 622 004**	**100**

<u>Payment appropriations 2003</u>

Member State:	Environment		Transport		Mixed	Total	
	Amount	% Envir	Amount	% Transport	Amount	Amount	%
Spain	795 426 626	46.1	929 305 015	53.9		1 724 731 641	78.6
Greece	25 913 242	64.7	14 164 441	35.3		40 077 683	1.8
Ireland	84 168 779	48.9	87 923 822	51.1		172 092 601	7.8
Portugal	135 539 103	52.5	122 584 061	47.5		258 123 165	11.8
Technical assistance	-	-	-	-	98 771	98 771	0
Total	**1 041 047 750**	**47.4**	**1 153 977 339**	**52.6**	**97 771**	**2 195 123 860**	**100**

After 2001, when the implementation of appropriations was clearly concentrated on environmental projects, in 2003 transport projects predominated for the second year running (53.8% of commitment appropriations and 52.6% of payment appropriations).

The major effort begun in 2000 to clear the appropriations remaining to be settled in respect of projects from the previous period was sustained in 2003 with some 26% of the appropriations remaining to be settled at the beginning of the year being paid or decommitted during the year. Accordingly, the appropriations remaining to be settled at the end of 2003 accounted for only 39% of the annual budget of the Cohesion Fund (as against more than half at the end of 2002). In all, 67 projects were closed during 2003. Naturally, this effort to liquidate the appropriations to be settled will continue in 2004.

<u>Settlement in 2003 of commitments for the period 1993-99</u>

Member State	Initial amount to be settled	Decommitments	Payments	Final amount to be settled
Spain	915 085 684	3 925 998	260 564 812	650 594 874
Greece	381 986 228	17 698 199	27 217 263	337 070 766
Ireland	90 492 409	111 600	34 292 729	56 088 080
Portugal	103 128 498	2 911 167	38 996 933	61 220 398
Technical assistance	96 454	96 454	0	0
Total	**1 490 789 273**	**24 743 418**	**361 071 737**	**1 104 974 118**

2. ECONOMIC ENVIRONMENT AND CONDITIONALITY

The Council Regulation on the Cohesion Fund[1] provides for financing by the Fund to be conditional. In particular, no new projects or, in the case of major projects, no new project stages may be financed if the Council, acting by a qualified majority on a recommendation from the Commission, finds that the Member State concerned has not implemented its stability or convergence programme in such a way as to avoid an excessive deficit.

In Portugal, the general government deficit amounted to 4.4% of GDP in 2001, exceeding the 3% of GDP reference value in the Treaty[2]. On 16 October 2002 the Commission adopted an opinion stating that an excessive deficit existed in Portugal. On 5 November the Council adopted a decision to that effect, in accordance with Article 104(6) of the Treaty, as well as a recommendation addressed to Portugal with a view to bringing the excessive government deficit to an end. As the Portuguese authorities took action to comply with this recommendation, the Commission did not recommend the suspension of the Cohesion Fund in Portugal. The Portuguese general government deficit for 2002 and 2003 is estimated at 2.7% and 2.8% of GDP respectively. On 11 May 2004, the Council therefore decided, on the basis of a Commission recommendation, to repeal the decision on the existence of an excessive deficit in Portugal.

The Commission activated the EDP for Greece on 19 May 2004 on the basis of figures showing that the deficit in 2003 amounted to 3.2% of GDP. On 5 July 2004, the ECOFIN Council adopted a decision (Art.104.6) on the existence of an excessive deficit in Greece and a recommendation for the excessive deficit correction (Art.104.7). The Council recommended the Greek authorities to put an end to the excessive deficit situation as rapidly as possible and by 2005 at the latest. The Council established the deadline of 5 November 2004 for the Greek government to take effective action. Also the Greek authorities were recommended to reduce the debt ratio at a satisfactory pace and to correct the serious deficiencies revealed in the process of validating the EDP notification.

Subsequently, large upward revisions of the deficit figures took place in September 2004, resulting in an outturn for 2003 of 4.6% of GDP for the deficit and of 109.9% for the debt. According to the Commission 2004 autumn forecasts, the general government deficit would reach 5.5% of GDP in 2004 and the debt ratio would attain 112.1% of GDP, while for 2005 the general government deficit would attain 3.6% of GDP in 2005. This development reflects at least partly the absence of effective action taken by Greece in accordance with the recommendations under Article 104(7). Consequently, the Commission may consider recommending to the Council to take further steps concerning the follow-up to such budgetary developments.

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1. Article 6 of Council Regulation (EC) No 1164/94 as amended by Regulation (EC) No 1264/99.
2. Namely the estimated outturn for 2001 in the September 2002 reporting of government deficits and debt levels in accordance with Council Regulation (EC) No 3605/93, as amended by Regulation (EC) No 475/2000.

3. PREPARING THE ACCESSION COUNTRIES TO IMPLEMENT THE COHESION FUND

For 2004-06, EUR 24 billion (current prices) has been earmarked for structural assistance in the 10 countries acceding to the EU, of which over one third (EUR 8.5 billion) has been allocated to the Cohesion Fund.

Table: Breakdown of allocations for the accession countries: 2004-06

Country	Mid-range allocations (EUR million - 2004 prices)
Cyprus	53.94*
Czech Republic	936.05
Estonia	309.03
Hungary	1 112.67
Latvia	515.43
Lithuania	608.17
Malta	21.94
Poland	4 178.60
Slovakia	570.50
Slovenia	188.71
Total	**8 495.04**

Upon accession on 1 May 2004, eight of the 10 ISPA beneficiary countries cease to benefit from ISPA and, together with Cyprus and Malta, become eligible under the Cohesion Fund. In order to prepare these countries for a smooth and timely transition to the Cohesion Fund, the Commission launched a series of activities in 2003, which are as follows:

– Consultations between the authorities of the new Member States and the Commission were started with a view to drawing up consistent Cohesion Fund strategic reference frameworks for 2004-06. The frameworks were to set the main areas of priority assistance and their financial breakdown and to define the role of the various national authorities in the management of the Fund.

With the exception of the frameworks of the Czech Republic and Slovakia, the Commission had been consulted on all the frameworks of the accession countries by the end of 2003. Expenditure under the Cohesion Fund in those countries will therefore be eligible from 1 January 2004.

– Considering the substantial relative increase in resources available to the accession countries under the Cohesion Fund, a series of technical assistance measures were adopted to help the countries concerned to prepare quality transport and environment projects for submission to the Cohesion Fund.

– Technical assistance at the initiative of the Commission continued to focus on training the public procurement authorities in the accession countries, with particular attention to the implications of the new Financial Regulation and public-private partnerships for public utilities.

* Including the Financial Instrument for Fisheries Guidance (FIFG)

– Finally, the Commission continued to audit the new Member States' financial management and control systems and make recommendations to improve these. Moreover, the Commission encouraged acceding ISPA countries to continue their efforts to move along the EDIS (extended decentralised implementation system) roadmap so as to obtain a positive certificate from the Phase 3 (compliance assessment) external auditor. As a result, by the end of 2003, five out of eight of these countries had completed Phase 3 for one or both intervention sectors and applied for either partial or full EDIS (Phase 4).

4. COORDINATION WITH THE STRUCTURAL FUNDS: THE STRATEGIC REFERENCE FRAMEWORKS

4.1. Transport

In 2003 the transport sector accounted for 53.8% of total Cohesion Fund commitments (EUR 1 526 million). As in the past, the Commission insisted that the work of the Fund should concentrate on railways. The projects and operations adopted in 2003 by Member State are set out in the Annex.

While TEN transport projects of common interest are financed from the trans-European transport networks budget line, the Cohesion Fund provides funds specifically for the overall TEN transport infrastructure networks. Coordination between the TEN budget and the Cohesion Fund is important because these Community financial instruments take into account the need for links between the central regions of the Community and those regions which are structurally handicapped by their insular, landlocked or peripheral status.

The process of revising the guidelines for the development of the trans-European transport network[3] continued during 2003. A high-level group consisting of representatives of the current and future Member States and the EIB made its recommendations to the Commission concerning new priority projects in the enlarged EU.

Based on the recommendations of the high-level group and the results of the public consultation on the report, the Commission brought forward a new proposal[4] on 1 October 2003, which supplements the 2001 proposal. The new proposal adds a further nine new projects to the list of priority projects, bringing the total number of projects on major transport axes up to 29. Member States should give appropriate priority to these projects when requesting funding from EU financial instruments.

4.2. Environment

The environment accounted for 46.2% of total Cohesion Fund commitments in 2003 (EUR 1 309 million). The priorities in this sector remained the supply of drinking

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[3] Decision No 1692/96/EC.

[4] COM(2003)564 final: Proposal for a Decision of the European Parliament and of the Council amending the amended proposal for a Decision of the European Parliament and of the Council amending Decision No 1692/96/EC on Community guidelines for the development of the trans-European transport network.

water and the treatment of waste water and solid waste. The projects and operations adopted in 2003 by Member State are set out in the Annex.

The Cohesion Fund contributes to the more general objectives of environmental policy in relation to sustainable development and in particular achievement of the priority areas of the 6th Action Programme, notably the management of natural resources, waste and climate change.

During 2003 the Cohesion Fund continued its efforts to implement environmental legislation, not only by directly financing infrastructure for waste-water treatment, drinking-water supply and the treatment of solid waste, but also by enforcing the correct application of certain Directives as a prerequisite for the grant of financing. This concerns both the subject-based directives with a large spatial component (e.g. those on nature conservation and the management of waste and waste water) and the directive on environmental impact assessments (EIA).

5. INSPECTIONS AND FINDINGS

During 2003, the Directorate-General for Regional Policy carried out 17 audit missions on projects and 10 audit missions on the management and inspection systems in the four Member States eligible under the Cohesion Fund. Problems were identified in all four Member States.

In the case of projects, the main shortcomings noted concerned the procedures for awarding public contracts, although the situation varies from country to country. The improvement in the situation noted in 2002, particularly as regards compliance with Decision 96/455/EC on publicity, was confirmed in 2003.

The irregularities detected are the subject of adversarial procedures with the four Member States with a view to determining whether financial corrections should be applied.

The audit of the systems set up by the Member States was implemented in three stages. In the first stage the Commission examined the descriptions of the systems that the Member States had communicated to it, and the two subsequent stages involved on-the-spot verifications by means of compliance testing. The findings showed that the Member States had continued their efforts to bring their organisation into line with the requirements of Commission Regulation (EC) No 1386/2002 on management and control systems for assistance granted from the Cohesion Fund and the procedure for making financial corrections, but that problems persist in certain well-defined fields.

An action plan was drawn up with Spain and Greece in order for the necessary changes to be made during 2004 to provide the Directorate-General for Regional Policy with reasonable assurances that the management and control systems are operating correctly.

6. IRREGULARITIES AND THE SUSPENSION OF ASSISTANCE

During 2003 the European Anti-Fraud Office (OLAF) finalised the reports on the joint audits carried out in 2002 with the Regional Policy DG in the four beneficiary Member States to look at their implementation of Regulation (EC) No 1831/94 as regards the systems and procedures for notifying and monitoring irregularities in this field. The conclusions of the audit were communicated to the Member States and a summary report was forwarded to the Council, Parliament and the Court of Auditors.

In addition, Article 3 of Regulation (EC) No 1831/94 concerning irregularities and the recovery of sums wrongly paid in connection with the financing of the Cohesion Fund and the organisation of an information system in this field requires the beneficiary Member States to notify the Commission of irregularities as soon as a preliminary administrative or judicial finding has been made.

In 2003, two Member States, Greece and Portugal, notified the Commission of 36 and 10 irregularities respectively. The cases notified by the Greek authorities involved a total of EUR 121 005 484 in Community contributions, and EUR 120 240 418 was subsequently deducted from payment requests submitted to the Commission. The irregularities concerned for the most part non-compliance with the rules on public contracts and applications for ineligible expenditure. The cases notified by the Portuguese authorities involved a total of EUR 21 043 856 in Community contributions and, here too, more than half the cases concerned non-compliance with the rules on public contracts, the rest concerning presentation of ineligible expenditure. In the latter case, more than half of the cases were detected during Community checks. EUR 897 896 was recovered at national level and the remainder is still to be recovered.

The other two beneficiary Member States notified the Commission under the Regulation that they had detected no irregularities during the year.

7. EVALUATION

Under the revised Regulation No (CE) 1164/94, the Commission and the beneficiary Member States both appraise and evaluate investment projects for which part-financing is requested from the Cohesion Fund, with a view to ensuring the effectiveness of Community aid.

Every application for assistance must be accompanied by an *ex-ante* cost-benefit appraisal of the project by the Member State, showing that the medium-term socio-economic advantages are in keeping with the resources deployed. The Commission scrutinises this appraisal on the basis of the new cost/benefit analysis guide used by both promoters and the Commission to assess whether part-financing is advisable. On the basis of the new guide for the cost/benefit analysis of major projects, during 2003 the Commission carried out substantial internal work to make the *ex-ante* financial analysis of the various projects more coherent.

In addition, the *ex-post* evaluation of a sample of 200 projects part-financed by the Cohesion Fund during the period 1994-2002 was launched in 2003. The results of this study are expected at the end of 2004.

8. INFORMATION AND PUBLICITY

Two information meetings with all 15 Member States and the applicant countries were held in Brussels, on 17 July and 19 November 2003.

At the first meeting, the Commission presented the commitment and payment forecasts for the year and the Member States presented the situation in their respective countries. The Commission presented the draft regulation on information and publicity measures drawn up on the basis of Decision 96/455/EC. As a result of the difficulties encountered in applying some of the Decision's provisions, certain Member States wished to amend the text. For legal reasons, the Decision was replaced by a Commission regulation.

During the November meeting, the Commission presented the 2002 annual report on the Cohesion Fund, the commitment and payment forecasts for the year and the information that, following the mid-term review, Ireland is no longer eligible under the Cohesion Fund from 1 January 2004.