



COMMISSION OF THE EUROPEAN COMMUNITIES

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**FIFTH ANNUAL REPORT FROM THE COMMISSION
TO THE COUNCIL, THE EUROPEAN PARLIAMENT,
THE ECONOMIC AND SOCIAL COMMITTEE
AND THE COMMITTEE OF THE REGIONS**

**THE EUROPEAN ECONOMIC AREA
FINANCIAL MECHANISM**

1. THE FINANCIAL MECHANISM

With the objective of stimulating economic cohesion and development between the European Economic Area (EEA) regions, a Financial Mechanism to support development projects in Greece, Ireland, Northern Ireland, Portugal and parts of Spain (the objective 1 regions as defined in 1988) was established on 1st January 1994 (article 115-116 of the EEA Agreement and Protocol 38).

Over the five-year period ending 31 December 1998, the Financial Mechanism allocated funds to the beneficiary regions of ECU 492.8 million in grant aid and interest rebates of 2 percentage points per annum on ECU 1.5 billion in loans from the European Investment Bank (EIB).

Priority has been given to projects which placed particular emphasis on the environment (including urban development), on transport (including transport infrastructure) or on education and training. Among projects submitted by private undertakings, special consideration has been given to small and medium-sized enterprises.

The Mechanism **is administered by the EIB**. The EIB has appraised each project according to financial, economic and technical criteria as well as its compatibility with the EU objectives, sectorial policies and environmental regulations and standards. The EIB then has submitted proposals to the Financial Mechanism Committee, appointed by the participating EFTA States and the Commission, which decided on the allocation of the financial resources available under the Mechanism. While the process of allocation of Funds has come to an end on 31 December 1998, the EIB continues to manage the projects portfolio until their completion.

The Mechanism was **initially funded** by the participating EFTA States. The role of the Commission was to give an opinion on the basis of the proposals before the approval of the EFTA Financial Mechanism Committee.

From 1 January 1995, following the accession of the Republic of Austria, the Republic of Finland and the Kingdom of Sweden to the European Union, Articles 83, 111 and 136 of the act concerning the conditions of this accession and the modification to the treaties on which the European Union is founded provide that the obligations of the three acceding countries for financing the Mechanism as laid down in article 116 of the EEA Agreement are financed out of the general budget of the European Communities. In consequence, the Commission has become co-responsible for the Mechanism in line with Art. 205 of the Treaty whereby the Commission shall implement the budget. The Communication by the Commission, adopted on the 30 march 1995 (C(95) 753), established the operational aspects for dealing with the Financial Mechanism within the Commission.

Following entry into force of the EEA Agreement for the Principality of Liechtenstein on 1 May 1995, the Principality fully participates in the Mechanism.

2. THE FIFTH ANNUAL REPORT

A first annual report was presented by the Commission to the Council in June 1995, concerning the activity of the Mechanism during the period from 1.1.94 to 31.5.1995.

The second annual report presented the activity concerning the Mechanism during the period from 1.1.95 to 30.06.96, the third from 01.07.96 to 30.06.97 and the fourth from 1.7.97 to 30.6.98.

This fifth annual report presents the activity from 1.7.98 to 31.12.99.

2.1. The activity of the Mechanism up to 31.12.99

The project's approval process has come to an end on 31.12.98. By that date, the Financial Mechanism Committee has approved:

- grant applications to a total of ECU 492.8 million corresponding to 98.6% of the total grant facility;
- interest rebates on a total loan portfolio of ECU 1500 million corresponding to 100% of the total EIB loan portfolio for which the interest rebate facility has been made available.

Grant activity

The distribution by beneficiary country of the grants approved by the Financial Committee over the whole period 1994-1998 and their sectorial distribution are shown below:

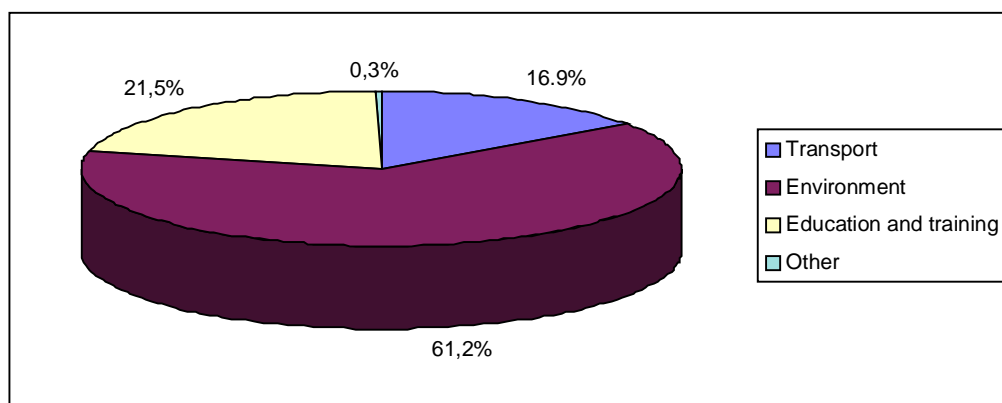
Grants distribution by country

MECU

	APPROVED GRANTS
Greece	114.3
Ireland	35.5
Northern Ireland	11.0
Portugal	105.0
Spain	227.0
TOTAL	492.8

Sectorial distribution

	MECU	Total
Transport	83 5	16.9%
Environment	301 9	61.2%
Education	105 9	21.5%
Other	1 5	0.3%



The grant allocations for Ireland, Northern Ireland, Portugal and Spain have been fully committed. As for Greece, despite contacts with the Ministry of National Economy to process a sufficient number of acceptable proposals, the commitments finally granted amounted to 94% of the available amount of ECU 121.5 million.

As of 31 December 1999, the grant disbursement amounted to EUR 231.915 million (excluding the EIB's fee of 0.5%) corresponding to 46 % of the total facility.

Interest rebate activity

The distribution by beneficiary country of the EIB loans benefiting from interest rebates approved by the Financial Committee over the whole period 1994-1998 and their sectorial distribution are shown below:

Loans distribution by country

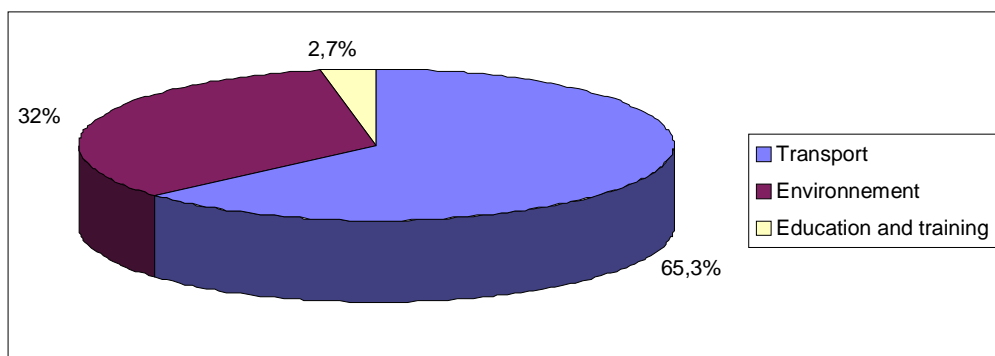
MECU

	APPROVED LOANS
Greece	364.5
Ireland	106.5
Northern Ireland	33.0
Portugal	315.0
Spain	681.0
TOTAL	1500.0

Sectorial distribution

	MECU	Total
Transport	958.5	65.3%
Environment	469.5	32.0%
Education	39.0	2.7%

(Non included a global loan of 33 MECU for Northern Ireland as the global loan covers all priority sectors)



The Financial Mechanism Committee has approved applications relating to total EIB loans of ECU 1,500 million corresponding to 100% of the total EIB loan portfolio for which the interest rebate facility has been made available.

As of 31 December 1999, the EIB loans disbursement benefiting from interest rebates amounted to EUR 1270.196 million, corresponding to 85 % of the total facility.

2.2. The approval of grants and interest rebates from 1.7.98 to 31.12.98

The following **grant applications**, amounting to ECU 118.76 million, were approved:

Greece

Greek Monasteries Rehabilitation B

ECU 5.86 million for rehabilitation, reconstruction, conservation and restoration works in Monasteries of Dochiariou (ECU 1.77 million), Pantokratoros (ECU 0.63 million), Vatopediou (ECU 2.46 million) and in the Skete of St. Andreas (ECU 1.00 million);

Greek Monasteries Rehabilitation C

ECU 7.39 million for rehabilitation, reconstruction, conservation and restoration works in the Monasteries of Dochiariou (ECU 1.26 million), Osiou Grigoriou (ECU 0.81 million), Simonos Petra (ECU 2.19 million) and Timiou Prodromou (ECU 3.13 million);

Meghistis Lavras Monastery - Energy Project

ECU 2.50 million for the generation of sufficient additional power to provide air-conditioning to the Monastery for the preservation of its valuable library and treasure chambers; extending thus the lifetime of irreplaceable collections of manuscripts, books and antique artifacts. This phase also includes measures to safeguarding the monastery's facilities against theft and fire as well as ancillary works like maintenance to existing building installations;

Gazi Sewerage

ECU 2.29 million for a primary sewer and a connection of this primary sewer to the Heraclion sewage system;

Thalassocosmos – Cretaquarium project

ECU 5.63 million for the construction and operation of a sea water aquarium for research, educational and tourism purposes; the aquarium will be located close to Heraclion, Crete.

Thessaloniki Science Centre

ECU 13.78 million for the relocation and expansion of the existing Technology Museum of Thessaloniki into a new Technology Museum and Science Centre based on the new concept of science-technology centres combining educational and entertainment functions with the aim of expanding knowledge.

Macedonian Museum of Contemporary Art

ECU 2.37 million for the extension of the existing museum and partial refurbishment of the existing building, including also the installation of air-conditioning as well as fire and intrusion security systems.

Ano Liossia Regional Park Development

ECU 12.4 million for the creation of a regional leisure park of 31 ha. in the flood threatened zone of Ano Liossia, north-west of Athens, being one of the less-developed and poorest areas of the Attica region. As such, the project also embraces certain measures of environmental protection (flood remedying, recation of green areas).

Ierissos Multipurpose Cultural Centre

ECU 1.04 million for the construction of a multipurpose cultural facility in Ierissos (small town in Halkidiki, Northern Greece) intended to host exhibitions and presentations and provide information on Byzantine and modern art and music related to Ierissos and Mount Ahtos.

Portugal

Urban Rehabilitation Alte

ECU 4.9 million for road works, renovation of typical village buildings, a new local professional training school and a multi-purpose hall. The project concerns the integrated rehabilitation of the village of Alte.

Urban Rehabilitation Porto

ECU 42.2 million for 6 sub-projects concentrated around the historical centre of Porto. Project works include road improvements to encourage inner urban development and ease traffic congestion and to improve quality of life and attractiveness of the urban environment for locals and tourists alike, with measures including renovation of historic buildings and provision of new tourist attractions. All sub-projects are part of Porto's Municipal Master Plan and Campanhã Strategic Plan.

Almada Waste Water Treatment Plant

ECU 7,821,280 for a tertiary sewerage treatment plant based an activated sludge process. The project is a component of the municipal master plan of Almada.

Spain

Renovación Urbana La Carolina

ECU 2.5 million for the renovation of a main avenue, installation of traffic lights, improvement of public street lighting and road re-paving and associated works and improvement of footpaths.

Sevilla Medio Ambiente

ECU 8,065,778 for a part of an investment package designed to enhance the urban environment and make Sevilla a more attractive town. The subprojects financed by the

Financial Mechanism comprise i.a. fencing and rehabilitation of gardens, afforestation of a ring road, cleaning and afforestation of degraded municipal land, installation of pneumatic waste collection and greening of one of the feeder roads.

Decommitments and recommitments were made for several projects in order to optimise the beneficiaries' use of funds.

The following **interest rebate applications**, amounting to a total loan amount of ECU 236.1 million were approved:

Greece

East Egnatia Motorway

ECU 77.2 million for two sections on the eastern part of the trunk road (Kavala bypass and Komotini – Kipi).

Northern Ireland

Global Loans

ECU 33 million for financing of investments in priority sectors of environmental protection, including urban renewal, forestry, heritage and restoration of historical buildings, transport and transport infrastructure and education and training.

Portugal

Metro do Porto Light Metro

ECU 71.7 million for the creation of a light metro network to serve the Area Metropolitana do Porto.

Spain

ICO Environmental Global Loan III

ECU 54,184,009 for financing of small and medium-scale environmental investments undertaken by private and public entities.

Limited decommitments and recommitments were made for several projects in order to optimise the beneficiaries' use of funds.

2.3. The implementation of the projects as per 31 December 1999

Grants as per 31 December 1999

Of the 56 grant projects, 7 had been fully disbursed, 35 were under disbursements and for 14 projects no disbursements had been made as at 31 December 1999. The grant disbursements and the still undisbursed amounts for each category of projects are shown in the table below.

(*) Excluding technical assistance disbursements (in total EUR 104330) for which earmarking per project is not available.

Grants as per 31 December 1999

	Number of projects	Disbursed amount in EUR	Remains to be disbursed in EUR	Total	%
Fully disbursed	7	73 564 321	0	73 564 321	15%
Under disbursement	35	158 350 636	185 523 311	343 873 947	71%
Not yet under disbursement	14	0	67 251 280	67 251 280	14%
<i>Total(*)</i>	56	231 914 957	252 774 591	484 689 548	100%

The grant disbursements follow the physical progress of project implementation, and the last grant disbursement cannot be made prior to documented project completion. Consequently, the grant disbursements are expected to take place until ult. 2002, for a few projects even later.

An ultimate deadline for disbursement has been stipulated in the commitment letters and the grant agreements. This deadline allows for a delay of up to 24 months after scheduled physical project completion.

Interest Rebates as per 31 December 1999

Of the 37 projects benefiting from interest rebates, 28 had been fully disbursed, 7 were under disbursements and for 2 no disbursement had been made as at 31 December 1999. The loan disbursements and amounts not yet disbursed for each category of projects are shown in the table below.

Loans benefiting from interest rebates as per 31 December 1999

	Number of projects	Disbursed amount in EUR	Remains to be disbursed in EUR	Total	%
Fully disbursed	28	1 062 721 202	0	1 062 721 202	71%
Under disbursement	7	207 474 511	119 596 087	327 070 598	22%
Not yet under disbursement	2	0	110 200 000	110 200 000	7%
<i>Total</i>	37	1 270 195 713	229 796 087	1 499 991 800	100%

It is expected that all the remaining disbursements for partly disbursed as well as undisbursed commitments will be disbursed before year end 2000.

2.4. The funding of the Financial Mechanism

The Act of Accession (Articles 83, 111, 136) of the EU specifies that the shares in the Mechanism of the new Member States in the Mechanism are to be met from the general budget of the European Communities. On a proposal from the Commission (COM(94) 398), the financial perspectives were already reworked accordingly by adding a specific heading under "Structural Activities". The budget adopted for the years 1994 to 1999 contained a heading with the relevant comments (B2-401). The amount forecast for each year from 1994 to 1998 was ECU 108 million and for 1999 EUR 5 million.

As far as the actual payments are concerned, taking over the shares of the new Member States means complying with the terms of Article 4A of the Cooperation Agreement

between the EFTA countries and the EIB dated 30 June 1992, as amended by the amending protocol of 18 June 1993.

In line with these procedures, the contribution for 1994 to 1998 and the shares between the participating EFTA countries and the Community were decided by the Financial Mechanism Committee. These contributions were calculated in accordance with the gross national product at market prices using data for the last three calendar years.

2.4.1. The annual contributions from the donors

At the creation of the Financial Mechanism a first estimate was made corresponding to an annual instalment of ECU 130 million. However, during the years 1994-1996, initial funding and replenishment of ECU 110 million of the Financial Mechanism took place as shown in the table below together with the aggregated contributions during the same period.

Article 4 of the Cooperation Agreement states that the participating EFTA States and the Community budget shall deposit the amounts necessary to meet the commitment schedules, the consequent disbursements and the associated administrative costs of the interest payments and the grants. The Bank and the Committee shall review the amount of grants and the interest subsidies disbursed in order to determine the amounts of the subsequent instalments to be deposited by the participating EFTA States and the Commission. Any amount outstanding at the time of termination of operations shall be repaid to the latest participating EFTA States and the Community budget.

On 17 December 1996 and on 16 December 1997, the Financial Mechanism Committee decided that the contributions from the donors would have to rise accordingly in order to meet the final obligations. Even though all the contributions have not been used it was important to keep a reasonable contribution to the Mechanism account each year in order to be able to match reasonably the final obligations in terms of commitments at the end of 1998. An increase from ECU 110 million to ECU 130 million in the replenishment for 1997 and a replenishment of ECU 135 million for 1998 have been decided.

For 1999, no replenishment was deemed necessary. The Committee concluded from a review of the Financial Mechanism's future payment obligations that future disbursement obligations would be met by the previously generated liquidity together with past and future interest earnings made on it.

2.4.2 The share between the Commission and the participating EFTA

The cost sharing of the initial funding and replenishment of the Financial Mechanism calculated in accordance with the gross national product at market prices using data for the last three calendar years was the following:

ECU million

	Iceland	Norway	Liechtenstein	Austria	Finland	Sweden	Total
				Community budget from 1995			
1994	1.078	18.436	0.187	29.348	20.526	40.425	110
	(0.98 %)	(16.76 %)	(0.17 %)	(26.68 %)	(18.66 %)	(36.75 %)	
				Total:	(82.09 %)		
1995	1.111	19.063	0.198		89.628 ¹		110
	(1.01 %)	(17.33 %)	(0.18 %)		(81.48 %)		
1996	1.122	21.604	0.198		87.076		110
	(1.02 %)	(19.64 %)	(0.18 %)		(79.16 %)		
1997	1.300	25.935	0.247		102.518		130
	(1.00 %)	(19.95 %)	(0.19 %)		(78.86 %)		
1998	1.296	27.916	0.2565		106.2315		135
	(0.96 %)	(20.16 %)	(0.19 %)		(78.69 %)		
Total	4.907	112.254	1.0865		475.7525		595

¹ The Commission did not request a transfer of Liechtenstein's reimbursement in August 1995. Accordingly, this amount was deducted from the third instalment in 1996.

2.5. The management of the Financial Mechanism liquidity

The Financial Mechanism liquidity was initially managed solely through a Financial Mechanism account at the EIB. On 9 July 1999 a Fund Management Agreement was concluded between the Financial Mechanism Committee and the European Community represented by the Commission of the European Communities acting through the Economic and Financial Affairs DG. Since 15 July 1999, the Financial Mechanism liquidity is managed by the Financial Affairs DG and disbursement instructions are sent by the EIB to the Fund manager. Transfers of funds to the Beneficiary (respectively to the borrower in case of interest rebates) take place via a designed EIB Financial Mechanism disbursement account.

In summary, the account transactions from 30 June 1998 were as follows:

Management by the EIB

ECU/EUR

<i>Balance as of 30 June 1998</i>	399 184 268.33
<i>Crediting</i>	
Interest	12 585 177.73
<i>Debiting</i>	
Disbursements (grants, interest rebates)	89 117 833.74
Liaison Officer function cost	523 148.00
Miscellaneous	26 005.42
<i>Balance as of 15 July 1999</i>	322 102 458.90

Management by the Economic and Financial Affairs DG.

EUR

<i>Balance as of 15 July 1999</i>	322 102 458.90
<i>Crediting</i>	
Net income (<i>yield on the invested capital</i>)	4 271 495.00
<i>Debiting</i>	
Disbursement to <i>EIB</i> (<i>grants, interest rebates</i>)	34 010 869.49
<i>Balance as of 31 December 1999</i>	292 363 084.41

2.6. Coordination and complementarity with other financial instruments of the European Union

The Commission has ensured, within the framework of the partnership, coordination and consistency between the projects carried out under the Financial Mechanism and measures undertaken by the Structural Funds, the Cohesion Fund, the European Investment Bank and the other financial instruments of the European Union.

In that respect, operating rules concerning the combination and overlapping of the Financial Mechanism aid with other Community assistance had been clearly defined in the "Operational arrangements" concluded between the Commission and the European Investment Bank on 9 March 1994.