



COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 28.10.2005  
COM(2005) 533 final

**REPORT FROM THE COMMISSION**

**16th ANNUAL REPORT ON IMPLEMENTATION OF STRUCTURAL FUNDS 2004**

**{SEC(2005)1348}**

## TABLE OF CONTENTS

1.	Introduction .....	3
2.	Analysis of Implementation in 2004 .....	3
3.	Consistency and Coordination .....	7
4.	Evaluations .....	9
5.	Controls .....	9
6.	Committees Assisting the Commission .....	11

## REPORT FROM THE COMMISSION

### 16th ANNUAL REPORT ON IMPLEMENTATION OF STRUCTURAL FUNDS 2004

This report is presented in accordance with Article 45(2) of Regulation (EC) n° 1260/1999 laying down general provisions on the Structural Funds. It is the 16<sup>th</sup> annual report covering the Structural Fund activities during 2004.

The informations outlined in this report are presented in greater detail in the Commission Staff Working paper.

#### 1. INTRODUCTION

The year 2004 was marked by three important events in the life of the current generation of European programmes: the allocation of the performance reserve; the mid-term review of the programmes in the EU 15; the enlargement of the Union giving rise to 43 additional programmes mostly in the category of less developed regions. For the latter, Community aid totalling EUR 24 billion (at current prices) has been allocated for the period 2004-06.

Meanwhile, outside the framework of the current programmes, negotiations were launched on the new regulatory framework for cohesion policy for 2007-2013. The Commission's proposals to the Parliament and to the Council are intended to confirm the role of cohesion policy as the principal budgetary instrument at Community level for the realisation of the Lisbon competitiveness agenda with estimated budgetary requirements of some EUR 336.1 billion over 7 years for three priority objectives: *Convergence*, in the least developed regions; *Competitiveness and Employment*, in the other regions; *European territorial co-operation*, across borders.

#### 2. ANALYSIS OF IMPLEMENTATION IN 2004

##### 2.1. Budgetary Implementation

###### 2.1.1. Commitments

In 2004 the available commitment appropriations for the Structural Funds totalled EUR 35 353 million, i.e. 32% of the EU budget. The commitment appropriations for the ten new Member States amounted to EUR 3 812 million. Commitments actually made totalled EUR 35 212 million, practically 100% of the available appropriations (reflecting the system of essentially automatic commitments). All of the allocation foreseen in the Copenhagen agreement for the EU-10 programmes was committed.

###### 2.1.2. Payments

Payments on commitments in 2004 were the highest ever recorded for the Structural Funds, equivalent to EUR 31 516 million euros, or 99% of the available payment

appropriations. This represented a significant acceleration in the realisation of the current generation of programmes in the fifth year of the programming period.

This reflected more proactive management by the authorities at Community, national and regional level, helping to keep the programmes on track for a successful implementation over the 7 years, 2000-06.

For Objective 2, 100% of the available payment credits were used. For Objectives 1 and 3, as well as for the Community Initiatives, the figure was also close to 100%. For the FIFG (outside Objective 1 programmes) the figure was 83%, an improvement on the performance of previous years. On the other hand, the figure for innovative measures and technical assistance decreased from 90% in 2003 to 78% in 2004. At the level of each Fund, the ERDF, EAGGF-Guidance and ESF all achieved high payment levels (between 98% and 100% of available credits). For the FIFG the figure was 81% in 2004, down from 86% in 2003.

In the ten new Member States, the payments in 2004 largely consisted, as expected, of advances to create the rolling funds to help programme realisation<sup>1</sup>. They amounted to EUR 1 550 million. The total amount of interim payments (concerning only Objective 1 programmes) was EUR 23.7 million.

### 2.1.3. *Implementation by Member States (EU 15)*

In 2004, the accelerated implementation allowed seven out of the fifteen Member States to decrease their outstanding commitments in absolute terms. Absolute reductions in this respect were highest for Spain (EUR 500 million) and Ireland (EUR 361 million). Reductions were also achieved on accumulated commitments in Denmark, Finland, Luxembourg, Portugal and Sweden. Five Member States accounted for almost three-quarters of all payments, in order, Spain, Germany, Italy, Portugal and Greece. In the Fifteen, these are the major beneficiaries of EU cohesion policy.

### 2.1.4. *“N+2” rule<sup>2</sup>*

Decommitments of resources in the absence of a valid payment claim with the time delays set by the n+2 at the end of 2004 were minor relative to total resources deployed. For the ERDF, the figure amounted to an estimated EUR 56.1 million for 26 programmes. Most concerned INTERREG programmes which, involving management arrangements across national borders, are more difficult to execute. The figure represented only 0.3% of the annual commitment for ERDF. The figures will be definitive once the agreement of the Member State concerned will be received.

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<sup>1</sup> The advances for EU-10 Structural Fund programmes amount to 16% of the total commitment envelope of € 16 billion for the period 2004-2006, or € 2.56 billion, split between 2004 (10%) and 2005 (6%).

<sup>2</sup> Art. 31 (2), par.2 of the Regulation N° 1260/1999 provides for definition of the “N+2” rule: The Commission shall automatically decommit any part of a commitment which has not been settled by the payment on account or for which it has not received an acceptable payment application, as defined in Article 32(3), by the end of the second year following the year of commitment or, where appropriate and for the amounts concerned, following the date of a subsequent Commission decision necessary in order to authorise a measure or an operation or by the end of the deadline for the transmission of the final report referred to in Article 37(1); the contribution from the Funds to that assistance shall be reduced by that amount.

Estimates for the other Structural Funds gave slightly higher rates of de-commitment: for the ESF the figure was EUR 123.5 million, or 1,3% of the annual commitment, for the EAGGF EUR 44.4 million, or 1.5% of the annual commitment, and for the FIFG EUR 70.2 million or 12.5% of the annual commitment.

For all 4 Funds taken together, the overall result should equate to a de-commitment of less than 1% (around 0,96%) of the total 2002 annual commitment, suggesting that the n+2 rule is performing the role for which it was intended by encouraging a more even pattern in financial execution of the programmes year-on-year.

## **2.2. Programme Implementation**

### *2.2.1. Objective 1 and 2*

#### *2.2.1.1. EU 15*

In 2004, an important event was the allocation of the performance reserve followed by the mid-term review. This innovation in the programmes for 2000-06 also allowed Member States to adapt programmes to changes in the general socio-economic situation or to changing labour market conditions and to take on board the results of the mid-term evaluations. In general, this provided the opportunity to contribute better to the priorities of the revised European Employment Strategy (EES) and to the achievement of the Lisbon objectives. The mid-term review also allowed Member States to introduce changes in the structure of the programmes, for example, to simplify implementation.

#### *2.2.1.2. New Member States*

Experience of the first year of programme implementation in EU-10, begun in May, suggests that project selection activity is well under way in most cases. Encouragingly, the amount of project applications for some measures exceeded the financial resources available in the programmes. At the same time, challenges remain such as raising the quality of projects and ensuring a balanced geographic coverage, as well as the need to address deficiencies in management.

### *2.2.2. Objective 3*

A main message arising from the mid-term evaluation reports is that the strategy initially agreed for the ESF interventions remains relevant in the majority of the cases, and that it continues to contribute to the implementation of the European Employment Strategy. Recommendations mainly concerned fine-tuning of the programmes. Many of the changes introduced aimed at simplifying the programmes, increasing flexibility to respond to socio-economic challenges or reducing the allocation to measures where needs appear to be less than expected as reflected in under-spending.

### *2.2.3. Fisheries outside Objective 1*

The mid-term review provided the opportunity to adapt the programmes to the requirements of the reform of the Common Fisheries Policy in particular regarding the discontinuation of aid for the renewal of fishing vessels and the permanent transfer of Community vessels to non-member countries, which is no longer allowed

from 2005; changes in the terms and conditions for aid from Member States to fishermen and ship owners who temporarily cease their fishing activity; changes in the aid for the retraining of fishermen which is widened to include diversification into other activities while they continue to fish part-time.

#### 2.2.4. *Community Initiatives*

##### 2.2.4.1. Interreg

With the accession of ten new Member States, 11 new cross-border programmes were launched and amendments were introduced to 17 programmes to add the new Member States among the participants. The additional ERDF funding for INTERREG for the new Member States totals EUR 479 million for the period 2004-2006. Together with the indexation funds for the period 2004-2006, this has brought the ERDF budget for INTERREG III to some EUR 5.8 billion. Many programmes were modified in 2004 as a result of the mid-term review process.

##### 2.2.4.2. Leader+

The payments in 2004 for the 73 Leader+ programmes amounted to 238 Million EUR from EAGGF Guidance. More than 20 000 projects were approved since the beginning of the programming period by the Local Action Groups mainly within the domains of tourism, support to SMEs, renovation and development of villages and rural heritage, basic services to the rural population and rural economy. For the new Member States, the possibility exists to implement a Leader+-type measure under their rural development programmes.

##### 2.2.4.3. URBAN

The year 2004 was largely devoted to the launching of work on thematic networks (programme URBACT). Fifteen thematic networks have been approved, each organised around different themes. Participation is high with 150 cities as partners including 36 cities in the new Member States. New results for the Urban Audit were published<sup>3</sup>.

##### 2.2.4.4. EQUAL

In 2004, the first round of implementation of the Partnerships for Development (PDD) came to an end and the second phase was launched. A new focus was introduced involving support activities to strengthen institutional capacity and efficiency in national managing teams for EQUAL. Several EQUAL publications were produced and are available electronically<sup>4</sup>.

In 2004, 27 new decisions were adopted to incorporate changes as result of the mid-term review and the indexation or to draw up new Community Initiative Programmes (PIC) for the new Member States.

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<sup>3</sup> <http://www.urbandaudit.org>

<sup>4</sup> [www.europa.eu.int/equal](http://www.europa.eu.int/equal)

### 2.2.5. *Innovative Actions*

#### 2.2.5.1. ERDF

Some 139 programmes were approved with total amount of EUR 660 million, of which EUR 344 million under the ERDF. A major event in 2004 was the prize-giving ceremony for the winners of the European Regional Innovation Awards competition<sup>5</sup>. Comprehensive checklists and models for the amendment and eventual closure of the programmes were prepared during 2004 as part of the drive to ensure sound financial management and to help identify best practices.

#### 2.2.5.2. ESF

Some 35 projects in the field of social dialogue were finalised. 33 projects were selected under the first round of a call for proposals on “*Innovative approaches to the management of change*”. In order to assist in the mainstreaming of results, the Commission launched a call for proposals on the “*transfer and dissemination of innovation from ESF Article 6 projects*”.

#### 2.2.5.3. FIGG

The year 2004 mostly concerned the implementation of projects selected in previous years. Three projects were brought to a close. An ex-post evaluation of the results of projects selected within measure “Innovative actions” was launched.

## 3. CONSISTENCY AND COORDINATION

### 3.1. Consistency with other Community Policies

#### 3.1.1. *Competition*

Regulation (EC) No 1260/1999 states that assistance approved by the Commission must include all the elements required for the *ex-ante* assessment of the compatibility of state aids with the common market. Accordingly, during 2004 the Commission paid particular attention to ensuring compliance with state aid rules, firstly, in the programmes for the new Member States for 2004-06, and, secondly, in the programmes for the Fifteen, including the assessment of competition policy aspects of certain major projects as defined by Articles 25 and 26 of Regulation 1260/1999.

#### 3.1.2. *Environment*

For the ten new Member States, some EUR 720 million are estimated to be spent on environment priorities for the period 2004-6 which represents 4.8% of the EUR 15 billion allocated for the Structural Funds for the new Member States compared with 13% out of EUR 196 billion in the EU15 for the period 2000-6. All new Member States have water and waste management projects as important priorities.

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<sup>5</sup> [http://europa.eu.int/comm/regional\\_policy/innovation/concours\\_en.htm](http://europa.eu.int/comm/regional_policy/innovation/concours_en.htm)

A particular challenge for the new Member States concerns the application of the Environmental Impact Assessment Directive and the Birds and Habitats Directives (for the Natura 2000 network).

### *3.1.3. Internal Market*

Greater decentralisation has been introduced into the management of the Structural Funds, increasing the responsibility of the Member States for the award of contracts financed by the Community Funds. To ensure that these procedures comply with Community rules, the Commission has encouraged national authorities to adopt various preventive measures such as appropriate training for staff involved in awarding contracts and issued procedural guidelines.

### *3.1.4. Transport*

The revised Community guidelines for the development of the Trans-European network were adopted on 29 April 2004<sup>6</sup>. These Guidelines comprise 30 priority projects of European interest across EU-25 with cost of around EUR 225 billion. As projects of European interest, they help to focus funding from the Structural Funds in this field, especially in the regions covered by Objective 1.

## **3.2. Coordination of Instruments**

### *3.2.1. The Structural Funds and the Cohesion Fund*

There are now 13 Member States eligible for support under the Cohesion Fund (the ten new Member States, Portugal, Spain and Greece). Ireland was no longer eligible for support since the 2003 review which found that GNI per capita had grown above the threshold level.

The principal coordination instrument between the interventions of the Cohesion Fund and Structural Funds is the strategic reference framework (SRF). The ten new Member States presented their SRF during the first semester of 2004.

### *3.2.2. The Structural Funds and the EIB/EIF*

In 2004, cooperation between the Commission and the EIB was further intensified in terms of dialogue and preparatory work for reinforced cooperation in the next programming period 2007-2013. The Bank assisted the Commission in appraising 15 major ERDF projects and 25 Cohesion Fund projects. At the end of 2004, technical negotiations began between the Commission and the EIB on how to strengthen cooperation in order to offer the Member States additional help to prepare quality projects with a view to accelerating execution. The negotiations are expected to conclude in 2005.

In 2004, the European Investment Bank lent a total of EUR 43.2bn (in 2003, 42.3bn) for projects strengthening the European Union's political objectives. Financing in the EU-25 Member States totalled EUR 39.7bn.

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<sup>6</sup> Decision N° 884/2004/EC amending Decision N° 1692/96/EC.

In 2004, the European Investment Fund (EIF) acquired holdings worth EUR 358 million in venture capital funds, bringing its aggregate portfolio to EUR 2.8bn, and provided a total of EUR 1.4bn in guarantees for SME portfolios of financial intermediaries.

The total lending of EUR 28.5bn for regional development represents some 72% of the EIB's aggregate lending within the EU-25.

## **4. EVALUATIONS**

### **4.1. Mid-Term Evaluation**

The mid term evaluations were based on a mix of methodologies, including desk research, primary research and, for larger programmes, some macro-economic modelling. Significant improvements were evident in the quality and rigour of the evaluations. The results were used to improve the implementation of Structural Funds, particularly to develop further indicators, to help implement horizontal priorities and to improve project selection criteria.

### **4.2. Performance Reserve**

The performance reserve is an innovation for the 2000-2006 period. In total, over EUR 8 billion was allocated to Structural Fund programmes (Community Initiatives were excluded)<sup>7</sup>. The performance of each programme, priority or measure was assessed on the basis of financial, effectiveness and management indicators. As a general rule, the majority of programmes and priorities performed sufficiently well to merit an allocation from the reserve, although the sums involved varied considerably in the light of the review results.

A major strength of the process was to create an incentive for capacity building in good management practices. There was some diversity between Member States in the methods used for assessing performance and for making allocations reflecting differing circumstances.

### **4.3. Other Evaluations**

During 2004, the Commission carried out or completed a series of ex-post evaluations as well as a strategic evaluation on the contribution of the Structural Funds to the Lisbon strategy.

## **5. CONTROLS**

### **5.1. ERDF**

Closure audits on the 1994-99 period have been completed on 56 programmes covering all Member States. In a limited number of cases, the audit findings led to the suspension of the closure process.

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<sup>7</sup> See annex-part 5: Performance Reserve: Range of Percentage Allocations, Objective 1 and Objective 2.

A new audit enquiry on the 2000-06 period was launched to verify that the systems work effectively in practice. Eight audits were carried out in 2004 in different Member States.

Co-ordination meetings were organised during the first part of the year with EU-15 Member States to discuss control issues with the national control bodies covering all the Funds.

As regards the new Member States, the audit work concerned the assessment of the systems descriptions submitted under Article 5 of Regulation 438/2001.

## **5.2. ESF**

The 2004 risk assessment focused primarily on those programmes which represented the highest financial impact factor. 42 system audits were carried out in the EU-15 Member States and 17 coordination meetings were held with the designated national Article 10 and 15 control authorities.

System descriptions were reviewed following Article 5 reports, supplemented by 5 on-the-spot, fact-finding missions in the new Member States. Three closure audits of the 94-99 programmes were carried during the year.

## **5.3. EAGGF**

In 2004, five missions in Member States aimed at closure audits of the 94-99 programmes and covering the biggest national programmes for Objective 5a measures were carried out.

Some 17 audit missions were carried out in Member States to identify certain situations which were held to be unsatisfactory (representing some 2-3% of the EAGGF payments in 2004) to be followed by appropriate corrections.

## **5.4. FIG**

A total of 8 on-the-spot controls were carried out in 2004. Five on-the-spot audits concerned the verification of management and control systems of 2000-2006 programmes (EUR 407 Million ) in four Member States. One FIG audit concerned the closure of 1994-1999 programmes (EUR 1,1 Million). Two projects of innovative actions were audited for an amount of FIG aid of EUR 236.000. In total nineteen structural projects were audited (EUR 5,35 Million), FIG aid amounting to EUR 1,8 Million.

## **5.5. OLAF**

During 2004, OLAF undertook 29 operational missions in the Member States. Some 22 of these missions related to the controls and verifications on the spot effected by the Commission for the protection of the EC financial interests against fraud or other irregularities. Seven other missions were to assist either the national administrations or the legal authorities.

Sixteen missions concerned the ESF, three missions for the ERDF, two missions concerned FIG and one regarding the EAGGF Guidance Section.

In 2004, Member States themselves communicated to the Commission, in accordance with the Regulation (EC) No 1681/94, some 3037<sup>8</sup> cases of irregularities involving 431 million euros which have affected payments incurred during both periods 1994-1999 and 2000-2006. Both amounts and number of cases have increased comparing to the year 2003. This is likely to affect the finalisation of the process leading to the closure of programmes relating to the period 1994-1999. It shows at the same time an encouraging increase in awareness among Member States of their obligations in this field, leading to better detection and reporting as opposed to an underlying rise in the incidence of irregularities.

## **6. COMMITTEES ASSISTING THE COMMISSION**

### **6.1. Committee on the Development and Conversion of Regions (CDCR)**

The CDCR in its role as management committee gave favourable opinions on amendment of the guidelines for INTERREG III and INTERREG IIIC and on Commission Regulation (EC) N° 448/2004 as regards the eligibility of expenditure on operations co-financed by the Structural Funds. As a consultative committee, the CDCR considered the Technical assistance measures planned for 2005, approval of the lists of the areas eligible under Objective 2 in the ten new Member States, and the approval of programming documents for the new Member States.

### **6.2. ESF Committee**

The Committee adopted 3 opinions: on the adoption of Commission Regulation (EC) N° 448/2004, on the programming documents of the new Member States and on the future regulatory framework for the Structural Funds.

### **6.3. Committee on Agricultural Structures and Rural Development (STAR)**

The STAR Committee met 11 times in 2004 and gave favourable opinions on 52 modifications of rural development programmes under Article 44 (2) of Council Regulation (EC) N° 1257/1999 and 5 on rural development programmes under Article 4 of Council Regulation (EC) N° 1268/1999.

### **6.4. Committee on Structures for Fisheries and Aquaculture (CSFA)**

The Committee was consulted on the following subjects: the draft Regulation n° 448/2004, FIFG programming documents of the 10 new Member States, the innovative actions projects, the conference on the future of FIFG, the interpretation of Article 16 of Regulation 2797/99 and on the draft rules of procedure of the Committee.

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<sup>8</sup> See also Annual Report 2004 on the protection of the Community financial interests –the fight against fraud, [http://europa.eu.int/comm/anti\\_fraud/reports/index\\_en.html](http://europa.eu.int/comm/anti_fraud/reports/index_en.html).