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ANNUAL REPORT ON THE INSTRUMENT FOR STRUCTURAL POLICIES FOR
PRE-ACCESSION (ISPA) 2010

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1. INTRODUCTION

Following the Brussels European Council in June 2004, which awarded *candidate country* status to Croatia, the country benefited from ISPA as of 1st January 2005. Croatia thus followed the previous ISPA beneficiary countries which received ISPA assistance from when the instrument was launched in 2000. On 1st January 2007 Bulgaria and Romania became members of the European Union and ceased being beneficiaries of pre-accession assistance including ISPA. The accession of these two countries left Croatia as the only recipient of ISPA assistance.

This report therefore only covers the ISPA activities carried out by Croatia.

2010 witnessed the successful physical completion of the first two ISPA projects. Due to delays accumulated in four ISPA measures it was necessary to extend the end date of eligibility for these measures by one year until the end of 2011. As a result of lower than expected contract prices, four measures were modified to enable an increase in the scope of work to be financed by ISPA funds, and/or to increase the co-financing rate.

In 2010 the national authorities concentrated on actual physical implementation, project management, monitoring and payments.

Implementation of ISPA in 2010 was parallel to the implementation of operational programmes funded by the Instrument for Pre-Accession Assistance (IPA) and the extensive preparations for future cohesion policy (accession negotiations under chapter 22: *Regional policy and coordination of structural instruments*). These three parallel processes required considerable input from the national administration.

2. ISPA BUDGET

In accordance with the Commission's activity based accounting system, the budget for the ISPA was provided for by two budget lines: the functional budget line B13.01.04.02 and the operational budget line 13.05.01.01. The first line contains the means for covering Technical Assistance (TA) administrative expenses mainly for reinforcing the Delegation of the European Union to the Republic of Croatia. This ended in 2006. The second budget line encompasses payment appropriations made available for the effective implementation and operation of ISPA for Croatia.

Budget line 13.05.01.01 covers all expenses for co-financing infrastructure projects (measures). A total of EUR 14,659,692.82 was paid out from this line in 2010.

Table 1: ISPA budget in 2010 – in Euro

Budget line	Payments implemented
Functional budget line B13.01.04.02 (closed in 2006)	0
Operational budget line 13.05.01.01	14,659,692.82
Total	14,659,692.82

Project funding

3. NEW ISPA PROJECTS

No new ISPA projects were adopted in 2010.

4. NEW COMMITMENTS

No new commitments were made in 2010 for projects either in the environment or transport sectors since the ISPA ended in 2006.

5. PROJECTS FUNDED BETWEEN 2005-2010

Between 2005 and 2006, the Commission approved a total of 6 projects on the basis of proposals submitted by Croatia. Of these projects, 3 concern the environment sector, 2 the transport sector, and 1 horizontal TA measure (for the organisation of the statutory monitoring committees and supporting ISPA implementing agencies). The total eligible investment cost of these projects is EUR 107,474,736 with a total of EUR 59,000,000 or 54.8%, being allocated as ISPA grants. By the end of 2006, the Commission had committed 100% of the ISPA funds set aside for Croatia covering the period 2005 to 2006 with the commitments distributed in a balanced manner between the environment and transport sectors.

Table 2: Projects approved in Croatia in 2005-2006¹ – in Euro

Sector	Project decisions N°	Eligible cost	ISPA contribution	Average grant rate %	Commitments
Environment	3	46,287,701	29,466,355	64	29,466,355
Transport	2	60,924,700	29,271,310	48	29,271,310
Horizontal TA	1	262,335	262,335	100	262,335
Total	6	107,474,736	59,000,000	55	59,000,000

6. PAYMENTS

Generally, payments for each investment project consist of two advance payments totalling 20% of the ISPA contribution, as well of intermediate payments (i.e. reimbursements) of up to 80% (and in exceptional cases up to 90%) of the contribution, as well as payment of the final balance after closure. A total of EUR 14.65 million in payments were made in 2010 for the ISPA projects approved in Croatia, representing 24.8 % of the corresponding ISPA grants. The amount paid represents a significant increase (more than doubling) in amounts paid out in comparison with the figure for 2009 (EUR 6,76 million).

96% of the payment requests for the year 2010 were for interim payments which is linked to the advanced implementation of ISPA.

¹ No projects have been approved since 2006 due to the ending in that year of the ISPA programme.

By the end of the period 2005-2010, a total of EUR 35,5 million had been paid out to Croatia, representing 60% of the budgetary commitments implemented in that period (EUR 59 million).

Table 3: Payments – in Euro

Sector	2005-2009	2010	Total 2005-2010
Environment	7,877,349.62	4,001,450.43	11,878,800.05
Transport	12,758,806.09	10,658,242.39	23,417,048.00
TA	209,868.00	0	209,868.00
Total	20,846,023.71	14,659,692.82	35,505,716.05

7. SUMMARY TABLES

Table 4 presented below provides an overview of the ISPA interventions for both the year 2010 and for the period 2005-2010.

Table 4: Projects decided in Croatia in 2005-2010 – in Euro

Sub-sector	N° of projects	Eligible cost	ISPA contribution	2010		2005 – 2010	
				Commitme	Payments	Commitme	Payments
Environment							
Water	0	0	0	0	0	0	0
Water & wastewater	1	36,000,000	22,500,000	0	2,950,858.49	22,500,000	9,668,557.17
Wastewater	0	0	0	0	0	0	0
Solid waste	1	8,823,601	6,000,049	0	837,193.08	6,000,049	1,437,198.08
Air quality	0	0	0	0	0	0	0
Horizontal	1	1,464,100	966,306	0	213,398.86	966,306	773,044.80
Sector total	3	46,287,701	29,466,355	0	4,001,450.43	29,466,355	11,878,800.05
Transport							
Road	0	0	0	0	0	0	0
Rail	1	60,182,962	28,789,180	0	10,465,390.39	28,789,180	23,031,344.00
Road and rail	0	0	0	0	0	0	0
Inland waterways	0	0	0	0	0	0	0
Airports	0	0	0	0	0	0	0
Horizontal	1	741,738	482,130	0	192,852.00	482,130	385,704.00
Sector total	2	60,924,700	29,271,310	0	10,658,242.39	29,271,310	23,417,048
Horizontal							
TA	1	262,335	262,335	0	0	262,335	209,868
TOTAL	6	107,474,736	59,000,000	0	14,659,692.82	59,000,000	35,505,716.05

Technical assistance

8. FORMS AND METHODS OF PROVIDING TECHNICAL ASSISTANCE

Two types of technical assistance measures are utilised:

- technical assistance which is carried out on the initiative of the beneficiary country and which is directly related to project funding, e.g. project preparation/development, technical assistance for implementation, and technical assistance for enhancing administrative capacity;

- technical assistance which is carried out on the initiative of the Commission and which mostly relates to activities performed by the EU Delegation, including project appraisal;

9. TECHNICAL ASSISTANCE ON THE INITIATIVE OF THE BENEFICIARY COUNTRY

Project preparation and institutional strengthening

The total number of TA measures between 2005 and 2006 stands at three. Two for project preparation, representing a total eligible cost of EUR 2,205,838 of which EUR 1,448,436 (65.6%) is being financed by ISPA. One technical assistance measure for institutional capacity building was approved in 2006, representing a total eligible cost of EUR 262,335 which is 100% financed by ISPA.

Two of the three technical assistance measures are aimed at preparing IPA project pipelines in the environment and transportation sectors. The TA measure for project preparation in transport sector was finalised in 2010. The TA measure for project preparation in environment sector is still under implementation. The third measure, finalised in 2010, was aimed at developing the institutional capacity of the CFCA to manage and implement the ISPA projects.

The two TA measures which have been finalised in 2010 reached the payments level of 80% of the ISPA contribution. The remaining balance will be paid once the closure procedure for these measures is finalised and the final payment accepted by the Commission.

**Table 5: Technical assistance measures on the initiative of Croatia
2005-2009 – in Euro**

Sub-sector	No of projects	Eligible cost	ISPA contribution	Commitments 2010	Payments 2010	Commitments 2005-10	Payments 2005-10
Environment							
Sector total	1	1,464,100	966,306	0	213,398.86	966,306	773,044.80
Transport							
Sector total	1	741,738	482,130	0	192,852.00	482,130	385,704.00
Horizontal TA							
Sector Total	1	262,335	262,335	0	0	262,335	209,868.00
TOTAL	3	2,468,173	1,710,771	0	406,250.86	1,710,771	1,368,616.80

10. TECHNICAL ASSISTANCE ON THE INITIATIVE OF THE COMMISSION

Since the beginning of ISPA, technical assistance activities carried out on the initiative, or on behalf of the Commission, have been concentrated on enabling the EU Delegation to perform its *ex-ante* control procedures (including project appraisal) in accordance with the standards required for the management of EU funds. No such technical assistance measures have been funded by ISPA since 2006. All such measures since that time have been financed from IPA.

Management and implementation

11. IMPLEMENTATION

The first two projects in Croatia were approved in December 2005 with a final four being approved in July and September 2006. By the end of 2010, physical implementation was ongoing on all the 6 ISPA projects. Two ISPA measures have been completed and for the four remaining measures the final date for eligibility has been extended until 31 December 2011². Contracted amount at the end of 2010 equals to 95.8% of the allocated amounts.

By the end of 2010 two contracts were in the evaluation stage (works and supply). Three contracts still remained to be tendered out. These were: one supply contract, one framework contract and one works contract. For the latter one there is a risk that its implementation will go beyond the end date of eligibility.

Most of the ISPA projects are now entering the final stages of implementation. As a result attention is being focused more and more on completing the measures within the given deadlines and ensuring that the ISPA measure is fully functional and fully compliant with its objectives.

12. PROJECT MONITORING

Overall monitoring and evaluation of the progress and effectiveness of ISPA implementation is ensured by regular meetings in the EU Delegation offices, monitoring reports submitted by the implementing bodies, site visits by Commission staff and formal monitoring through the twice yearly ISPA Monitoring Committee meetings held in Croatia, as well as the receipt of annual reports for each ISPA project from the implementing authority.

Two ISPA Monitoring Committees were held in Croatia in 2010; in June and November respectively. Considerable attention was given to the delays in environmental projects. The extension of eligibility dates for four ISPA measures was also thoroughly discussed in the monitoring committee.

² Following modification of Guidelines on the Closure of Cohesion Fund and Ex-ISPA projects 2000-2006 adopted in order to extend the final date of eligibility of expenditure up to 31 December 2011, similar provisions were made for the ISPA projects presently under implementation in Croatia. In Croatia one year extension was granted to four ISPA measures.

13. FINANCIAL MANAGEMENT AND CONTROL, INCLUDING *EDIS*

The principal requirements for both the financial management and control and the treatment of irregularities are governed by the provisions of the ISPA Regulation³ and of Annex III of the Financing Memorandum, as applicable under the regime of *ex-ante* control by the Commission. The key elements relate to the establishment of internal financial control systems and procedures that can ensure transparent and non-discriminatory procurement procedures, the accuracy of declared expenditure, adequate internal audit capability, sufficient audit trail and appropriate treatment of irregularities.

The EU Delegation in Zagreb continued as the main mechanism for ensuring sound financial management and control. The rejection rate for ISPA documents continued to be high which is a clear sign that still more work needs to be carried out by the Croatian authorities before confidence exists of their ability to correctly manage ISPA funds independently.

DIS

The requirement for the DIS (Decentralised Implementation System) accreditation of the implementing agency in Croatia, the CFCA, follows the provision of Article 164 of the Financial Regulation⁴. DIS accreditation was awarded by the Commission on 13th February 2006.

EDIS

Since ISPA ended in 2006 with the introduction of the Instrument for Pre Accession (IPA) the purpose of moving ISPA to EDIS (using the Extended Decentralised management Implementation System – EDIS with only *ex-post* control by the Commission) has become superfluous. Recent efforts by the Croatian authorities have therefore been concentrated on preparing the IPA structures for the move to decentralised management without *ex-ante* controls as these structures will stay in place after accession. In the meantime the EU Delegation in Croatia continues to perform its important role in supervising the daily management, implementation and monitoring of the ISPA measures.

14. RISK ASSESSMENT

The audit strategy planned for 2010 was based on the results of an analysis of the state of ISPA implementation and the related objectives of the Audit Directorate of Directorate General for Regional Policy. The audit strategy sets out the objectives which are defined by the senior management of Directorate General for Regional Policy. These objectives are defined on the basis of detailed discussions with the operational directorates during which information on potential risk is shared. The audit strategy then sets out the actions to achieve the objectives, taking account of the

³ Council Regulation (EC) No 1267/1999 of 21 June 1999 establishing an Instrument for Structural Policies for Pre-accession [OJ L 161, 26.6.1999, p. 73].

⁴ Provision, however, deleted as of 1 May 2007 by Regulation (EC, Euratom) No 1995/2006 [OJ L 390, 30.12.2006, p. 1].

risks identified. In general, risk is minimized by implementing this strategy. Audit of ISPA was carried out in Croatia in 2010.

The audit unit of DG REGIO carried out in March 2010 audit for ISPA measure *Vinkovci to Tovarnik to State Border Railway Rehabilitation*. The audit covered the implementing agency (CFCA), the final beneficiary (Croatian Railways) and the national authorising officer for the selected measure. The findings of this audit refer to 1) the delays in implementation of signalling contract, 2) delays between tender evaluation meetings and contract signature in three contracts, 3) and maintained high rejection rate by the EU Delegation within ex-ante controls.

Under the system of *ex-ante* approval, priority is given to ensuring that sufficient control procedures are put in place regarding project implementation and payments. However, the management of pre-accession funds carries an inherent risk since the funds are delivered by a variety of organisations and systems. Eligibility of expenditure is determined by compliance with rules and conditions fixed at EU and national level which can lead to complexity and risk of misinterpretation.

15. EUROPEAN COURT OF AUDITORS FINDINGS

European Court of Auditors initiated in spring 2010 "Performance audit of pre-accession assistance to Croatia". The audit covered all types of pre-accession instruments including ISPA. The two-week audit mission to Croatia took place in October 2010. The audit report has not been finalised yet.⁵

16. CO-FINANCING PARTNERS – EIB AND EBRD

Given their expertise in project preparation and implementation, the Commission has maintained regular contact with these lending institutions, both at a horizontal level to co-ordinate policy and methodological issues related to programming and implementation, and at country level. The European Investment Bank is not involved in any ISPA project in Croatia.

The European Bank of Reconstruction and Development is the only International Financial Institution which is actively involved in an ISPA project in Croatia with the provision of a EUR 10 million loan for an environmental project approved in 2005 – the Karlovac Water and Wastewater Treatment Programme. Representatives of the EBRD therefore took part in both ISPA Monitoring Committees held in Croatia in 2010.

Contribution to European Union policies

17. PUBLIC PROCUREMENT

⁵ At the time of drafting this report the statement of preliminary findings has been communicated to the Commission services.

The fulfilment of the legal requirements for sound, fair and transparent public procurement as enshrined in the PRAG rules has proved to be a major challenge in the implementation of ISPA projects. Difficulties in complying with PRAG led to delays in the implementation of ISPA projects. The EU Delegation in Zagreb continued to intervene to ensure that procedures were correctly applied and errors rectified.

The *ex-ante* approval by the Commission, which governs the tendering and contracting of ISPA projects, continues to be entirely justified as plans to move to EDIS have now been dropped (see point 15). Under the current *ex-ante* system of approval and in line with the DIS decision for the conferral of management, only the CFCA plays the role of the contracting authority responsible for project implementation, whereas the Commission endorses each step of the procurement process. It follows that, although the Commission is not a contracting partner, it bears shared responsibility for the procedural correctness of the procurement process (without the Commission's approval, contracts concluded between beneficiaries and contractors are not valid).

18. COMPETITION POLICY

As ISPA assistance is directed primarily to cover public expenditure - or equivalent - concerning utility projects, this does not generally raise problems of incompatibility with the EU rules on competition. Unless the rules on public procurement are infringed, and provided free access to such infrastructure is guaranteed for all operators meeting the necessary technical and legal conditions, such assistance does not confer any special advantage to specific firms.

19. ENVIRONMENT POLICY

By providing direct assistance to priority projects for the environment, ISPA contributes to the implementation of environmental policy and to the compliance with EU standards in Croatia. Experience gained through project development and implementation enhance administrative capacity in the environment sector. ISPA environmental projects and experiences paved the way for bigger number of environmental projects being currently financed under IPA.

20. TRANSPORT POLICY

The transport networks in Croatia, agreed in accordance with TINA (Transport Infrastructure Needs Assessment) and REBIS (Regional Balkans Infrastructure Study) were constructed around the framework of pan-European corridors. Several of them run across the territory of Croatia including Corridors VII (the Danube river), X (Salzburg-Ljubljana-Zagreb-Beograd-Nis-Skopje-Veles-Thessaloniki, including branch Xa) as well as Corridor V, which has two branches in Croatia (Vb - Budapest, Zagreb Rijeka, and Vc - Budapest, Sarajevo, Ploče). These networks were used as the planning basis for the national transport strategy for ISPA purposes. As a consequence the single ISPA transport (railway) project forms part of the TINA and REBIS networks, i.e. it concerns the construction or rehabilitation of a section, nodal point or access relating to the networks. The TEN-T networks for Croatia are based on SEETO (South East Europe Transport Observatory) recommendations.

Co-ordination among pre-accession instruments

21. CO-ORDINATION WITH THE IPA INSTRUMENT

Management of ISPA measures and IPA programmes under Regional Development component by the same Commission services ensures close coordination of activities, complementarity of supported actions and continuity of policies.

Publicity

22. PUBLICITY ACTIONS

ISPA monitoring committee in June 2010 was held in Karlovac where investments in water and wastewater sector are supported by ISPA. At the margin of the committee press conference was organised which was followed by the visit on project site. Moreover, EU assistance is advertised in all investment projects by billboards and publicity actions in media.