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**REPORT FROM THE COMMISSION**

**18th Annual Report on Implementation of the Structural Funds (2006)**

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# REPORT FROM THE COMMISSION

## 18th Annual Report on Implementation of the Structural Funds (2006)

This report is presented in accordance with Article 45(2) of Regulation (EC) No 1260/1999 laying down general provisions on the Structural Funds. It covers the activities of the Structural Funds during 2006.

More detailed information is available in the Commission staff working paper (annexed to this report).

### 1. INTRODUCTION

A major step was taken in 2006 with the adoption of the legislative framework for the 2007–2013 programming period, some two years after the Commission's initial proposals of July 2004. The framework comprises the general regulation<sup>1</sup>, four regulations laying down specific rules on the European Regional Development Fund (ERDF)<sup>2</sup>, the European Social Fund (ESF)<sup>3</sup>, the Cohesion Fund (CF)<sup>4</sup> and the European Grouping of Territorial Cooperation (EGTC)<sup>5</sup> plus the Commission implementing regulation<sup>6</sup> adopted on 8 December 2006.

Reflecting the fact that future programmes will be implemented within the framework of Community priorities, Community Strategic Guidelines (CSG) were adopted on 6 October 2006 making the Lisbon strategy for growth and jobs the central focus of the new cohesion policy programmes.

A series of reforms relating to management of the operational programmes have been introduced for 2007-2013. In terms of the delivery system, legislation has been streamlined and rules simplified for managing cohesion policy. In particular there is:

- One set of management rules with a single Commission implementing regulation for the 2007-2013 programming period, which replaces 10 existing regulations for the 2000-2006 programming period;
- One set of eligibility rules for expenditure with Member States using national eligibility rules, rather than European eligibility rules in addition to national eligibility rules;
- Simplification of financial management giving a wider autonomy to the national authorities in charge of the management of operational programmes;

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<sup>1</sup> Regulation (EC) No 1083/2006, OJ L 210, 31.7.2006, p. 25.

<sup>2</sup> Regulation (EC) No 1080/2006, OJ L 210, 31.7.2006, p. 1.

<sup>3</sup> Regulation (EC) No 1081/2006, OJ L 210, 31.7.2006, p. 12.

<sup>4</sup> Regulation (EC) No 1084/2006, OJ L 210, 31.7.2006, p. 79.

<sup>5</sup> Regulation (EC) No 1082/2006, OJ L 210, 31.7.2006, p. 19.

<sup>6</sup> Commission Regulation (EC) No 1828/2006, OJ L 45, 15.2.2007, p. 3.

- Increased proportionality and simplification for control systems, and for smaller programmes (total eligible public expenditure under 750 million EUR and Community co-financing under 40 % of total public expenditure), certain requirements on control arrangements can be carried out by national bodies;
- The organisation of the Rural Development policy (financed by the EAFRD<sup>7</sup>) and the fisheries policies (financed by the EFF<sup>8</sup>) henceforth independent of the Structural Funds on the basis of the European Agricultural Fund for Rural Development (aligning the rules of management and control with those of the first pillar of the Common Agricultural Policy) and the European Fisheries Fund. This requires an effective complementarity between the co-financed actions by all the financial instruments concerned (Cohesion, Rural Development and Fisheries policies);
- Improved information and communication with citizens and potential beneficiaries having the same access to information on funding opportunities;
- Greater reliance on electronic government in practice with data exchange between the Member States and the Commission being done only electronically.

In addition, for the implementation phase, and in order to bring in new sources of support and expertise, the Commission and the international financial institutions have prepared three joint initiatives: Jaspers (Joint Assistance to Support Projects in European Regions) to assist the twelve beneficiary countries with preparing major projects, Jeremie (Joint European Resources for Micro to Medium Enterprises) to improve access to finance for SMEs and develop micro-credit and Jessica (Joint European Support for Sustainable Investment in City Areas) to support sustainable and recyclable urban investment and development in cities.

A significant level of support in the new programming period will be directed towards strengthening public administrations and public services. It will support the modernisation and the development of the public administrations and public services to better meet the expectations of citizens and business and also to strengthen its role as an important factor of social and economic development.

## **2. ANALYSIS OF IMPLEMENTATION**

### **2.1. Budget Implementation**

#### *2.1.1. ERDF*

The implementation of the budget in 2006 was very satisfactory and for Objectives 1 and 2 and the Community initiatives, 100 % of the resources available were committed.

Concerning payment appropriations, 99.92 % of the resources available were used (99.65 % in 2005). The projected level of payment appropriations for 2006 ERDF

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<sup>7</sup> Regulation (EC) No 1698/2005, OJ L277, 21.10.2005, p. 1.

<sup>8</sup> Regulation (EC) No 1198/2006, OJ L223, 15.8.2006, p. 1.

was reduced by 2.8 billion EUR in the course of the year in order to take account of the temporary suspension of payment claims by Spain and the United Kingdom (amounting to 2.3 billion EUR) pending the implementation of action plans to improve aspects of management and control systems, and due to forecasting errors made by EU-10.

Commitments from previous years on which payments were still to be made<sup>9</sup> totalled EUR 45.8 billion at the end of 2006 (compared with EUR 39.1 billion in 2005).

Concerning the application of the n+2 rule, at the end of 2006 and in relation to the 2000, 2001, 2002, 2003 and 2004 commitments, EUR 1 billion had not been paid at the beginning of 2007. However, in view of the exceptions that can be granted to the n+2 rule (for cases involving state aid decisions, major projects, etc.), the estimate of resources at risk of decommitment, because they have not given rise to payments, is much smaller at EUR 162 million (only 0.0018 % of total commitments).

### 2.1.2. *ESF*

Implementation of the budget in 2006 was also very satisfactory: 99.97 % of commitment appropriations were implemented in 2006 (against 99.93 % in 2005). Concerning payments, 99.87 % of the appropriations were executed (99.86 % in 2005). The total outstanding payments on commitments at the end of 2006 stood at EUR 22.96 billion (outstanding payments compared with EUR 20.74 billion in 2005), out of which EUR 22.76 billion were for the current ESF programming period (EUR 20.44 billion in 2005). The outstanding payments from earlier ESF programming periods decreased significantly from EUR 304.7 million at the end of 2005 to EUR 204.6 million at the end of 2006 (-32.8 %).

Concerning application of the n+2 rule, at the end of 2006 to the 2000, 2001, 2002, 2003 and 2004 commitments, 19 programmes were involved for which a total of EUR 129.31 million was proposed from the ESF (0.19 % of total ESF). For those programmes the Commission opened negotiations ('the contradictory procedure') with the Member States. Only at the end of this procedure can the amounts to be decommitted be known.

### 2.1.3. *EAGGF*

The 2006 budget was fully used in terms of both the commitment and payment appropriations (respectively 99.3 % and 108.5 % of the budget initially voted). The figure for payments was achieved due to the fact that the payment appropriations budget was topped-up by EUR 360 million in December 2006.

Compared with 2005, an extra EUR 207 million was committed and an extra EUR 2 million paid.

The payments added up to EUR 3 589 million, of which EUR 3 562.1 million was for the 2000-2006 programmes (Objective 1: EUR 3 193.0 million; Leader+: EUR 361.1 million; Peace: EUR 8.1 million) and EUR 26.9 million for the closure of 45 programmes from the 1994-1999 programming period.

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<sup>9</sup> "RAL" (restes à liquider). Open commitments from previous years.

Outstanding EAGGF commitments at the end of 2006 totalled EUR 7 636 million (compared with EUR 7 085 million in 2005), of which EUR 7 288 million corresponded to 2000-2006 programmes.

Implementation of the n+2 rule for the 2003 commitments resulted in EUR 9.3 million being decommitted.

#### *2.1.4. FIFG*

In all, 99.58 % of commitment appropriations and 84.16 % of payment appropriations were implemented. The payment rate was 86.23 % in Objective 1 regions and 79.06 % in regions outside Objective 1. The total outstanding payments on commitments for the FIFG for the 2000-2006 programming period totalled EUR 1 336 million in 2006 (compared with EUR 1 111 million in 2005).

Concerning the application of the n+2 rule, at the end of 2006 and in relation to the 2000, 2001, 2002, 2003 and 2004 commitments, 9 programmes were involved for which a total of EUR 22 million was at risk. For these programmes the Commission opened the contradictory procedure with the Member States. Only by the end of this procedure the amounts to be decommitted will be definitively known.

## **2.2. Programme Implementation**

### *2.2.1. Objective 1*

Expenditure on the Objective 1 programmes followed the same path as in 2005. The Objective 1 programmes focused investment on basic infrastructure projects (41.6 %), with over half (54.4 %) of all investment in this category spent on transport infrastructure. More than one-third (33.5 %) of the Objective 1 resources were invested in productive environment, where the priority continues to be on assisting SMEs and the craft sector (30 %). Projects targeted at human resources took 23.2 % of resources in Objective 1 regions. The main fields of activity were, almost equally, labour market policies (31.6 %) and education and vocational training (31 %).

### *2.2.2. Objective 2*

In Objective 2 regions, the main focus of the programmes continued to be on productive environment, with over half of all financial resources (56.3 %) allocated to this category. Within this field, assistance to SMEs and the craft sector predominated (56.5 %). The second most important field of activity was basic infrastructure, with 29.1 % of all Objective 2 resources. Unlike the Objective 1 programmes, the most important area in financial terms was planning and rehabilitation of industrial zones (44.6 %). In the human resources category (10.2 % of all investment in Objective 2 regions), workforce flexibility, entrepreneurial activity, innovation, information and communication technologies were the main fields of investment (31.6 %).

### *2.2.3. Objective 3*

The main emphasis of the ESF programme in 2006 continued to be on support for the European Employment Strategy, particularly measures aimed at improving employability on the labour market (31 % of expenditure), lifelong learning (27 %)

and equal opportunities (6 %), while measures to promote entrepreneurship remained stable (19 %) but below the level suggested by the programming documents (21 %). Furthermore, there was still a marked difference in financial implementation of programmes between EU-15, where long-established programmes continued to be implemented, and EU-10, where some Member States are experiencing considerable difficulties in getting some projects and measures underway.

#### 2.2.4. *Fisheries outside Objective 1*

Take-up for structural improvements in the fisheries sector progressed in 2006. This was reflected in the financial implementation of the FIFG operational programmes, which contributed to achieving the objectives of the common fisheries policy.

#### 2.2.5. *Community initiatives*

##### 2.2.5.1. Interreg

The implementation of the 81 Interreg III/Neighbourhood programmes progressed well in 2006 in pursuit of their objective of reducing the negative economic impact of borders and promoting cooperation.

Over the period from 2000 to 2006, the 81 Interreg III/Neighbourhood programmes selected some 13 000 projects and networks. For some programmes, changes were necessary due to enlargement and/or the integration of the Union's new Neighbourhood programme concept. N+2 decommitments and updates of the mid-term evaluations contributed to further changes to the programme in the two following years.

##### 2.2.5.2. Equal

In 2006, good progress continued to be made with implementation of the 27 programmes and more than 3 300 projects under Equal. Under the n+2 rule, six Member States were unable to use a part of the 2004 budgetary commitment. In order to make maximum use of the results of the Equal programmes and to prepare for mainstreaming Equal into the next generation of operational programmes, the Commission and the Member States worked in partnership during 2006 on issues such as the treatment of asylum seekers, diversity, youth employment, ex-offenders, social economy, inclusive business creation, media and discrimination, management principles (partnership, transnational cooperation, innovation and gender mainstreaming).

##### 2.2.5.3. Urban

In 2006, the twenty thematic networks and six working groups created within the framework of Urban continued their efforts to promote best practices and exchange information. Thirteen networks completed this work and a final conference was organised to present their results and recommendations. A report on the "role of the cities in the development of disadvantaged districts", based on the experience of the cities, was produced under the auspices of the German Presidency.

#### 2.2.5.4. Leader

73 Leader+ programmes have been approved for the period 2000-2006. Of the 938 Local Action Groups (LAGs) proposed, 892 were finally selected.

#### 2.2.6. *Innovative actions*

##### 2.2.6.1. ERDF

Some 181 regional programmes for innovative actions were approved for the period 2000-2006. By the end of 2006 fifty-nine programmes had been brought to a conclusion. This resulted in 40 projects being identified as best practice examples for dissemination to other regions (for example, through the Inforegio website). It should be recalled that the programmes are organised around the following themes: knowledge and technological innovation, information society and sustainable development.

##### 2.2.6.2. ESF

During the year 37 projects relating to Local Employment Strategies were finalised. In 2006, 19 projects were selected under the third round of the call for proposals on “Innovative approaches to the management of change”. Together with the 61 ongoing projects selected in previous rounds, they address two priority issues: management of restructuring and management of demographic change. With a view to mainstreaming the results, six projects were selected under the second round of the call on “Transfer and dissemination of innovation from ESF Article 6 projects”.

##### 2.2.6.3. FIGF

Nine projects were brought to a conclusion in 2006. Following the 2005 *ex post* evaluation of transnational projects for innovative action in the fisheries sector, it was decided not to launch any new call for proposals in 2006. The evaluation showed that the overall EU added value of these projects was rather limited. The key characteristics of the innovative action - innovation, networking and transnational cooperation – have, however, been included in the European Fisheries Fund Regulation.

### **3. CONSISTENCY AND COORDINATION**

#### **3.1. Consistency with other Community policies**

##### *3.1.1. Competition*

Under Regulation (EC) No 1260/99 Member States are required to verify that all operations comply with EC legislation, including the rules on State aid. Where the Commission is informed of, or audits demonstrate, any breach of EC legislation, appropriate action is taken. In order to provide full transparency, Member States indicate the State aid schemes for which assistance from the Structural Funds is used in their programmes. The majority of regional aid schemes expired on 31 December 2006. New guidelines apply as of 1 January 2007 with a view improving the efficiency of state aid as well as increasing transparency and simplicity of operation.



### *3.1.2. Internal market*

Under Regulation (EC) No 1260/99, Member States are also required to verify that operations financed by the Funds comply with EU Public Procurement Directives. Where the Commission is informed of any breach of EC legislation or where audits demonstrate that this is the case, appropriate action is taken. In the programming context the Commission requires information from the Member States in the annual reports on the programmes. The Directorates General for Regional Policy and for Internal Market have contributed to clarify the legal treatment of concessions dating before accession of new Member States, on 1 May 2004, and which were not in compliance with the EC-acquis. A new regulatory framework for public procurement law has been introduced in order to provide greater legal certainty both for the private and the public sector.

### *3.1.3. Environment*

The main focus has been on using appropriate actions under the cohesion policy programmes to support compliance with the Community Acquis in the field of urban wastewater, water supply and waste management. Other important areas of investment have been in eco-innovation and rehabilitation of polluted soil. The promotion of sustainable development has been achieved with investments in environmentally-friendly transport and energy, introducing environmental criteria into project selection, and by pro-actively ensuring compliance of projects with environmental legislation.

### *3.1.4. Transport*

Cohesion programmes continue to be the main source of Community support for the realisation of Community priorities in transport. Accordingly, the main focus has been on supporting investment in line with European transport policy. For a list of major projects supported in this field by the ERDF, see Part 3 of the Annex.

### *3.1.5. Gender equality*

In March 2006, the Commission adopted “A Roadmap for Equality between Women and Men”, covering the period 2006-2010, which reflects the Commission’s commitment to this issue and covers all external and internal EU policies. The roadmap outlines six priority areas for EU action on gender equality. It is designed to improve governance by exploring the possibilities to develop gender budgeting at EU level, particularly in the Structural Funds within the possibilities of shared management for the new period.

## **3.2. Coordination of instruments**

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

In 2006, before the latest enlargement to Romania and Bulgaria on 1 January 2007, whereas all 25 Member States benefited from the support of the Structural Funds, there were 13 Member States benefiting from also the Cohesion Fund which supports the less prosperous countries.

The Structural Funds have been carefully co-ordinated among themselves, and vis-à-vis the Cohesion Fund (ERDF in particular), to avoid duplication in projects supported.

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

In 2006 Jaspers (Joint Assistance to Support Projects in European Regions), a new technical assistance facility to assist the new Member States to prepare major projects, came into operation. Action plans (work programmes) for 2006 were agreed with eleven of the twelve beneficiary countries.

The Commission and the EIB Group have also agreed to launch a joint initiative – Jeremie (Joint European Resources for Micro to Medium Enterprises) – to improve access to finance for SMEs and develop micro-credit for the next programming period.

Another initiative, Jessica (Joint European Support for Sustainable Investment in City Areas), has been put in place with the EIB and the Council of Europe Development Bank to support sustainable urban investment and development in cities in the EU from the Structural Funds. Under Jessica, managing authorities in the Member States have the opportunity to use some of their Structural Fund allocations to invest in Urban Development Funds (UDFs) and recycle these resources for further rounds of investment in urban areas.

JEREMIE and JESSICA represent a cultural shift for cohesion policy, seeking to move away from an exclusive dependence on grants towards greater use of repayable forms of assistance.

## **4. EVALUATIONS**

In 2006 the Commission carried out strategic and thematic evaluations to support decision-making under cohesion policy. In addition, its summary reports analysed the quality and the results of evaluations carried out by the Member States. Another important task for the Commission was to provide methodological guidance to the Member States and organise exchanges of experience.

## **5. CONTROLS**

### **5.1. ERDF**

For the 1994-1999 programming period, closure audits were completed on a sample of 56 programmes covering all EU-15. The work in 2006 involved completing the follow-up of all audits, reaching final positions on corrections to be applied and launching financial corrections procedures, where applicable.

For the 2000-2006 period, the audit work carried out in 2006 consisted of 85 on-the-spot missions covering both systems audits and substantive testing on 332 operations. The audit work carried out substantially advanced the level of security regarding the operation of systems in the Member States and achieved important improvements through the implementation of action plans, in certain cases.

By the end of 2006, for EU-15, a total of 126 audit missions had been carried out covering 61 programmes or 22.1 % of the number of the mainstream and URBAN programmes and 52.6 % of the ERDF resources available. For EU 10, at the end of 2006, 28 audit missions had been carried out representing audits on 9 programmes or 45 % of the number of the mainstream programmes and 65.5 % of the decided ERDF contribution.

As regards INTERREG, in 2006, 5 programmes were audited representing 28 % of ERDF commitments.

## **5.2. ESF**

During 2006, 69 audit missions were organised by the Commission: 53 system audit missions on 2000-2006 plus 16 closure audits on 1994-1999.

Out of a total of 237 European Social Fund programmes, 123 have been covered by the Commission, with the emphasis on those assessed as high-risk programmes. In all, 34 programmes assessed as high-risk were audited in 2006, including 10 new programmes. Every Member State except Luxembourg was visited. In five Member States a follow-up audit was performed.

In 2006, 12 financial correction procedures and 14 action plans were agreed.

## **5.3. EAGGF**

By the beginning of 2006, the planned *ex post* audit programme for 1994-1999 had been completed. Programmes accounting for 32 % of total expenditure were audited in this action. A number of financial correction procedures are underway: bilateral meetings were held with the Member States in 2006 on 18 programmes. Four financial correction decisions covering five programmes were adopted by the Commission in the course of the year.

A total of 21 programmes, covering 38 % of the planned expenditure, were audited over the year for the period 2000-2006 (EU-25). By the end of 2006 a total of 73 of the 152 programmes approved for the EAGGF-Guidance Section had been audited.

## **5.4. FIG**

A total of six on-the-spot checks were carried out in 2006 for the FIG. Three of these missions were to verify and follow up the effective functioning of the management and control systems for the period 2000-2006, combined with sample checks in Italy, Poland and Sweden.

Another two missions were carried out in France and in Portugal and concerned system audits combined with sample checks to verify effective functioning of the management and control systems for operational programmes under Objective 1.

## **5.5. OLAF**

During 2006 OLAF undertook 44 missions in the Member States relating to measures co-financed by the Structural Funds. Some 30 of these missions concerned on-the-spot checks<sup>10</sup>, while 14 were conducted for other purposes, e.g. to gather information or to assist either national administrations or judicial authorities. Among problems identified were cases of false declarations and invoicing and failure to respect public procurement rules.

In 2006, Member States communicated to the Commission, in accordance with Regulation (EC) N° 1681/94, some 2 988 notifications of irregularities involving EUR 516 697 561 affecting co-financed measures of the 1994-1999 and 2000-2006 programming periods. The number of notifications showed a slight decrease compared to 2005, probably as a result of the modifications introduced with (EC) Regulation N° 2035/2005<sup>11</sup> and in particular the increase of the threshold for the reporting of irregularities from EUR 4 000 to EUR 10 000. However, the financial amounts concerned increased. The figures demonstrate an increased awareness and a better reporting by the Member States in conformity with Community law obligations.

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

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

In 2006 the CDCR was consulted on technical assistance on the initiative or on behalf of the Commission and on amendment of Commission Regulation (EC) No 448/2001.

A new Coordination Committee of the Funds (COCOF) was established under Article 103 of Regulation (EC) No 1083/2006 which entered into force on 1 August 2006. It was consulted as a management committee on the rules for implementing Council Regulation (EC) No 1083/2006 and on the method for calculating the structural public and equivalent expenditure for additionality purposes.

The Committee was consulted as an advisory committee on the list of areas eligible under the European Territorial Cooperation Objective, cost-benefit analysis methodology, guidelines concerning the evaluation methodology and the allocation of technical assistance on the initiative or on behalf of the Commission.

### **6.2. ESF Committee**

The Committee discussed a wide range of issues relating to both implementation of the 2000-2006 programming period of the ESF and preparations for the 2007-2013 programming period.

The Committee examined issues concerning the new regulations for 2007-2013, including ESF support to education and training, health, anticipation, management of

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<sup>10</sup> Regulation (EC) No 2185/1996, OJ L 292, 15.10.1996, p. 2.

<sup>11</sup> OJ L 328, 15.12.2005, p. 8.

change and restructuring, social partners and migrants, and the mainstreaming of EQUAL principles.

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

The STAR Committee met 12 times in 2006 and gave favourable opinions on 31 amendments to rural development programmes under Article 44(2) of Council Regulation (EC) No 1257/1999 and six amendments to rural development programmes under Article 4 of Council Regulation (EC) No 1268/1999.

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

In 2006, the Committee was consulted on a number of issues: the draft working paper on *ex ante* evaluation for the European Fisheries Fund operational programmes; the draft working paper on indicators for monitoring and evaluation for the European Fisheries Fund operational programmes; the draft Commission Regulation laying down detailed rules for the implementation of Council Regulation (EC) No 1198/2006 on the European Fisheries Fund; the draft codification of Commission Regulation (EC) No 908/2000 of 2 May 2000 laying down detailed rules for calculating aid granted by Member States to producer organisations in the fisheries and aquaculture sector.