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1. GENERAL CONTEXT

1.1. Convergence and economic development in the beneficiary Member States

1.1.1 Greece

In 2007 GDP per capita in PPS reached 94.8% of the EU-27 average. In 2008 real GDP growth decelerated to 2.9% reflecting heightening economic uncertainty in the wake of the global economic and financial crisis, that led to weakening private consumption and more importantly, declining investment. The external deficit declined somewhat, but remained still high, at above 12% of GDP in 2008, compared with 14% of GDP in 2007 and 11.5% of GDP in 2006. Due to expenditure overruns and to a lesser extent, revenue shortfalls, the general government deficit increased to 5% exceeding the estimation included in the January 2009 stability programme by 1.25 of a percentage point of GDP. The debt-to-GDP ratio increased by almost three percentage points, and reached 97.75% in 2008.

The Greek government submitted its update of the stability and growth programme on 30 January 2009 and an addendum on 6 February 2009. The macroeconomic scenario underlying the programme envisages that real GDP growth will fall from 3% in 2008 to 1.1% in 2009 before picking up again to 1.75% on average over the programme period. In the medium term, the programme aims at reducing the general government deficit from 3.7% in 2009, to 3.2% of GDP in 2010 and 2.6% by 2011. Based on a significantly less favourable growth scenario, with real GDP contracting by almost 1% in 2009, as well as a prudent assessment of the fiscal consolidation measures announced for 2009, the Commission services' spring 2009 forecast foresees the general government deficit in 2009 to remain at 5% of GDP. Under a no-policy-change assumption, the deficit is projected at 5.75% of GDP in 2010.

In its Opinion on the stability programme of 10 March 2009, the Council noted that the programme envisages reducing the budget deficit over the medium term, but falls short to address the structural imbalances of the Greek economy timely and effectively and reverse the upward trend of public debt. Although the consolidation strategy beyond 2009 relies on permanent expenditure restraint and increasing tax revenues, the programme does not spell out concrete measures to back the planned budgetary adjustment in 2010 and 2011 fully. Strengthening the fiscal consolidation path would be paramount to achieve sound and sustain public finances in Greece. Moreover, the structural nature of the factors underlying competitiveness losses and the widening external imbalances urgently requires the implementation of bold structural reforms. In the long term, the level of debt which remains among the highest in the EU, coupled with the projected increase in age-related spending, will also challenge the long term sustainability of public finances.

1.1.2. Spain

In 2007, Spain's GDP per capita in PPS attained 105.4% of the EU-27 average in 2007. In 2008, GDP growth slowed sharply to 1.2%, reflecting both the global economic downturn and a marked correction in the construction sector. The sharp deceleration in domestic demand was attenuated by government consumption, which accelerated and grew at more than 5%. The annual inflation rate rocketed to just

above 4% in 2008 on the back of higher oil and food average prices. The rapid deterioration of the economic situation undermined also public finances, turning previous surpluses into a deficit. For 2008, the general government deficit reached 3.8% of GDP, compared with an original target of a surplus 1.2% of GDP. The deviation from the target stems mainly from the much lower GDP growth and expenditure slippages.

The latest update of the stability programme submitted on 30 January 2009 and covering the period 2008-2011, targets government deficits of 5.8% of GDP in 2009, 4.8% in 2009 and 3.9% of GDP in 2011. These figures rest on the programme's assumptions that GDP will decline by 1.6% in 2009 and grow by 1.2% and 2.6% in real terms in 2010 and 2011 respectively. In line with the European Economic Recovery Plan, Spain has adopted a sizeable stimulus package, particularly in 2009, including a November 2008 stimulus package (slightly 1 % of GDP) aiming mostly at fostering public investment. According to the Commission services' spring 2009 economic forecasts, the government deficit is projected to reach 8.5% of GDP in 2009 and, on the basis of the no-policy change assumption, 9.75% of GDP in 2010. The more marked deterioration in public finances in the Commission service's forecasts result, notably, from a significantly sharper contraction of growth in the forecast and a gloomier labour market outlook.

In its Opinion the stability programme of 10 March 2009, the Council noted that "the sharp slowdown of economic activity and some discretionary measures led to a deficit above 3% of GDP in 2008, after a prolonged period in which the Spanish public finances were close to balance or in surplus. [...] Spain is invited to: (i) implement the 2009 fiscal policy as planned in line with the European Economic Recovery Plan and within the framework of the Stability and Growth Programme, while avoiding a further deterioration of public finances in 2009, and carry out with determination significant structural consolidation in 2010 and beyond, backing it up with measures; (ii) improve the long-term sustainability of public finances by implementing further measures aimed at curbing the increase in age-related expenditure; (iii) ensure that fiscal consolidation measures are also geared towards enhancing the quality of the public finances as planned in the light of the needed adjustment of existing imbalances."

1.1.3. Portugal

Portugal's GDP per capita in PPS attained 76.1% of the EU-27 average in 2007. In 2008, GDP stagnated in real terms, after growing by 1.9% in 2007, as the result of marginally declining investment and exports, with the latter reflecting visibly the fall in external trade in late 2008. The inflation rate was 2.7% in 2008 after 2.4% in 2007. According to the March 2009 Excessive Deficit Procedure notification, the general government deficit came out at 2.6% of GDP in 2008, which coincides with the outturn of 2007 (but the budgetary execution of 2008 benefited from deficit-reducing one-off operations worth over 0.75% of GDP, whereas similar operations had yielded only 0.1% of GDP in 2007). The 2008 outturn compares with an original target of 2.4% of GDP set in 2008 Budget Law. The deviation from the target stems mainly from the much lower GDP growth (2.2% in the Budget) and, to a lesser extent, expenditure slippages. This more than offsets a positive base effect thanks to the better-than-expected 2007 budgetary execution by some 0.5% of GDP. The debt-to-GDP ratio was at 66.4% in 2008 up from 63.5% in 2007.

The most recent update of the stability programme of Portugal was submitted on 30 January 2009 and covers the period 2008-2011. The update targets government deficits of 3.9% of GDP in 2009, 2.9% in 2009 and 2.3% of GDP in 2011. The programme hinges on the assumption that GDP will decline by 0.8% in 2009 and grow by 0.5% and 1.3% in volume terms in 2010 and 2011 respectively. In line with the European Economic Recovery Plan (EERP), Portugal implemented a stimulus package for 2009 representing 1.25% of GDP (0.8% of GDP to be financed out of the national budget and the rest through EU funds). The package adds to other discretionary measures of smaller size. According to the Commission services' spring 2009 economic forecasts, the government deficit is projected to reach 6.5% of GDP in 2009 and, on the basis of the no-policy change assumption, 6.7% of GDP in 2010. The differences between the national targets and the Commission forecasts result from the sharper recession foreseen in the latter, where GDP is projected to contract by 3.7% in 2009 and by 0.8% in 2010.

In its Opinion on the update of the stability programme of 10 March 2009, the Council noted that "the programme aims at a significant temporary fiscal impulse in 2009 in line with the EERP. The programme rightly plans the resumption of fiscal consolidation as soon as the economy recovers. Yet, economic growth may underpin fiscal consolidation by less than envisaged in the programme." The Council mentioned also the need to strengthen fiscal sustainability. The Council invited Portugal to "implement the 2009 fiscal policy as planned, while avoiding a further deterioration of public finances in 2009 and carry out with determination the planned adjustment in 2010 and beyond" and to "further strengthen the budgetary framework and ensure that fiscal consolidation measures continue to be geared towards enhancing the quality of the public finances in the light of the needed adjustment of the existing imbalances."

1.1.4. Cyprus

In 2007 Cyprus' GDP per capita in PPS reached 90.8% of the EU-27 average. In 2008 real GDP growth decelerated following the global economic downturn, to 3.7%. Activity was almost exclusively driven by dynamic domestic demand, while net exports posed a drag on growth. The deteriorating external environment had an adverse effect on exports, particularly tourism. On the other hand, imports, driven by buoyant domestic demand, continued growing dynamically. This, coupled with high commodity prices, particularly oil, led to a historically high external deficit, which reached 18.25% of GDP. The general government surplus is estimated to have fallen to 1% in 2008 from 3.4% of GDP in 2007. This decline mainly reflected revenue shortfalls, due to subdued activity in the housing and real estate sector as well as reduced corporate profitability. It also reflected expenditure overruns, partly due to the drought and the expenses associated with maintaining water supplies, as well as to social cohesion measures. The 2008 surplus is nonetheless above the target of 0.5% of GDP set in the 2007 stability programme, benefiting from higher-than-expected revenue, lower interest payments and a positive base effect from 2007. The debt-to-GDP ratio declined in 2008 by about 10.25 percentage points of GDP to about 49%. Average inflation reached 4.4% in 2008 due to buoyant domestic demand and high commodity prices, especially for oil and food.

The Cypriot government submitted its latest update of the Stability and Growth Programme on 13 February 2009. The macroeconomic scenario underlying the

programme envisages that real GDP growth will decelerate from 3.8% in 2008 to 2.1% in 2009, before recovering to an average rate of almost 3% over the rest of the programme period. Due to slower growth and lower revenue, the update targets a deficit of 0.75% of GDP in 2009. Based on a markedly less favourable growth scenario, with real GDP growing at 0.25% in 2009, the Commission services spring 2009 forecast projects a higher fiscal deficit, at almost 2%. This projection takes into account additional revenues from the recently adopted pension reform and an announced extra-budgetary package of social measures, not incorporated in the official projections. On a no-policy-change basis, the deficit is projected to edge up to 2.5% of GDP in 2010, due to an increase in current primary expenditure.

The Council adopted its opinion on the Stability programme of Cyprus on 27 April 2009. The overall conclusion is that fiscal stance in 2009 will be expansionary due to the adoption of significant stimulus measures in 2009 in line with the European Economic Recovery Plan. In the subsequent years covered by the programme (until 2012), the fiscal balance is projected to continue worsening. The implied fiscal loosening does not appear justified in view of the relatively good economic prospects for Cyprus and the existence of a large external imbalance. Moreover, against the background of a sharp deterioration in the global economic environment, the budgetary strategy is subject to significant downside risks, as the macroeconomic scenario is based on favourable growth assumptions. In the light of the high external imbalances, maintaining prudent policies and strengthening fiscal sustainability should be a major priority. Therefore, controlling current expenditure and avoiding pro-cyclicality represents a major challenge for the fiscal policy in Cyprus. In addition, fostering the quality of public finances is also important in order to underpin a smooth adjustment of the economy in the light of the imbalances it faces.

1.1.5. Czech Republic

Czech GDP per capita in PPS reached 80.2% of the EU-27 average in 2007. The Czech economy grew by 3.2% in real terms in 2008. Growth decelerated toward the end of the year with a contraction in output in the fourth quarter driven by falling external demand. Annual inflation rose to 6.3% on average in 2008, due partly to administrative measures, while declining steeply to 3.3% in December year-on-year. The general government deficit in 2008 was 1.5% of GDP compared to an estimated deficit of 1.2% in the November 2008 convergence programme. The slightly poorer outturn was mainly due to a shift in revenues from tobacco excise duty from 2008 to 2007.

The Czech Republic submitted its latest convergence programme, covering the period 2008-2011 on 20 November 2008. The macro-economic scenario underlying the programme estimated real GDP growth at 3.7% in 2009 rising gradually to just above 5% of GDP in 2011. These projections reflect the programme's early date of submission; the latest Ministry of Finance forecast foresees negative growth in 2009. Exports and investment will be particularly badly affected by a sharp fall in external demand. The main aim of the budgetary strategy is to achieve budgetary consolidation toward the end of the programme period. The programme targeted a deficit of 1.6% of GDP in 2009 declining to 1.5% of GDP in 2010. The Commission's spring forecast predicts that the deficit will be 4.3% of GDP in 2009 and 4.9% of GDP in 2010, against projected growth of -2.7% of GDP in 2009 and 0.3% of GDP in 2010. The large discrepancy between the programme's targets and

the Commission's spring forecast is mainly due to a much poorer macroeconomic outlook and the impact of fiscal stimulus measures in 2009 approved after the convergence programme was submitted.

In its Opinion on the convergence programme update on 10 March 2009, the Council concluded that there are risks to the budgetary projections, in particular in view of favourable growth assumptions, and that concerns remain regarding long-term fiscal sustainability due to a rapidly ageing population. The Council invited the Czech Republic to implement the budgetary plans in 2009, including stimulus measures, carry out consolidation in 2010 with specific measures for reducing expenditure in 2010-2011 and continue with the necessary pension and health care reforms, in order to improve the long-term sustainability of public finances.

1.1.6. Estonia

The period of high economic growth that helped Estonia to reach a GDP per capita in PPS of 67.9% of EU average in 2007 peaked early in that year. 2008 marked an abrupt reverse, with the economy contracting by 3.6%. The reversal of the cycle was increasingly aggravated by the deepening global financial crisis. With confidence plummeting and banks becoming increasingly cautious in their lending decisions, domestic demand contracted by 7.4% in 2008, while a sharp contraction of external demand in late 2008 exacerbated the downturn. Inflation remained high throughout the year, at 10.6% for the year as a whole. A reversal of trend also took place in 2008 with regards to public finances, as the general government posted a deficit of 3.0% of GDP, following six years of nominal surpluses. The outcome was considerably worse than the surplus target of 1.3% set in the November 2007 convergence programme, due to a sharp contraction of revenue caused by declining economic activity and despite the adoption of a restrictive supplementary budget in mid-2008.

The December 2008 update of the convergence programme projects real GDP to decline by 3.5% in 2009, returning to a positive growth path in 2010 and accelerating to around 5% in 2011-2012. The programme envisages a moderation in previously high imbalances in line with the declining economic activity, with inflation set to reach low single digit levels in 2009 and 2010, partly due to wage moderation, and the external deficit shrinking to pre-boom levels. Fiscal policy is planned to be restrictive. The policy is geared in the short term towards restoring market confidence and keeping the general government deficit within the Treaty reference value, given the authorities' euro adoption objective. The programme targets a budgetary deficit of 1.7% of GDP in 2009, against the 3.0% deficit expected in the Commission services' spring forecast. The deterioration in the fiscal outlook, despite the adoption of several consolidation measures in February and April 2009, is due to a considerable downward revision to the macroeconomic outlook. The budgetary deficit is expected to increase to 3.9% of GDP in 2010 in the Commission services' forecast, under a no-policy-change assumption. In the medium term, the goal of the programme is to achieve a structural surplus.

In its Opinion of 10 March 2009, the Council concluded that Estonia, while facing a severe economic downturn following years of above-potential growth, is planning a restrictive fiscal stance from 2009 until 2011 and that this is an appropriate response in light of the existing imbalances. The Council invited Estonia to implement the consolidation of public finances in the short term, ensure keeping the general

government deficit below 3% of GDP and take the necessary measures to underpin the consolidation in the medium term, as well as to reinforce the medium-term budgetary framework, particularly by improving expenditure planning and efficiency. To support the adjustment of the economy and to strengthen competitiveness, the Council also invited Estonia to implement prudent public sector wage policies.

1.1.7. Hungary

In 2007, Hungary's GDP per capita in PPS reached 62.6% of the EU-27 average. In 2008, GDP grew only by 0.5%, due to the deceleration of both external and domestic demand in view of adverse global economic environment, external financing shortages and deteriorating income expectations, while inflation decreased to an annual average of 6%. As a response to the external market financing shortages, the IMF and the EU granted financial assistance of € 20 billion to Hungary. Due to the continuation of the fiscal consolidation programme, the budget deficit was 3.4% of GDP in 2008, substantially lower than the budgeted target (4%). The debt-to-GDP ratio increased from 65.8% in 2007 to 73% in 2008, chiefly due to the reserve build-up financed from the international financial assistance in response to the financial crisis. Given the sizeable macroeconomic and public finance imbalances, the Government did not adopt fiscal stimulus measures, in line with the European Economic Recovery Plan.

The December 2008 convergence programme set a general government deficit target of 2.6% of GDP (lower than the previous target of 3.2% of GDP). In view of the significant deterioration in the 2009 growth outlook (from -1% to -3.3%), the Government revised its deficit target slightly to 2.9% of GDP, while adopting additional corrective measures of around 0.7% of GDP. Following a further deterioration of GDP growth, the authorities announced additional corrective measures of 1% of GDP so as to respect the revised official target. The Commission services' spring forecast projects a somewhat higher deficit of 3.4% of GDP for 2009, chiefly due to the fact that not all the measures announced by the new government on 19 April were detailed enough to be incorporated in the forecast. For 2010, the Commission services' forecast, on the basis of a no-policy-change assumption, projects a deficit of 3.9% of GDP.

In its Opinion on the convergence programme update of 10 March 2009, the Council noted that, in spite of distinct improvements in its high imbalances, Hungary has been particularly exposed to the financial crisis and thus had to limit the financing need of the government. The programme foresees a continuation of the front-loaded consolidation strategy. However, the deficit reduction path was deemed subject to risks, especially due to the markedly favourable macroeconomic assumptions underlying the programme. The Council therefore invited Hungary to maintain adequate buffers and take the necessary measures to bring the budget deficit below the 3% of GDP threshold in 2009; ensure the full implementation of the fiscal responsibility law; continue expenditure moderation through further structural reforms; strengthen financial market regulation and supervision; and in view of the level of debt and the increase in age-related expenditure, further improve the long-term sustainability of public finances.

1.1.8. Latvia

After having reached a level of GDP per capita in PPS amounting to 57.9% of the EU average in 2007, Latvia's real GDP shrank by 4.6% in 2008. The global financial crisis amplified the shock of the reversal of Latvia's own lending and real estate boom by tightening credit availability and conditions, reinforcing the steep decline of domestic demand over the course of 2008. The concomitant downturn in Latvia's main export markets has hit the relatively small tradable sector, already weakened by huge domestic cost increases over the previous years. Inflation in 2008 rose to an average of 15.3% (10.1% in 2007). The April 2009 Excessive Deficit Procedure notification indicates a budget deficit of 4.0% of GDP for 2008, a far weaker outturn than the target surplus of 0.7% of GDP set in the initial budget, reflecting both a significantly worsened economic environment and substantially higher-than-budgeted expenditures, including an increase in social transfers. The debt-to-GDP ratio increased to 19.5% in 2008 from 9.0% in 2007.

Following Latvia's applications for international financial assistance and its associated adoption of a medium-term economic and budgetary stabilisation programme in December 2008, a revised update of Latvia's convergence programme covering the period 2008-2011 was submitted on 14 January 2009. The main goal of the medium-term budgetary strategy in the programme is to fulfil Maastricht budgetary criteria in 2011, with planned general government deficits of around 5% of GDP in 2009 and 2010 and below 3% in 2011. The macroeconomic scenario underlying the programme projects a contraction of real GDP in 2009 by 5% and by a further 3% in 2010, before a slightly positive growth in 2011. The Commission services' spring 2009 forecast, however, projects that under a no-policy change assumption the general government deficit could reach above 11% of GDP in 2009 and 13% of GDP in 2010, while GDP is expected to contract by around 13% in 2009 and around a further 3% in 2010.

In its March 2009 opinion on the convergence programme, the Council concluded that Latvia is facing a severe economic downturn following years of above-potential economic growth and that therefore the budgetary outcomes in the programme are subject to significant downside risks. The planned restrictive fiscal stance from 2009 until 2011 is considered an appropriate response in light of existing imbalances. The Council invited Latvia to submit to Parliament by the end of March 2009 the details of the supplementary budget adopted on 12 December 2008 and to take further measures if needed to achieve a general government deficit no higher than 5.3% of GDP in 2009 and continue the targeted fiscal consolidation thereafter. It also invited Latvia to implement public sector nominal wage reductions rigorously to facilitate the alignment of whole-economy wages with productivity, thereby improving cost competitiveness, and to strengthen fiscal governance and transparency, by improving the medium-term budgetary framework and reinforcing Ministry of Finance spending controls. It further invited a strengthening of the supply side of the economy by wide-ranging structural reforms and by making efficient use of available EU structural funds.

1.1.9. Lithuania

In 2008 Lithuania's GDP per capita in PPS reached 60.6% of the EU average, while real GDP in 2008 grew by 3.0%. Economic activity decelerated from the beginning

of the year and declined sharply by the end of the year, when the domestic slowdown was reinforced by the deepening global financial crisis and contracting export demand. Whereas private consumption still held up reasonably, investment fell significantly, mostly as a consequence of the end of the real estate boom. Inflation in 2008 rose to an average of 11.1% (5.8% in 2007). The April 2009 Excessive Deficit Procedure notification indicates a budget deficit of 3.2% of GDP for 2008, a substantially weaker outturn than the target deficit of 0.5% of GDP, reflecting both revenue-decreasing measures such as direct tax reductions and substantially higher-than-budgeted expenditures, including an increase in social transfers and a substantial rise in public sector wages. The debt-to-GDP ratio declined to 15.6% in 2008 from 17.0% in 2007.

The January 2009 update of Lithuania's convergence programme covers the period 2008-2011. The central budgetary strategy in the programme is to achieve a medium-term objective (MTO) of a general government structural deficit of 1% of GDP by 2010. From a planned deficit of 2.1% of GDP in 2009 the general government deficit is projected to narrow further in 2010 and to be in balance in 2011, while the macroeconomic scenario underlying the programme projects a sharp contraction of real GDP by 4.8% in 2009 and a further small decline by 0.2% in 2010, before a recovery to growth of 4.5% in 2011. The Commission's spring forecast projects a 5.4% of GDP deficit for 2009. The difference is explained by a markedly less favourable macroeconomic outlook, despite substantial consolidation efforts by the government. The Commission's spring forecast expects real GDP to contract by 11.0% in 2009 and by a further 4.7% in 2010. The budget deficit is expected to rise further to 8.0% of GDP in 2010 in the Commission's forecast, under a no-policy-change assumption.

In its March 2009 Opinion on the convergence programme, the Council concluded that Lithuania is currently facing a severe contraction in domestic demand following years of above-potential economic growth and therefore the budgetary outcomes in the programme are subject to significant downside risks, with the headline deficit possibly exceeding the 3% of GDP threshold in 2009 and 2010. The planned restrictive fiscal stance from 2009 until 2011 is considered an appropriate response in the light of existing imbalances. The Council invited Lithuania to implement measures needed to achieve the budgetary target in 2009 by prioritising expenditures and to continue targeted fiscal consolidation in the medium-term, as well as to strengthen fiscal governance and transparency, by enhancing the medium-term budgetary framework and reinforcing expenditure discipline. To facilitate the alignment of whole-economy wages with productivity and to strengthen cost competitiveness, the Council also invited Lithuania to implement public sector wage restraint.

1.1.10. Malta

In 2007, Malta's GDP per capita in PPS reached 77.4% of the EU-27 average. Real GDP growth decelerated to 1.6% in 2008, down from 3.8% in the previous year. While private consumption was very strong, investment and exports shrank markedly, as the effects of the global downturn started hitting the Maltese economy. The general government deficit increased to 4.7% in 2008, higher than the target of 1.2% set in the November 2007 update of the stability programme. The difference primarily reflects higher-than-planned expenditure by 3 percentage points of which

0.8 percentage point is due to a one-off deficit-increasing measure related to early retirement schemes given to Malta Shipyards employees and 1.3 percentage points are due to the reclassification of the shipyards in the general government sector. Expenditure was also adversely affected as a result of both higher compensation of employees and energy subsidies given to households.

The December 2008 update of the stability programme is based on a significantly favourable macroeconomic outlook, projecting GDP growth to accelerate from 2.2% in 2009 to 2.5% in 2010. In contrast, the Commission's spring 2009 forecast, expects GDP to contract by almost 1% in 2009 before recovering moderately by 0.2% in 2010. According to the programme, the deficit is targeted to fall to 1.5% of GDP in 2009, whereas the Commission's spring 2009 forecast projects a deficit of 3.6% of GDP. The deviation is mostly accounted for by the significantly more favourable macroeconomic scenario of the programme. The budget for 2009 introduced some measures to support the economy in response to the European Economic Recovery Plan, within a broader consolidation effort. These include higher public investment on infrastructure and the environment, support to the tourism industry and SMEs and a widening of personal income tax bands. Under the customary no-policy-change assumption, the deficit is projected to decline marginally to 3.25% of GDP in 2010 according to the spring forecast.

In its Opinion of 10 March 2009, the Council noted that, following a breach of the 3% of GDP deficit reference value in 2008, the December 2008 stability programme envisaged a return to budgetary consolidation from 2009 onwards. There were risks to the achievement of the deficit and debt targets stemming from the favourable macroeconomic scenario, the reliance on volatile revenue, the possibility of expenditure slippages and the lack of information on the consolidation measures in the outer years. The Council invited Malta to resume fiscal consolidation so as to bring the deficit below 3% of GDP in 2009 and ensure that the general government debt ratio was reduced accordingly. Malta was also invited to strengthen the medium-term budgetary framework and enhance the efficiency and effectiveness of public spending.

1.1.11. Poland

In 2007, Poland's GDP per capita in PPS attained 53.7% of the EU-27 average. In 2008 growth started to decelerate due to deteriorating external demand and lower investment activity and real GDP in 2008 grew by 4.9%. Unemployment continued to fall and reached roughly 7% in 2008. The general government deficit increased strongly to 3.9% of GDP in 2008 from 1.9% in 2007, well above the initial targets. Besides slower growth, this result stems mainly from both lower-than-expected revenues and expenditures executed above the planned levels. The debt-to-GDP ratio increased to 47.1% in 2008.

According to the most recent update of the convergence programme the general government deficit was expected to reach 2.5% of GDP in 2009, despite the planned rise in public investment, a personal income tax reform and a reduction of the tax burden for businesses. In the April 2009 fiscal notification the government revised the expected deficit to 4.6% of GDP owing partly to a further slowdown in growth. Nonetheless, the new target for 2009 remains lower than the deficit of about 6.5% of GDP projected in the Commission's spring 2009 forecast. The difference stems

mainly from less favourable growth assumptions in the spring forecast. According to the Commission services, GDP is expected to contract by 1.4% in 2009. The Polish authorities may also anticipate some corrective measures, to be included in an amended budget, which are not yet publically known. For 2010, the Commission projects, under the "no policy change" assumption, that the general government deficit will further deteriorate to more than 7% of GDP.

In its Opinion of 10 March 2009 on the convergence programme update, the Council concluded that given the optimistic GDP growth forecasts, the budgetary outcomes projected in the programme were subject to downside risks, according to the Commission's forecasts, throughout the whole period covered by the current update. In addition, for the outer years, the planned spending restraint would have to be backed up with specified measures, as appropriate. In view of the above assessment, Poland was invited to implement the 2009 fiscal plans, including the stimulus measures in line with the European Economic Recovery Plan and the framework of the Stability and Growth Programme, while avoiding to breach the reference value, as targeted by the Government; back up the consolidation strategy for 2010 and 2011 with specific deficit-reducing measures; and reinforce the budgetary framework through better control over expenditure, including the swift implementation of the amended public finance act and performance budgeting.

1.1.12. Slovakia

Slovakia's GDP per capita in PPS reached 67.0% of the EU-27 average in 2007 while economic growth decelerated to 6.4% in 2008 from 10.4% recorded in 2007. Against the background of strong employment growth, unemployment fell significantly to 9.5% in 2008 from roughly 11% in the previous year. In 2008, annual inflation averaged 3.9% compared with 1.9% in 2007. The increase in annual inflation was mainly driven by rising food and energy prices in the first half of 2008. According to the April 2009 EDP notification, the 2008 general government deficit was 2.2% of GDP, just below the initial target of 2.3 % of GDP foreseen in the November 2007 update of the convergence programme. The better-than-expected budgetary outcome in 2008 was the outcome of the revenue-increasing measures implemented in 2008 (e.g. broadening of the corporate and personal income tax base, increase in the maximum ceiling on social contributions), which offset the shortfall in revenues due to worsening economic conditions.

Slovakia submitted its stability programme on 30 April 2009, covering the period 2008-2012. The macro-economic scenario underlying the programme projects that real GDP growth will decelerate from 6.4% in 2008 to 2.4% in 2009, before rebounding to 3.6% in 2010. Growth should be mainly driven by domestic demand, in particular private consumption and fixed investment. The general government deficit is projected to increase from 2.2% of GDP in 2008 to 3.0% of GDP in 2009 and decline to 2.9% of GDP in 2010, reflecting slower growth as well stimulus and structural measures adopted in line with the European Economic Recovery Plan of 0.4% of GDP. These measures are aimed at boosting internal demand, improving the business environment and alleviating the impact of the crisis on labour markets. According to the Commission's 2009 spring forecast, the general government deficit is set to widen more markedly to 4.7% of GDP in 2009 and, under the no-policy change assumption, to 5.4% of GDP in 2010. The difference in the budgetary projections stems mainly from the much weaker macroeconomic outlook for 2009

and 2010 in the Commissions' forecast, which expects GDP growth to contract by 2.6% in 2009 and slightly rebound by 0.7% in 2010.

In its Opinion of 7 July 2009 on the stability programme, the Council noted that the budgetary projections underlying the programme are based on markedly favourable macroeconomic assumptions and the risks to the budgetary targets are therefore clearly negative. The envisaged expansionary fiscal stance in 2009, including the stimulus measures, was deemed appropriate and in line with the European Economic Recovery Plan and within the framework of the Stability and Growth Pact, especially in view of an ensuing competitiveness challenge. The Council invited Slovakia to implement the planned anti-crisis measures and ensure consolidation as of 2010, which would be backed up by concrete expenditure measures and further supported by the introduction of binding expenditure ceilings for the general government. Finally, in order to preserve the long-term sustainability of public finance in the context of an ageing population, the Council recommended Slovakia to continue reforming the concerned pillar of the pension system and avoid undermining the stability of the fully-funded pension pillar.

1.1.13. Slovenia

In 2007, Slovenia's GDP per capita in PPS reached 89.2% of the EU-27 average. As a highly open economy Slovenia was strongly affected by the global downturn in the second half of 2008 and real GDP growth slowed to 3.5% in 2008 from 6.8% in 2007. Inflation picked up markedly, averaging 5.5% in 2008. The general government balance recorded a deficit of 0.9% of GDP in 2008, which is the same as the target set in the end-2007 update of the stability programme.

The macroeconomic scenario underlying the April 2009 update of the stability programme projects real GDP to fall by 4% in 2009, followed by a mild recovery of 1% in 2010. The Commission services' spring 2009 forecast projects real GDP to drop by 3.4% in 2009, followed by a modest positive growth of 0.7% in 2010. The update of the stability programme targets a deficit of 5.1% of GDP, including also as yet unspecified measures. Taking into account, as usual, only fully specified measures, the Commission services' spring 2009 forecast projects a deficit of 5.5% of GDP. The government has responded to the crisis with two stimulus packages in line with the European Economic Recovery Plan. A wage subsidy for shorter working hours as well as subsidies and tax allowances for investment and R&D, estimated by the government to cost around 1% of GDP, are the main measures in 2009. In addition, companies benefit from tax relief decided earlier, namely a one percentage point cut in the corporate income tax rate and the phasing-out of the payroll tax from 1 January 2009. The Commission services' spring forecast expects a further increase in the deficit in 2010 on a no-policy change basis, to 6.5% of GDP.

On 7 July 2009, the Council adopted an opinion on the updated stability programme of Slovenia. The overall conclusion is that fiscal policy in Slovenia will be expansionary in 2009 in line with the European Economic Recovery Plan. At the same time, as the room for fiscal manoeuvre is constrained by the long-term sustainability challenge, consolidation measures to help finance the stimulus measures have been adopted. The programme plans a return to fiscal consolidation, with improvements in the primary structural balance in 2010 and, to a lesser extent, 2011, but the deficit is not foreseen to be brought below the 3% of GDP reference

value by 2011. The budgetary strategy is subject to downsize risks, as economic growth could be lower than projected. In addition, it might be difficult to reverse the stimulus measures and expenditure overruns cannot be excluded. Although the debt ratio is low (albeit increasing rapidly), Slovenia is assessed to be at high risk with regard to the long-term sustainability of public finances due to the significant projected budgetary impact of ageing. The Council invited Slovenia to: (i) implement the stimulus measures in 2009; (ii) start reversing the fiscal stimulus as planned in the programme in 2010 and implement a significant consolidation thereafter; (iii) improve the long-term sustainability of public finances by further reforming the pension system.

1.2. Conditionality

Article 6 of the Council Regulation (EC) No 1164/94 which governs the Cohesion Fund for projects approved prior to the end of 2006 attaches budgetary policy conditions to the disbursements by the Fund. It provides that "no new projects or, in the event of important projects, no new project stages shall be financed by the Fund in a Member State in the event of the Council, acting by a qualified majority on a recommendation from the Commission, finding that the Member State [...] has not implemented [its stability or convergence programme] in such a way as to avoid an excessive deficit".

At the end of 2008 one Member State eligible for support under the Cohesion Fund (Hungary) remained in the excessive deficit procedure (EDP), which, according to the aforementioned Regulation, may under certain conditions be associated with the suspension of transfers from the Fund. There was however no need to adopt such a measure since the Council, on the basis of available information, decided that the Hungarian government had acted in a manner consistent with its recommendation. As noted in the previous annual report, the Council decided to abrogate the EDP for Slovakia, Portugal, Poland and the Czech Republic in July 2008.

Hungary entered EDP immediately upon accession in 2004, based on a general government deficit of 5.9% for 2003. Since then, Hungary's failure to take effective action in response to Council recommendations has been noted on two occasions, in January 2005 and in November 2005. Since Hungary is not a member of the euro area, it has a specific derogation from the application of further steps of the EDP. In July 2007, the Council issued a new set of recommendations under Article 104(7) of the treaty¹. On neither of these occasions did the Commission recommend a suspension of Cohesion Fund commitments to the Council. In July 2009 the Council decided, in view of the economic crisis, to issue a new deadline of 2011 to put an end to the excessive deficit in accordance with Article 107(7).

¹ Treaty establishing the European Community, Article 104 on excessive government deficits.

2. FINANCIAL EXECUTION OF THE 2000-2006 PERIOD IN 2008 AND CLOSURE OF PROJECTS

2.1. Payments made in 2008 for projects adopted under the 2000-2006 period

In 2008 there were 15 Member States (12 new Member States and Greece, Portugal and Spain) eligible to the Cohesion Fund in which projects were co-financed by the Fund under the 2000/04-2006 period. Since 1 January 2004, Ireland is no longer eligible. Bulgaria and Romania became eligible for the Cohesion Fund with their accession on 1 January 2007.

Given that all commitments for the Cohesion Fund projects financed under 2000-2006 programming period have been executed by 31 December 2006, the financial resources available for the Cohesion Fund in 2008 were made only of payment appropriations.

The 2008 initial budget amounted to € 1,937 million. However, the submission pace of payment requests quickly required reinforcements in terms of payment appropriations. The Directorate General for Regional Policy requested increases of payment appropriations for a total amount of around € 553 million. The increase of the credits was the result of an overall good performance of Member States and in particular for four beneficiary Member States that exceeded their forecasts, namely Slovenia, Slovakia, Lithuania and Estonia.

As far as the ex-ISPA budget lines are concerned, at the end of the year, the situation resulted in 100 % execution rate of the available appropriations.

At the end of 2008, the average absorption rate (payments vs. commitments) of all current beneficiary countries for both the Cohesion Fund and former ISPA projects was 66.3 %. Bulgaria presents the lowest absorption rate (39.8 %), whereas Malta shows the highest absorption rate at 79.8 %. The other Member States range from 50.9 % to 76.1 % of the decided amount.

Table 1 presents the overall payments implementation in 2008 (including technical assistance) for the Cohesion Fund and the ex-ISPA payments:

Table 1: Implementation of the Cohesion Fund and ex-ISPA payments in 2008 (Euro)

Payment Appropriations	Initial	Movements	Final Resources	Outturn	Cancelled	Carryovers 2009
Cohesion Fund	1.936.747.200	+ 250.000.000 + 300.000.000 + 2.779.418	2.489.526.618	2.489.299.691	-	-
Ex-ISPA	650.000.000	-100.000.000 -10.000.000	540.000.000	531.454.029		
TOTAL	2.586.747.200	+442.779.418	3.029.526.618	3.020.753.720	-	-

Table 2 shows the level of payments in 2008 for each Member State. The payments done in the framework of the ex-ISPA contribution are included, as they have all been turned into Cohesion Fund projects at the date of the accession. Main

beneficiary Member States are Spain among the EU-3 Member States, Poland in the EU-10 Member States and Romania in the EU-2 Member States.

Table 2: Payments made in 2008 to Cohesion Fund and ex-ISPA projects per Member State (including technical assistance)

Member State	Environment		Transport		Technical Assistance	TOTAL	
	Amount	%	Amount	%	Amount	Amount	% of total EU 15
Greece	81.235.894	40,7%	115.853.539	58,0%	2.518.623	199.608.056	6,6%
Portugal	121.124.899	62,3%	73.149.733	37,6%	181.537	194.456.170	6,4%
Spain	401.570.546	62,3%	242.969.772	37,7%		644.540.318	21,3%
EU 3	603.931.339	58,1%	431.973.044	41,6%	2.700.160	1.038.604.543	34,4%
Cyprus	5.814.955	65,0%	3.134.086	35,0%		8.949.040	0,3%
Czech Republic	86.699.762	50,3%	84.954.613	49,3%	633.784	172.288.158	5,7%
Estonia	38.398.994	54,6%	29.140.155	41,4%	2.765.566	70.304.714	2,3%
Hungary	40.777.254	51,3%	36.533.591	46,0%	2.110.617	79.421.462	2,6%
Latvia	64.544.604	64,5%	32.774.486	32,8%	2.746.852	100.065.942	3,3%
Lithuania	114.458.156	62,2%	61.109.392	33,2%	8.370.251	183.937.800	6,1%
Malta	5.212.565	99,4%		0,0%	29.765	5.242.331	0,2%
Poland	528.130.703	67,3%	247.053.953	31,5%	9.419.180	784.603.837	26,0%
Slovakia	82.362.076	53,1%	71.696.734	46,3%	927.381	154.986.191	5,1%
Slovenia	22.326.262	45,3%	26.911.481	54,7%		49.237.743	1,6%
EU 10	988.725.331	61,4%	593.308.491	36,9%	27.003.396	1.609.037.218	53,3%
Bulgaria	30.643.656	57,3%	6.944.044	13,0%	15.863.224	53.450.924	1,8%
Romania	180.683.377	56,5%	122.030.336	38,2%	16.947.321	319.661.035	10,6%
EU 2	211.327.034	56,6%	128.974.380	34,6%	32.810.545	373.111.959	12,4%
TOTAL	1.803.983.704	59,7%	1.154.255.915	38,2%	62.514.101	3.020.753.720	100,0%

2.2. Outstanding commitments from the 2000-2006 period

At the end of 2008, the outstanding commitments ("*reste à liquider*", RAL) corresponding to the 2000-2006 period (including two new Member States: Bulgaria and Romania) amounted to € 11.77 billion, down from 2007 (€ 14.80 billion). The 2000-2006 regulatory framework for commitments and payments implies a relatively

large stock of outstanding commitments. They are equal to the amount corresponding to almost three years of commitments.

Table 3: Cohesion Fund and ex-ISPA accepted amounts in 2000-2006 (including RAL)

Country	Net Committed (until 12/2008)	Paid (until 12/2008)	RAL as at 31/12/2008
Greece	2.503.744.174	2.450.738.235	1.152.286.728
Spain	11.788.531.423	9.838.026.775	3.094.434.304
Ireland	573.575.321	570.010.223	55.745.185
Portugal	3.156.539.424	2.427.127.170	1.077.862.318
EU 4	18.022.390.343	15.285.902.403	5.380.328.535
Cyprus	54.014.695	31.793.262	22.221.433
Czech Republic	1.228.077.241	796.786.963	431.290.278
Estonia	427.034.848	289.151.602	137.883.246
Hungary	1.482.597.185	780.102.018	702.495.167
Latvia	713.862.336	499.522.087	214.340.249
Lithuania	846.449.583	559.974.524	265.380.251
Malta	21.966.289	17.529.702	4.436.587
Poland	5.634.539.614	2.871.741.538	2.762.798.076
Slovakia	766.250.297	539.212.844	227.037.453
Slovenia	254.198.103	162.579.583	91.618.520
EU 10	11.428.990.190	6.548.394.123	4.859.501.260
Bulgaria	879.941.333	350.021.546	529.813.137
Romania	2.043.037.858	1.040.128.078	1.002.599.040
EU 2	2.922.979.191	1.390.149.624	1.532.412.177
TOTAL	32.374.359.723	23.224.446.150	11.772.241.972

2.3. Closure of projects from the 2000-2006 period

During 2008, 49 Cohesion Fund and ex-ISPA projects were closed, representing around € 750 million of payments. At the end of 2008, the total number of closed CF projects for the 2000-2006 period (including ex-ISPA projects) reached 216 and the number of projects remaining open decreased to 976 out of 1.192 projects. Table 4 provides information on the projects closed until the end of 2008 per Member States.

Table 4: Number of CF projects closed until the end of 2008 (including ex-ISPA)

Country	Total number of CF projects	Projects closed as of end 2008		Number of open projects as of end 2008
		Number of Projects	Total Paid in Euro	
Greece	124	34	886.825.780	90
Spain	407	80	2.363.473.998	327
Ireland	10	3	250.368.797	7
Portugal	109	24	580.082.620	85
EU 4	650	141	4.080.751.195	509
Czech Republic	58	14	192.671.263	44
Estonia	37	14	75.086.815	23
Cyprus	2	0	0	2
Latvia	46	10	44.331.604	36
Lithuania	51	9	82.084.499	42
Hungary	47	10	11.153.890	37
Malta	3	0	0	3
Poland	130	5	27.825.974	125
Slovenia	28	6	55.213.444	22
Slovakia	39	4	6.880.841	35
EU 10	441	72	495.248.330	369
Bulgaria	38	1	950.121	37
Romania	63	2	1.794.822	61
EU 2	101	3	2.744.943	98
TOTAL	1.192	216	4.578.744.468	976

3. THE IMPLEMENTATION OF THE 2000-2006 PROJECTS BY MEMBER STATES

3.1. Greece

3.1.1. Environment

The solid waste management interventions are based on the 2003 National Solid Waste Management Plan which in turn is linked to Regional Management Schemes. The strategic objective is the appropriate integrated management of urban solid waste and, where necessary, the rehabilitation of polluted or degraded areas. A similar plan has been drawn up for the collection and treatment of urban waste water, in accordance with the requirements of Directive 91/271/EEC.

Progress is noted in particular in relation to those Cohesion Fund projects that concern waste water treatment plants and closure of illegal landfills. The rate of performance of the environment projects differs per sector. While the waste water treatment projects are relatively well advanced, solid waste infrastructure, drinking water and nature protection projects, and in particular large projects such as the construction of dams, are seriously delayed. Close monitoring and accelerated efforts are required in order to ensure that they are completed and put into operation within the timeframes set. One of the main problems in the implementation of projects presenting a very low absorption remains in particular in the field of infrastructure works for solid waste management in Attiki region.

However, it should be noted that delays in the implementation of projects may also occur due to social reactions, in particular as regards waste management projects. Furthermore, the implementation of projects may also be linked to the application of a number of requirements deriving from relevant Directives and reflected in the specific terms of the funding decisions. Since 2002, Cohesion Fund decisions include certain specific clauses whose fulfilment, in a number of cases, is a precondition for the execution of either the advance or interim and final payments. These specific terms ensure that the projects co-financed are sustainable and comply with the requirements of the Community environmental legislation. These specific terms can be divided into those of an administrative nature (e.g. setting up of a solid waste management body or of an agency to manage the operation of a dam), and those of a legal or technical character (e.g. the completion of the legal framework relating to the solid waste management or certain actions considered necessary for the integrated management of solid waste). The timely and efficient application and implementation of these requirements are directly related to the implementation of the projects concerned.

Modification requests in the field of the environment received by December 2007 were treated in 2008. Very few remain pending, mainly because there is a need to update environmental terms or there are pending legal proceedings. These modification decisions concerned mainly the extension of the final date of eligibility, the adaptation of the physical object and the financing plan.

3.1.1. Transport

The strategy for transport projects seeks to develop the following corridors and projects:

- the priority trans-European (TEN) road axes in Greece, i.e. the PATHE, EGNATIA and IONIAN axes, as well as the Korinthos – Tripoli – Kalamata / Sparti motorway;
- the modernisation of the PATHE railway axis, also part of the TEN, including its electrification and signalling systems, and construction of a freight railway line from the Ikonio port to the railway freight centre of Thriassio;
- the infrastructure facilities of Igoumenitsa and Iraklion ports including the construction of new port infrastructure at Lavrio;
- the airports of Thessaloniki and Iraklion and the air traffic control system in Greece; and
- public transport infrastructures in Attica and Thessaloniki, such as metro, tramway, and bus transport.

In 2008, two modification requests for transport projects were processed. These modifications mainly concern the extension of the final date of eligibility, the adaptation of the physical object and the financing plan. It is clear that the transport projects are progressing better than the environment projects with motorway projects being particularly well advanced.

3.2. Spain

3.2.1 Environment and transport

Activity in 2008 was limited to physically following up and financially auditing ongoing projects, accompanied by interim payments to projects depending on progress recorded, closure of finalised projects and adjustments to reflect the reality of the situation on the ground, through amendments to the Commission Decisions granting Community aid.

Altogether, 12 projects were closed in 2008, all from the period 2000-2006. Almost all (11 of them) were environment projects. The outstanding commitments in respect of these projects stood at € 3.1 billion. This represents a 17% reduction in the outstanding commitments associated with the Cohesion Fund for 2008.

In addition, in order to create wider awareness and a better understanding of the "Guidelines on the Closure of Cohesion Fund and Ex-ISPA Projects 2000-2006" adopted by the Commission in April 2008 (SEC (2008)415), a seminar was held in Madrid on 16 and 17 October 2008, attended by over 300 participants. This provided an opportunity to remind the players involved in the closure of projects of the deadlines and the regulatory requirements involved in the closure procedure.

As regards amendments to project decisions, 29 amending decisions were approved in 2008. Of these, 18 concerned the environment sector and 11 the transport sector. In general, the amendments involved extending the projects' scheduled completion dates, often accompanied by modifications, mostly minor, to the physical object of the projects. The amendments had no impact on the total eligible cost of projects or on the level of Community assistance.

The inclusion of some flexibility in the rule for amending 2000-2006 Cohesion Fund decisions was presented to the Member States in February 2008. As a result, a total of 69 amendment requests were sent by the Spanish authorities, the vast majority (65) relating to environment projects. They are still under examination.

As regards interim payments and payment of balances, 184 payment requests were received, with a total of € 644.5 million paid out. This is less than in 2007 and significantly less than in 2006, when the total payouts were, respectively, € 742.6 million (for 229 payment requests) and € 1 283 million (for 255 payment requests), which reflects the decreasing number of open projects.

Finally, the Commission services, in compliance with Commission Regulation (EC) No 621/2004 of 1 April 2004 concerning information and publicity measures, were very attentive to measures aimed at increasing the visibility of projects and raising public awareness on the role of the European Union. In particular, given its economic and social impact and the amount of money invested, the national authorities took care to emphasise in 2008 the role the Community has played in financing port infrastructures in Spain.

In this framework, a press conference was held in Madrid on 15 December, in the presence of the Spanish Secretary of State for Transport and representatives from the Commission, to publicise the Community's involvement in providing and improving port infrastructures in Spain. Indeed, European co-financing for this type of transport infrastructure over the period 2000-2006 was considerable, representing € 2 157 million in eligible costs through the co-financing of 22 projects, with € 1 169 million having been provided through the Cohesion Fund.

3.3. Portugal

3.3.1. Environment

According to the environment strategic reference framework for Cohesion Fund interventions under the 2000-2006 period, the priority sectors financed by the Fund are "Water Supply", "Sewerage and Wastewater Treatment" and "Urban Waste Management".

The strategic reference framework was updated in the mid-term review exercise conducted in 2004, which emphasized the need for reinforcing coordination between the Cohesion Fund and Structural Funds. In this context, the regional programmes have also focused on projects that contribute to the accomplishment of the municipal systems of water supply, urban waste water treatment and solid waste treatment, in the latter case with a particular emphasis in the development of recycling and the reduction of landfills. The integrated water networks in the areas of Minho-Lima and Vale do Ave and the waste treatment system in Madeira are worth mentioning, in view of the overall financial support involved from the Cohesion Fund.

Seventeen amending decisions were adopted during the year, generally to adjust the final specifications of projects, mostly in order to include new elements and/or amending others, and to extend the date of projects' completion. In 2008, four environmental projects were closed.

3.3.2. *Transport*

As for the environment sector, transport infrastructure development under the Cohesion Fund is programmed within a strategic reference framework for the 2000-2006 period, in coordination with the Transport and Accessibilities Operational Programme, and notably its priority axis 1 relating to the TEN-T network.

The projects under implementation contribute to the development of the Trans-European Transport Network and enhance the multimodal articulation amongst the various means of transport in place, in line with the objectives of the strategic reference framework. The ongoing investments in railway infrastructures, upgrading the north-south railway axis and northern and southern links from Portugal to Spain are of particular importance in this context. Other important areas are the enlargement of the harbours in Madeira and Açores and the development of the underground networks in Lisbon and Porto.

Four amending decisions were adopted during the year which related to adjusting the projects' description and extending the dates of completion.

3.4. **Cyprus**

The Cohesion Fund allocation for Cyprus amounts to approximately € 54 million. Two projects are co-financed by the Fund: one transport project (upgrade of Limassol motorway) and one environmental project (solid waste management covering the regions of Larnaka-Ammochostos).

In the framework of the partnership with the Cypriot Authorities and in order to ensure sound financial management of Cohesion fund projects, both projects were surveyed. The transport project is advancing satisfactorily, with an absorption rate of more than 80%.

Concerning the environment project, it is to be underlined that its implementation was delayed, due to reactions from the residents of nearby municipalities, resulting in the relocation of part of the project. In view of this situation and the subsequent slow absorption, this project was subject to a specific technical meeting with the Cypriot Authorities in December. An updated modification request, including the extension of the eligibility date, is expected to be submitted to the Commission.

3.5. **Czech Republic**

3.5.1. *Environment*

The implementation of the Cohesion fund projects in the sector of environment is progressing well. Out of 38 projects approved in 2000-2006 programming period, five were closed during the year and the closure procedure was launched for three other projects. Most of the ongoing projects are in the final stage of implementation.

In 2008, the Commission received five requests for modification of the Commission decision. By the end of the year, two amending decisions were adopted. One modification concerned the correction of technical errors in the text and the second one the extension of the eligibility end date (which is also the reason for the other already submitted modifications).

In order to help the Czech authorities to cope with the fulfilment of the specific condition on private operators in the water sector inserted in most of 2004-2006 Commission decisions, the Commission decided to make use of the technical assistance. The assignment started in September 2008 and should be achieved by May 2009.

3.5.2. *Transport*

In the sector of transport, the progress of the implementation is well advanced for most of the projects. In 2008, one project was closed. At the same time, the closure procedure was launched for another transport project in 2008. One modification request for technical assistance in the transport sector was approved in 2008. This modification concerned the extension of the eligibility end date and an update of the indicative list of projects.

3.6. **Estonia**

3.6.1. *Environment*

Due to the overheating of the construction market, cost overruns were observed (on average 217% since 2006). Up to end 2007, the implementation of projects was delayed by these cost increases. For several projects, the implementing bodies were not able to accept tender results in 2007 due to too high prices and possible cartel agreements. The situation reversed in 2008 and this enabled to go forward with the projects. Estonia planned an extra EEK 720 million to be financed out of the State budget for the years 2007 and 2008 in order to cover these cost overruns.

The Commission approved one modification decision concerning a technical assistance project for preparation and management of the Cohesion Fund. The decision consisted in extending the eligibility end date and modifying the list of sub-projects and their cost without any modification of the project's total cost.

Delays in the progress of project implementation were mainly due to delays in the design and/or construction, and/or to cost overruns.

The Estonian authorities had some difficulties in meeting the requirements of cost-benefit analysis during the closure process of projects. Consequently, closure of environment projects took between six months and one year. In the meantime, the Estonian authorities decided to take measures to improve their compliance with cost-benefit analysis. Nevertheless, at the end of 2008, nine projects were closed and two were under the process of being closed.

3.6.2. *Transport*

Works on all transport projects have started on the ground. Three modification requests were submitted in 2008 in the transport sector. They concerned "Tallinn-Tartu-Võru-Luhamaa road Vaida-Aruvalla section and Puurmanni junction"; "Eastern extension of Muuga harbour", and "Jõhvi-Tartu-Valga road".

Technical assistance has helped prepare transport infrastructure projects for implementation in the 2007-2013 programming period. The use of the JASPERS facility enabled a better preparation of major projects to be submitted in future.

By the end of 2008, seven projects (including two technical assistance projects) were closed. Among the closures, one technical assistance project that did not reach its objectives was identified. The Estonian authorities agreed to correct the final payment request accordingly.

3.7. Hungary

3.7.1. Environment

In 2008, further progress towards the completion of ongoing projects was observed and the first projects adopted in 2000 and 2001 are in their final stage of implementation. In spite of the initially slow development, projects adopted in the last years of the 2000-2006 programming period show in general an improved performance.

A number of projects in the solid waste sector show significant cost overruns due to the underestimation of initial budget for the rehabilitation of landfills, which were non-compliant with the European and national legislations. Most of these projects were modified and their scope reduced. The rehabilitation works which were taken out from the 2000-2006 period, will be carried out in the 2007-2013 period.

In the case of two solid waste projects (North-East Pest and North Balaton) notoriously lagging behind, the contracting rate improved significantly in 2008 (58% and 92% respectively). These projects are now on track and will be completed by the end of 2010.

Waste water projects are mostly faced with cost savings, which shall be used within the projects by the end of 2010 for financing additional elements in line with the initial project objectives. The savings within the biggest ongoing environment project – the Budapest Central Municipal Wastewater Treatment Works and Collector Systems – amount to € 63 million. Due to the financial corrections to the main contract, additional € 62 million are likely to be replaced with new elements within the framework of the current modification request.

The Győr wastewater project and two technical assistance projects (Zagyva-Tarna river basin management plan; Preparation of Ex-ISPA projects) were closed.

Closure documentation for two projects (Miskolc waste and Szeged wastewater) were submitted to the Commission in the fourth quarter of the year. Their closure procedure is ongoing.

3.7.2. Transport

The projects' implementation continued at an increased pace, due to the fact that four modification decisions were adopted by the Commission.

Cost overruns were encountered in a number of rail projects, but the necessary funds to cover overruns in the railways projects were made available from national sources at the end of 2008.

In several projects public procurement problems have led to the re-launch and review of a number of contracts. This caused serious delays and puts certain projects at risk

of not completing all elements by the currently foreseen eligibility end date. In certain projects important works contracts have still not been contracted.

Problems related to land acquisition are present in a number of projects. While in some cases the outstanding issues are purely procedural, there are instances where work is being delayed because of this.

No transport projects were closed or are in the process of being closed. Four modification requests (three rail projects; one road project) were received in the fourth quarter of the year.

3.8. Latvia

3.8.1. Environment

Closure payments for two projects were effected: "Solid waste management in Ziemeļvidzeme region" and "Technical assistance for environmental projects".

The Commission also adopted four modifying decisions for the following projects:

"Development of Water Services in Rēzekne City"; "Technical assistance for projects for water services development in Latvian municipalities"; "Development of Water Services in Daugavpils, Stage II"; "Technical assistance for the environment sector in Latvia". The modifications mainly concerned an extension of the eligibility end date; adjustment to some of the physical indicators and consequently to the description of the projects; inclusion of additional components.

3.8.2. Transport

Closure payments for three projects were effected: "Improvement of Via Baltica road from Gauja to Lilaste", "Improvements of links to Via Baltica (Airport Access Road and a related section on A10" and "E67 Via Baltica, section Ķekava – Iecava".

The Commission also adopted four modifying decisions for the following projects:

"Riga Airport: Runway extension and lightning system reconstruction"; "Modernization of the signalling system in Latvia"; "Technical Assistance for Transport Sector in Latvia"; "Technical Assistance to Ministry of Transport". As for environment projects, the modifications mainly concerned the extension of the eligibility end date; adjustments of some of the physical indicators; the inclusion of additional components.

3.9. Lithuania

3.9.1. Environment

The closure procedure for two environment projects was successfully finalised at the beginning of 2008; the closure of a third project was initiated in July 2008.

Four modifying decisions, related to the extension of the end date and adjustment of monitoring indicators, were adopted. In addition, nine modification requests were

received in the last quarter of the year, of which the majority concern cost overruns and the extension of the eligibility end date.

3.9.2. Transport

Four projects were closed before 2008. In 2008, the closure procedures were initiated for two transport projects, of which one was successfully completed; the closure of the second project was finalised in January 2009.

Lithuania also submitted four modification requests for transport projects. All of them were infrastructure projects. The modifications included the extension of eligibility end dates and adjustments to the physical monitoring indicators.

3.10. Malta

3.10.1 Environment

The project "Upgrading of Sant' Antnin waste treatment facilities" aims at reducing the negative environmental impact of the waste cycle, which is of utmost importance for the Malta main island due to its very high population density.

The Commission decision was modified on 13 August 2008 with the result that a new mechanical treatment plant will be built instead of upgrading the existing one. An extension of the eligibility end date until 31 December 2010 was also included.

The project is progressing well. The material recycling facility has been completed; the acceptance certificate for the final handover was issued in May 2008.

3.10.2. Transport

The project "Restoration and upgrading of sections of TEN-T" consists in the upgrading of three lots of the TEN-T network in Malta and Gozo (St. Paul's Bay bypass, Civil Aviation Avenue in Luqa and Mġarr Road in Għajnsielem in Gozo) in order to reduce travel time, accident rates, transport costs and facilitate competitiveness in the transport of goods.

The Commission decision was modified on 17 October 2008, covering transfer of funds between the project sections and extending the eligibility end date until 31 March 2010.

The project is physically complete. Further savings have arisen and an additional modification request to include further section(s) of the TEN-T network is awaited.

Technical Assistance

The project aims at preparing the environment projects pipeline for 2007-2013 (mechanical biological waste treatment plants and storm water master plan). The Commission decision was modified on 30 July 2008 in order to take into account the delays in the identification of potential sites for the waste treatment plant and the need to comply with obligations arising from Directive 2001/42/EC. In addition, the deadline for the eligibility of expenditure was extended until 31 December 2010.

3.11. Poland

In 2008, the Commission adopted fourteen amending decisions granting assistance from the Cohesion Fund – eight in the environment sector and six in the transport sector. In addition, the Commission adopted eight modifying decisions. The modifications mostly concerned the physical scope and/or the eligibility end date of the projects, as well as the increase of the threshold for interim payments.

A substantial number of projects will be finalised in 2010, which means that the bulk of closures can be expected in 2011. Numerous projects in both sectors indicated significant cost overruns which in total represent approximately 1/3 of the Cohesion Fund allocation for Poland.

In 2008, the Commission authorised payments amounting to € 784.6 million.

3.11.1. Environment

The level of contracting was over 100% of the originally estimated costs for environment projects, taking into account the cost overruns. The physical and financial progresses aggregated for the sector were about 55% and 50% respectively. About one third of projects reached the threshold for interim payments at the end of the year.

At the end of the year, unlike for transport projects, there were still some environment projects for which the national authorities were still seeking for appropriate solutions to finance cost overruns. Seven environment projects were subject to pending environmental impact assessments (EIA).

One closure was ongoing for an environment project.

3.11.2. Transport

The level of contracting was over 100% of the originally estimated costs for transport projects, taking into account the cost overruns. The physical and financial progress aggregated for the sector was about 57% (both physical and financial) for roads and 62% (both physical and financial) for railways. Almost half of transport projects reached the threshold for interim payments.

At the end of the year, three transport projects were still subject to pending environment impact assessments (EIA).

The closure procedures for 3 investment projects were ongoing. In the sector of transport, the national authorities managed to secure the additional financing for all projects concerned by cost overruns.

Technical assistance

One closure was ongoing and another one was initiated for technical assistance projects.

3.12. Slovakia

3.12.1. Environment

Significant progress in financial and physical implementation was recorded in the majority of environment projects. Relatively few projects remain problematic: Galanta, Samorin, Home Kysuce, and Velky Krtis water sector projects. In the case of these projects the Slovak authorities were advised to draw up action plans to monitor progress closely and identify steps to be taken to ensure their completion by the end of 2010.

Ten modification decisions were adopted (Komárno, Kosice, Humenne, Trnava, Piestany, Zvolen, Zilina WWTP, Poprad, TA Regional water companies, and TA water sector). The modifications concerned mainly the extension of eligibility end dates to take account of delays incurred in particular during the earlier procurement stage, and the adjustment of physical indicators. Cost overruns are a growing problem in a number of projects, with final beneficiaries (public water sector companies) having to fund the additional costs.

Three water sector infrastructure projects were completed in 2008 (Nitra, Považská Bystrica, and Martin) plus one technical assistance project. The quality of final reports was generally considered to be insufficient and final payments were therefore interrupted pending improvements. Weaknesses related in particular to the project descriptions, statements on achievement of project objectives, and demonstration of financial sustainability.

3.12.2. Transport

All contracting within the transport projects had already been completed in 2007 (with some minor exceptions) and physical implementation further advanced satisfactorily during 2008. As for environment, the Slovak authorities were advised to draw up an action plan for the main problematic transport project: Mengusovce-Janovce motorway, which has suffered implementation delays, cost increases and design changes.

The first transport project "Modernisation of rail track Bratislava Rača-Tmava (section Bratislava-Rača-Šenkvice)" was closed and two other projects (one road infrastructure and one for technical assistance) were submitted for closure. The road project in question relates to the Bratislava-Vienna Port Bridge.

3.13. Slovenia

3.13.1. Environment

In line with the Strategic Reference Framework for the Cohesion Fund, the main aim for assistance from the Cohesion Fund and former ISPA during the period 2000-2006 was to assist municipalities and regions in improving drinking water supplies, sewerage networks and wastewater treatment (a total of 12 projects in the water sector) and waste management (4 projects).

In 2008, after several years marked by delays in public procurement, the last contracts for works were successfully concluded. As many projects are set up as

design and build, the actual construction lagged several months behind the date of contract signature. However, those projects which entered the construction phase steadily progressed both physically and financially.

Four projects in the water sector completed already in 2007 yet remain to be closed. Construction and/or trial operation on one further water project and one in the waste sector were finished as well. In compliance with the relevant procedures, closure of these projects is expected in 2009.

3.13.2. Transport

The national authorities have defined in 2003 a National Cohesion Strategy for the Transport sector which identifies the objectives of its transport strategies and the projects to be financed. It involves the country establishing itself as a maritime transit country within the European Union and market its geopolitical position at the crossroads of two important European corridors (Corridors V and X) along the existing southern border of the EU. To this end, bottlenecks on corridors must first be removed involving the completion of the motorway network, upgrading, modernisation and completion of the rail network and the increase of the range of logistical services.

The Cohesion Fund co-finances six railway and two motorway projects. In early 2008 one motorway and one railway project were closed, while construction on the second motorway project was finished. After reported delays due to public procurement in previous years, railway projects (except partially one) were fully contracted and marked progress in works as well as in payments executed. The closure of remaining transport projects is expected in the beginning of 2010.

4. MONITORING, INSPECTIONS, FINANCIAL CORRECTIONS AND IRREGULARITIES

4.1. Monitoring: committees and missions

4.1.1. Greece

One major technical meeting took place in June in Brussels with the managing authority of the Cohesion Fund and DG REGIO to review and monitor the progress of all projects. Three other technical meetings took place in Athens to ensure the close monitoring, identify the critical issues, boost further the implementation and identify actions that will ensure total absorption of funds by 2010.

No monitoring missions for ongoing projects were carried out in 2008.

4.1.2. Spain

The monitoring committee met in Madrid on 24 April. In preparation for the meeting the national authorities submitted information sheets outlining the implementation situation as at 31 December 2007 in respect of all the decisions (single projects or groups of projects) still ongoing. From these information sheets the managing authority, in partnership with the Commission services, selected 50 projects which, by virtue of their particular situation, were subject to specific monitoring and

analysis by the Committee during its sessions. At the meeting the Commission services highlighted three points:

- It was underlined that, although some flexibility was introduced in the revised guidelines on the amendment of Cohesion Fund projects, there was no automatic entitlement to further modifications; requests still have to meet the conditions laid down in the guidelines; the eligibility end date of 31 December 2010 was also confirmed.

- The Guidelines on the Closure of Cohesion Fund Projects were adopted by the Commission on 4 April. The Commission services invited the Spanish authorities to organise a seminar on this question, which was subsequently held in Madrid in October.

- The third point concerned the recurring problem of the recovery of VAT amounts concerned by the Court of Justice judgment of 16 October 2005. The Commission services urged the Spanish authorities to effect these recoveries without delay, even if this means leaving open the cases affected by tax inspections or legal appeals.

Finally, the Commission services mentioned Commission Regulation (EC) No 621/2004 of 1 April 2004 concerning publicity measures. They pointed out the obligation to take effective information and publicity measures so as to increase the visibility of Cohesion Fund projects and raise public awareness on the role the European Union is playing through its Cohesion policy.

Technical and follow-up missions

On 28 November a technical meeting was held in Madrid between the managing authority, the certifying authority and DG REGIO to address the problems encountered in the day-to-day management of projects and possible measures for solving them. Three main topics were discussed, namely delays in the examination of modifying requests; difficulties encountered during the closure of projects; organisation of the "information and publicity" day concerning port infrastructures.

In addition, two follow-up missions took place in 2008. The first was a visit to Pamplona on 19 February, concerning project "Actuaciones en materia de residuos urbanos en la Comunidad Foral de Navarra" (Urban waste management measures in Navarra). The object of the visit was to examine alternative waste treatment solutions to that proposed in the decision adopted in 2001, as a court decision had brought the infrastructure works to a halt.

The second, on 20 May, was a visit to project "Actuaciones de Suministro de Agua y Abastecimiento a poblaciones ubicadas en la Cuenca Hidrográfica del Río Guadiana: Comarca del Andévalo" (Water supply to populations living in the Guadiana river basin, district of Andévalo), to check how the project was progressing on the ground. The visit was decided upon as a result of the Member State having applied for a second amendment to extend the period of eligibility. The inspectors were able to obtain clarification from the project leaders on the difficulties encountered in implementing the project and to evaluate the "*force majeure*" arguments put forward by the project managers.

4.1.3. Portugal

The two monitoring committee meetings concentrated on the follow-up of the implementation of the projects and the solution to the problems encountered. Both meetings were held in Lisbon, on 26-27 May and on 25 November.

The May monitoring committee reviewed approximately half of the ongoing projects and those approaching closure. It also examined the prospects for implementation during the rest of the period. It was preceded by a technical meeting between the Cohesion Fund national authorities and the Commission, in order to discuss the main outstanding issues.

The November monitoring committee meeting focused on projects or types of projects with particular problems or outstanding issues, as identified by the Commission and/or the Member State. General questions were also discussed, notably the perspectives for completion of open projects or groups of projects in the two full years still available. It was also preceded by a technical meeting between the Cohesion Fund national authorities and the Commission.

During the year, several projects were visited by the Commission services in order to take note of their state of progress and, in certain cases, to discuss with the national authorities technical or legal problems which have arisen.

4.1.4. Cyprus

Technical meetings took place in June and December. Progress in the implementation of the two Cypriot projects was presented, while other technical issues related to monitoring and reporting were also addressed.

4.1.5. Czech Republic

In general, two Cohesion Fund monitoring committee meetings are organised each year. Due to heavy workload at the end of 2007, the second 2007 monitoring committee took place on 15-16 January 2008. Further monitoring committees took place on 24-25 June and on 9-10 December. Discussions were organised on a project-by-project basis using the monitoring sheets and giving substantial time to the national authorities, beneficiaries and the Commission to clarify any outstanding issues. Issues of general character were discussed in the Core Group meeting with the national authorities.

In the course of the year, the Czech Cohesion Fund managing authority further improved the monitoring of the implementation of projects allowing for a better overview of the progress on the ground.

4.1.6. Estonia

One monitoring committee was held in 2008 covering implementation, quality of spending, financial progress and publicity actions. Furthermore, a contract of confidence was signed on 12 February between the Commission and the national audit authority. The compliance assessment of the monitoring and control system for the Operational Programmes 2007-2013 has not been completed in 2008.

Situation regarding lags in the implementation has been followed on a constant basis. The Commission highlighted mainly the need to learn from the past and try to improve and build on existing experience for the 2007-2013 programming period. Issues relating to the Cohesion Fund under the 2007-13 period were covered in the two Monitoring Committees held in April.

4.1.7. Hungary

Four Cohesion Fund monitoring committee meetings (two for each sector – environment and transport) were held in Budapest, on 8-10 April and 29-31 October. All adopted projects were reviewed and overall presentations were provided.

The monitoring committee meetings were conducted in the form of technical discussions on a project-by-project basis, giving sufficient time to each final beneficiary to present the progress of each project.

4.1.8. Latvia

Two monitoring committees took place in Riga, on 11 April and on 7 October. The meetings were used for the monitoring and assessment of the progress in implementation as well as for discussions on any problem encountered and on horizontal issues such as financial execution, publicity, technical assistance.

During the April meeting, the impact of cost increases on projects was discussed and the Latvian authorities reported on the steps taken to combat inflation. In both meetings problematic projects were closely monitored: i.e. "Track renovation on stages of the East-West rail corridor in Latvia", "Modernisation of rail signalling systems" and "Development of the district heating supply system in Ventspils". On 10 April, the Commission representatives visited the project "Solid Waste Management in the Maliena Region" and observed planned administrative, financial and technical checks performed by the Ministry of Environment.

On 7 October, the Commission representatives visited two projects: "Modernisation of the signalling system" on the upgrading of the Latvian East-West railway corridor; and "Hazardous waste management in Latvia, Stage I" for the establishment of a national Hazardous Waste Management System.

4.1.9. Lithuania

Two monitoring committee meetings took place, on 21-23 April and 6-7 November. The committee examined the progress reports submitted by the national authorities and discussed the implementation of all ex-ISPA and Cohesion Fund projects and how to accelerate their implementation. In addition, an ad-hoc monitoring committee meeting was held on 28-29 July to address the amendment of certain environment projects having encountered significant cost overruns.

Two technical missions took place in February for on-site visits, meetings with the final beneficiaries, discussions on the implementation and closure of projects, preparation of applications for major projects, support from JASPERS (Joint Assistance in Supporting Projects in European Regions), and foreseen publicity measures.

4.1.10. Malta

The monitoring committee meetings for all three Cohesion Fund projects were held on 23 May and 16 October. Annual progress reports were submitted for all three projects.

A monitoring mission on the project "Upgrading of Sant' Antnin waste treatment facilities" took place on 21 May.

4.1.11. Poland

Two monitoring committees were held, on 27 June and 12 December. The meetings were preceded by meeting of working groups for the environment sector and the transport sector.

The meetings were dedicated to the review of the progress in implementation of individual projects. Besides that, a number of horizontal issues were discussed, namely: payment rate and financial forecasts, cost overruns, EIA conditions, closure forecast, modifications of projects in terms of scope and timeline, delays in implementation, and compliance with the "M+24" and "M+12" rules. The review of end dates revealed that a substantial number of projects will be finalised only in 2010 which means that the bulk of closures can be expected in 2011. Numerous projects indicated substantial cost overruns which in total represent approximately 1/3 of the Cohesion Fund allocation for Poland. The sector of transport secured the additional financing for all concerned projects. In the environment sector, there was a limited number of projects for which the national authorities were still seeking for appropriate solutions. These cases were closely monitored in both monitoring committees. A special attention was paid to the monitoring of seven projects with pending EIA conditions. No projects breaching the M+24 and M+12 rules have been recorded.

No Cohesion Fund monitoring missions were carried out during the year.

4.1.12. Slovakia

Two monitoring committee meetings were held, in Bratislava (March) and Nitra (October). The monitoring committees reviewed the state of progress of all ongoing ex-ISPA and Cohesion Fund projects. Recommendations were made to improve reporting on physical indicators, identification of legal and technical problems in implementation, and on audit findings. Attention focused in particular on projects at risk of not being completed by the end of 2010, for which the Slovak authorities have now drawn up action plans.

In addition, key horizontal issues were discussed: privatization of water companies; cost overruns; closure of projects; quality of final reports; and the need to identify lessons learned from the 2000-2006 period to be applied in future major projects.

Site visits to the Kosice and Humenne water sector projects took place in April, during which the proposals for modification were discussed and progress on the ground was observed. In addition, site visits to the Komárno WWTP project was undertaken during the March monitoring committee, and to two additional projects on

the occasion of the October committee: Nitra WWTP (completed project under closure procedure) and Galanta (problematic project).

The representatives of the Commission also participated in two audit missions in April (follow-up systems audit for the Cohesion Fund) and in November (retrospective verification of public procurement).

4.1.13. Slovenia

One monitoring committee meeting was held, on 25 November. It focused on the ongoing implementation of projects, delays in public procurement, cost overruns, project closure and publicity. The meeting included a detailed review of all ongoing environment and transport projects as well as a discussion on payments and payment forecasts. The Commission in particular highlighted the necessity to further accelerate the implementation of projects where substantial delays occur.

One project visit was carried out in the framework of the monitoring committee. The three visited environment projects (one in the water sector and two in the waste sector) showed satisfactory progress.

4.2. Audits and financial corrections

2008 was a year of overlap between the management of the final stage of implementation of the 2000-2006 programming period including the preparation for its closure, and the opening of the 2007-13 programming period. The management and control environment in place in 2008 was therefore meant to address both risks related to the preparation for closure of past programmes and projects and the risks of set up of management and control systems in the new programmes.

Audit work for Programming period 1994-1999 - EU 4 (Greece, Ireland, Portugal, Spain):

The Cohesion Fund closure enquiry concerning the period 1994-1999 covered 10% of Cohesion Fund projects representing 20% of the co-financed expenditure during this period. The fieldwork was finalised in 2003 and the main deficiencies found were insufficient management verifications resulting in ineligible expenditure and breaches of public procurement rules. Financial correction procedures resulting from the closure enquiry were concluded during 2008, except for three remaining projects (two in Spain, one in Portugal) which will be finalised in 2009.

Audit work for Programming period 2000-2006 - EU 14 (EU 10 + EU 4):

For EU-14 Member States in 2008, four audit missions were carried out which focused on the follow-up of previous audit recommendations. In addition, five missions for the review of winding-up bodies were performed in order to verify the preparation of Member States for closure and to identify and mitigate related risks.

In 2008, DG Regional Policy examined winding up declarations submitted for the closure of 2000-2006 Cohesion Fund projects, of which 60 (representing 5% of all projects) related to Spanish projects.

Other audit work for the programming period 2000-2006 included the examination of the annual control reports received under Article 12 of Regulation No. 1386/2002. By the end of 2008, the majority of reports had been analysed, and replies sent to the Member States with observations and, where necessary, requests for additional information in order to be able to draw as much assurance as possible from the results of national audit work. Furthermore, a number of national system audit reports were received in 2008.

The last of the annual bilateral coordination meetings with the Directorate General for Regional Policy for the year 2007 was held in February 2008. As 2008 was a transitional year, it was decided to reschedule the bilateral coordination meetings for 2008 to the first half of 2009. Bilateral meetings are held annually with national audit authorities to exchange information on the implementation of audit work and to discuss progress on sample checks and follow-up of audit findings. The meetings in 2009 will cover issues concerning both programming periods 2000-2006 and 2007-2013.

Impact of controls

Financial corrections

In the exercise of its supervisory role, DG Regional Policy has implemented a policy of suspending interim payments and applying financial corrections as soon as it is established that there are serious deficiencies which put at risk the reimbursements of Funds made to Member States. It also established a revised manual of procedures to streamline the internal arrangements for the adoption of suspension and correction decisions.

Where, after due verifications, the Commission finds that the expenditure certified in an interim payment application is linked to a serious irregularity and not immediate remedial action is taken by the Member State, the formal suspension of payments procedure is launched. During 2008 DG REGIO adopted for the Cohesion Fund one suspension decision concerning Bulgaria in relation to two projects in the road sector.

Financial corrections totalling € 92.7 million were made in 2008 as follow-up to audits by the Commission or the Court or Auditors or to OLAF enquiries. Of this total, € 38.2 million related to projects of the 1994-99 programming period and € 54.5 million to the 2000-2006 period. The corrections were either applied by formal Commission decisions (€ 66.2 million) or were accepted by the Member States without the need for a decision (€ 26.5 million).

Four financial correction decisions related to Cohesion Fund projects in the 1994-1999 programming period were adopted for an amount of € 31.5 million and nine for the 2000-2006 programming period for an amount of € 34.7 million.

Of the € 26.5 million of corrections accepted by the Member States € 6.7 million related to 1994-1999 and € 19.8 million to 2000-2006. These are implemented by deduction from payment claims or from the balance payable at closure.

Table 5 illustrates the amount of financial corrections by Member State and programming period.

Table 5: Cohesion Fund financial corrections in 2008 by period and country (in EUR)

Member State	Cohesion Fund		TOTAL
	Period 2000-2006	Period 1994-1999	
Greece	23,405,436	5,674,477	29,079,913
Spain	19,927,164	32,483,151	52,410,315
Ireland	-	-	-
Portugal	11,062,188	-	11,062,188
EU 4	63,259,764	38,157,628	92,552,416
Cyprus	-	-	-
Czech Republic	-	-	-
Estonia	125,073	-	125,073
Hungary	-	-	-
Latvia	-	-	-
Lithuania	65,833	-	65,833
Malta	-	-	-
Poland	123	-	123
Slovenia	-	-	-
Slovakia	-	-	-
EU 10	191,029	-	191,029
Bulgaria	6,156	-	6,156
Romania	-	-	-
EU 2	6,156	-	6,156
TOTAL	54,591,973	38,157,628	92,749,601

Management and Control systems

In the Directorate General's Annual Activity Report for 2008, for the functioning of the management and control systems (2000-2006), an unqualified opinion, signifying that there are no material deficiencies in key elements of the system, was given for the Cohesion Fund systems in seven Member States (Cyprus, Estonia, Hungary –

transport sector, Latvia, Malta, Portugal and Slovenia) corresponding to 15.45% of payments made in 2008 as a proportion of total payments for the Cohesion Fund.

For ten Member States, representing 84.55% of CF payments made in 2008, the opinion was qualified, signifying the existence of material deficiencies in key system elements. This concerned Bulgaria, the Czech Republic, Greece, Hungary (environment sector), Ireland, Lithuania, Poland, Romania, Slovakia and Spain. In all cases the impact of the deficiencies was judged to be moderate, except for the road sector in Bulgaria.

For the road sector in Bulgaria the opinion was qualified with the impact of the material deficiencies affecting key elements of the system being judged significant. Accordingly, a reservation was made for the road sector in Bulgaria in the Directorate General's Annual Activity report for 2008. The Commission suspended payments to the Bulgarian road sector projects between July 2008 and May 2009 for this reason.

4.2.1. Greece

In 2008, DG Regional Policy carried out two audit missions for the Cohesion Fund in Greece. For both audits a qualified opinion was given with possible financial implications after the contradictory procedure. As concerns audit work from previous years, three open audit missions carried out in 2007 were closed in 2008 or early 2009 without financial corrections. Fourteen winding up declarations for projects' closure were examined in 2008.

In 2008, one important financial correction decision was taken relating to systemic irregularities in the public procurement procedure for both closed projects and projects under implementation.

In the Annual Activity Report of 2008 a qualified opinion with moderate impact and no reservation was given to the Cohesion Fund in Greece as each project is audited by the national authorities (EDEL) at least once before closure and as the Commission examines the winding-up declarations before the closure of projects on an individual basis and any irregular expenditure can be identified and deducted at closure of each project.

4.2.2. Spain

No audits on Cohesion Fund were carried out by the Commission in Spain in 2008. As to the follow-up of previous missions, DG Regional Policy concluded the financial correction procedures for eleven projects during the year 2008 with a total corrected amount of € 52.4 million.

60 winding-up declarations for the closure of Spanish projects were analysed during the year and, as a result, irregular expenditure declared to the Commission were detected, mainly related to public procurement procedures and certain VAT eligibility issues.

In the Directorate General's Annual Activity Report for 2008 for the functioning of the management and control systems (2000-2006), a qualified opinion with moderate impact was given for the Cohesion Fund in Spain as a result of material deficiencies

affecting key elements of the systems. However, no reservation was proposed as the Directorate General concluded that it obtains reasonable assurance for payments and the financial risk to the Community budget is mitigated by the fact that the winding-up declarations are assessed before the closure of projects on an individual basis and any irregular expenditure can therefore be identified and deducted at closure of each project. Also, the maximum interim payments prior to closure are capped at 80% of the Community contribution.

4.2.3. Portugal

In 2008, no missions were carried out by DG Regional Policy in Portugal as regards Cohesion Fund. However, the European Court of Auditors audited one project in Portugal in the context of their DAS 2007 enquiry, with findings on public procurement issues.

As to the follow-up of previous missions, DG Regional Policy concluded the financial correction procedures for six projects and launched new financial correction procedures for two other projects in 2008. The financial corrections concluded for the six projects amounted to € 10 212 814, of which only € 720 731 was enforced through a Commission Decision and the remaining corrections were accepted and executed by the Portuguese authorities themselves. The audits done by DG Regional Policy in regard to five other projects were closed without financial corrections.

At the request of DG Regional Policy, the winding-up body carried out a specific enquiry in 2007 on the implementation of control procedures for the period from 1 January 2005 onwards. The conclusions of that enquiry revealed that the risks in respect of public procurement were mitigated as the national authorities implemented new control procedures following an action plan carried out in 2005. On the basis of that enquiry, together with the conclusions drawn from Commission audits and the analysis of national audit strategy, DG Regional Policy signed on 22 January 2008 a contract of confidence with "Inspecção-Geral de Finanças" (Portuguese winding-up body and audit authority) covering the Cohesion Fund and ERDF.

In 2008, DG Regional Policy analysed nine winding-up declarations for closure of Portuguese Cohesion Fund projects.

In the Directorate General's Annual Activity Report for 2008, for the functioning of the management and control systems (2000-2006), an unqualified opinion was given for the Cohesion Fund in Portugal.

4.2.4. Cyprus

One audit mission was carried out by DG Regional Policy in 2008 in Cyprus reviewing the work of the winding up body for ERDF and CF. There were no outstanding issues concerning CF from previous years' audits to follow-up in 2008 and no financial corrections were carried out in 2008. No projects were closed in 2008 in Cyprus.

Based on the positive results of the review of the winding up body, of the positive conclusions from other audit missions carried out in Cyprus, as well as of the desk work carried out, a contract of confidence for ERDF and Cohesion Fund was signed

between the Commission and the Cypriot Internal Audit Service (as the audit body in Cyprus) on 17 December.

In accordance with the above there was an unqualified opinion with no reservations for Cohesion Fund expenditure in Cyprus in the Directorate General's 2008 Annual Activity Report.

4.2.5. Czech Republic

In 2008 in the context of the Action Plan to strengthen the Commission supervisory role in the management of structural actions, the Commission services requested the Czech authorities to carry out an exercise of retrospective verifications of Cohesion Fund projects with the aim to determining the extent and potential systemic character of previously detected audit findings in the area of public procurement. The final report on this exercise was due in January 2009.

The Commission services carried out two audit missions for Cohesion Fund in the Czech Republic in 2008. The Commission services also closed one previous audit by opening a financial correction procedure for infringement of public procurement rules concerning a railway project. Eight winding-up declarations for closure of Czech projects were examined in 2008 by DG Regional Policy and as a result one financial correction was proposed on an environment project before closure.

In the Directorate General's Annual Activity Report for 2008, for the functioning of the management and control systems (2000-2006), an unqualified opinion was given for the Czech Republic as the winding-up declarations are assessed before the closure of projects on an individual basis and any irregular expenditure can therefore be identified and deducted at closure of each project.

4.2.6. Estonia

On the basis of audit work carried out in 2006 and 2007, a contract of confidence was signed in 2007 between the DG Regional Policy and Estonia covering the Cohesion Fund and ERDF.

No missions were carried out in Estonia in 2008. However, some follow-up work on an audit mission carried out in 2006 was done resulting in closure of all findings without financial correction. Additionally four winding-up declarations were examined in the context of closure of Estonian projects.

In accordance with the above there was an unqualified opinion with no reservations for Cohesion Fund expenditure in Estonia in the Directorate General's 2008 Annual Activity Report.

4.2.7. Hungary

The Directorate General's 2008 Annual Activity Report for the Cohesion Fund in Hungary contained an unqualified opinion for the transport sector and a qualified opinion for the environmental sector. The latter qualified opinion was linked to a

reservation originating from a significant public procurement-related finding² identified during the project audit of the Budapest Wastewater Treatment Plant in November 2007.

Considering financial impact of irregular procurement procedure, one audit mission was carried out by DG Regional policy in 2008 as an extension to audit work executed in 2007. Based on the work performed, it was concluded that the management and control systems function effectively, and that they are in compliance with Community legislation, in particular, with EU and national public procurement rules. A second audit mission carried out in Hungary in 2008 by DG Regional Policy focused on the review of the work performed by the winding-up body in the context of ERDF programmes and CF projects closure.

Three winding-up declarations related to closure of Cohesion Fund Technical Assistance projects, were examined in the course of 2008.

4.2.8. Latvia

DG Regional Policy did not carry out any Cohesion Fund audit missions in Latvia in 2008. However, findings from previous missions were followed up and during 2008 the Latvian authorities took corrective action, in particular in the field of public procurement procedures by issuing new guidelines and reviewing and correcting all non-compliant supplementary contracts.

One financial correction procedure was launched by the DG Regional Policy in 2008 for the project "Solid Waste Management in the Region of South-Latgale" due to irregularities detected in public procurement procedures.

The case by case assessment of closure declarations by DG Regional Policy and the actions undertaken by the Latvian Authorities to address the risks identified in the Cohesion Fund management and control systems were considered to provide adequate assurance that all irregularities will be detected and corrected before closure of projects. Accordingly, there was an unqualified opinion with no reservations for the Cohesion Fund in Latvia in the Directorate General's 2008 Annual Activity Report.

4.2.9. Lithuania

DG Regional Policy carried out one audit mission in Lithuania in 2008 on Cohesion Fund projects. The main findings related to cost increases, tendering issues and the IT monitoring system. DG Regional Policy and the Lithuanian winding-up body (NAO) are supervising closely the follow up of these issues.

All Cohesion Fund audits from previous years are closed, with one financial correction procedure of € 0.7 million launched in 2008 relating to public procurement issues. In addition, one complaint on a public procurement procedure concerning Lithuania was handled by DG Internal Market in 2008 concluding that the public procurement procedure in question was irregular. As the project linked to

² A financial correction of 25% on the contract concerned was accepted by the Member State in 2009.

the contract in question was co-financed by the Cohesion fund, the follow-up of this case, including possible financial corrections, will be done by DG Regional Policy.

Three winding-up declarations in the context of closure process of Lithuanian Cohesion Fund projects, were examined by DG Regional Policy in 2008.

In the Directorate General's 2008 Annual Activity Report a qualified opinion with moderate impact was given for the Cohesion Fund in Lithuania on the basis of the above material deficiencies affecting key elements of the systems in Lithuania. No reservation was proposed, as the DG is able to exercise a close management of each CF project and check in detail the risk areas at closure, and because the maximum interim payments prior to closure are capped at 80% of the Community contribution for CF projects.

4.2.10. Malta

No audit missions or financial correction procedures for Cohesion Fund were carried out in 2008 for Malta by DG Regional policy. One previous audit mission carried out in 2007 did not give rise to any significant findings.

Accordingly, there was an unqualified opinion with no reservations for the Cohesion Fund in Malta in the Directorate General's 2008 Annual Activity Report.

4.2.11. Poland

In 2007 and 2008 the Polish authorities undertook to implement a remedial action plan to ensure that all bodies in charge of carrying out public procurement checks apply financial corrections when irregularities are detected, and to revise their methodology for public procurement checks in order to ensure an adequate level of checking. The Action Plan was closed in March 2009 by DG Regional Policy.

In 2008, DG Regional Policy lifted the reservation given in its Annual Activity Report in 2007 for the Cohesion Fund in Poland as the systemic deficiencies in the area of public procurement had been identified during previous audit work and the Commission services are in a position to check during the assessment of individual winding-up declarations whether the ineligible expenditure resulting from these deficiencies have been identified and corrected by the Polish authorities.

No new audit missions were carried out by DG Regional Policy on Cohesion Fund projects in 2008. All previous systems and project audits have been closed. Most important systemic findings were followed up within the Action Plan for Poland which was closed in March 2009. The only missions remaining open are two public procurement audits with findings on discriminatory selection criteria, direct awarding of additional works/services, and modification of terms of contract after the contract award. The findings were accepted by the Polish authorities during the follow-up of the Action Plan, and the financial corrections will be finalised during 2009.

In 2008, DG Regional Policy examined five winding-up declarations for Polish projects.

4.2.12 Slovakia

Two audit missions concerning Cohesion Fund were carried out by DG Regional Policy in Slovakia in 2008: The first one was a follow-up audit to verify the implementation of previous recommendations and to audit selected projects. The second audit mission focused on verifying the quality of the retrospective review of public procurement procedures in the Cohesion Fund and ERDF projects, which was carried out by the Slovak Managing Authorities at Commission request.

In 2008, financial correction procedures were initiated for two Cohesion fund projects due to public procurement issues. One winding-up declaration and two annual control reports were examined in 2008. An annual audit coordination meeting between the Commission and the Slovak audit bodies was held in Brussels.

A qualified opinion with moderate impact was expressed on Cohesion Fund Slovakia in the Directorate General's 2008 Annual Activity Report. The main reason for the qualification was shortcomings detected in the management verifications in public procurement. The seriousness of the qualification was downgraded from 2007 and the reservation expressed in 2007 was lifted in 2008 due to the mitigating measures adopted by the Slovak authorities in 2008 (retrospective review of public procurement).

4.2.13 Slovenia

Following the positive results of audit work carried out in previous years, a contract of confidence was signed with Slovenia in February. No Cohesion Fund audit missions were carried out by DG Regional Policy in Slovenia in 2008. However, follow up work continued for previous missions resulting in the closure of one audit mission. No financial corrections procedures are ongoing or envisaged for the Cohesion Fund in Slovenia.

In 2008, other audit work included the examination of the annual control report under Article 12 of Regulation (EC) No 1386/2002 and several system audit reports from the Budget Supervision Office, and participation in the annual co-ordination of controls meeting with national audit body. Annual summary for 2008 confirmed the information available from other reports. Moreover, three winding up declarations submitted for the closure of three 2000-2006 projects were examined in 2008 with no major remarks.

Accordingly, there was an unqualified opinion with no reservations for Cohesion Fund expenditure in Slovenia in the Directorate General's 2008 Annual Activity Report.

4.3. Irregularities notified by the Member States

In 2008, the Member States communicated to the Commission, in accordance with Regulation (EC) No 1831/94, 140 notifications of irregularities involving a total affected amount of € 56,328,911 in respect of co-financed projects. Out of this amount, € 19,768,042 has been recovered, and the remaining amount is to be recovered. The Member States reporting the majority of cases are Spain, Portugal, Hungary and Greece (64, 21, 13 and 12 respectively). Spain reported more than 46%

of the total of the cases and 44% of the involved amount. However, it is to be pointed out that Ireland, with three notifications relating to the 1994-1999 period, stands on the second highest level in terms of amount involved, followed by Lithuania.

The number of notifications shows an increase, with a radical decrease of the involved amount, compared to the previous year. The main types of irregularities reported are ineligible expenditure, and infringements to public procurement rules. These two typologies cover almost 75% of all cases reported. However, the Lithuanian authorities reported two cases of "suspended fraud". The involved amount concerning both cases is yet to be calculated.

5. EVALUATION

The Commission and the Member States carry out appraisal and evaluation of all co-financed projects. The projects to be financed by the Fund are adopted by the Commission in agreement with the beneficiary Member States.

Each request for assistance is accompanied by a cost-benefit analysis (CBA) of the project. The CBA has to demonstrate that the socio-economic benefits in the medium term are proportionate to the financial resources mobilised. The Commission examines this CBA on the basis of the principles set out in the guide for cost-benefit analysis. The guide, first published in 2003, was updated in 2008 to incorporate the development of Community policies, financial instruments and the new regulatory framework under which major projects will be financed during the 2007-2013 programming period.

In 2008, the Commission continued to assist Member States through actions of capacity building aiming to improve the consistency of the ex-ante financial and economic analysis of the projects. As a result, the Guide rapidly achieved a wider circulation, both within civil servants in Member States and candidate countries as well as within the staff of financial institutions and consultants involved in the preparation and evaluation of major projects. A printed version of the Guide was therefore published, providing methodological guidance to project promoters in the Member States and candidate countries, while serving as a reference to Commission officials involved in the appraisal of major projects.

In addition, the Commission carries out ex-post evaluation on samples of projects co-financed by the Cohesion Fund. The last evaluation was published in 2005 and looked at a sample of 200 projects implemented over the 1993-2002 period. The next ex-post evaluation will be launched in the last quarter of 2009 and will look at a sample of both Cohesion Fund and ISPA projects implemented during the 2000-2006 period.

6. INFORMATION AND PUBLICITY

6.1. Information to/from the Member States

As indicated in the annual report for 2007, issues concerning the Cohesion Fund are, as from 1 January 2007, dealt within the Coordination Committee of the Funds (COCOF, according to Regulation (EC) No 1083/2006).

Apart from issues of common interest for ERDF and Cohesion Fund, some issues of specific interest for the Cohesion Fund were presented or discussed during the following meetings of the COCOF:

February: Revised Guidelines for the amendment of Cohesion Fund projects 2000-2006.

April: Guidelines on the closure of Cohesion Fund and Ex-ISPA projects 2000-2006, which were adopted by the Commission on 4 April (No (SEC(2008)415).

6.2. Commission measures on publicity and information

As regards the Commission measures on information and publicity, the focus in 2008 was on implementation of the publicity requirements for the 2007-2013 period. One of the biggest challenges was the examination of compatibility of the communication plans, as requested by Commission Regulation (EC No 1828/2006. Out of the 272 communication plans submitted to the Commission by managing authorities (communication plans could cover one or more Operational Programmes, and thus cover Cohesion Fund jointly with other funds), 212 were deemed compliant in 2008 (78%).

INFORM - a network of communication officers responsible for implementation of the information and publicity rules for ERDF and Cohesion Fund met for the first time in June. The second meeting took place in November. At each meeting around 130 communication officers exchanged experience and views on the practical aspects of their work. Both meetings provided opportunity for enhanced cooperation with Commission Representations, Europe Direct network, as well as with DG Employment, Social Affairs and Equal Opportunities.

DG Regional Policy published a "Review of EU Cohesion Policy Communication Plans 2007-2013 - Activities of national and regional managing authorities in the field of communication", which was carried out in the second half of 2008. The review, materials from the INFORM meetings, as well as various information and publicity tools prepared for both Cohesion Fund and ERDF, are available at a dedicated website³.

³ http://ec.europa.eu/regional_policy/country/commu/index_en.cfm?nmenu=1