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COVER NOTE

from:	Mr Vítor CALDEIRA, President of the European Court of Auditors
date of receipt:	25 May 2012
to:	Mr Nicolai WAMMEN, President of the Council of the European Union
Subject:	Special report No 6/2012: European Union assistance to the Turkish Cypriot Community

Sir,

I enclose a copy of Special report No 6/2012 "European Union assistance to the Turkish Cypriot Community" together with the Commission's replies.

The Special report, which is shortly to be published, was adopted by the Court at its meeting on 6 March 2012 and is accompanied by the replies from the Commission, which was notified of the preliminary findings on 19 December 2011.

(Complimentary close).

(s.) Vítor CALDEIRA

Encl.: Special report No 6/2012: European Union assistance to the Turkish Cypriot Community¹

¹ In English only. The other languages of this report are available on the European Court of Auditor's website: <http://eca.europa.eu/>.

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Special Report No 6/2012

(pursuant to Article 287(4), second subparagraph, TFEU)

European Union Assistance to the **Turkish Cypriot Community**

together with the Commission's replies

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EXECUTIVE SUMMARY

I. The Court of Auditors assessed whether the Commission is managing the instrument for financial support to the Turkish Cypriot community (hereafter referred to as TCc) in the northern part of Cyprus² effectively. Specifically, the Court examined whether the Commission drew up an assistance programme which reflected the instrument's objectives and put in place appropriate implementing arrangements and whether the individual projects are achieving their intended results.

II. The audit covered the period from the adoption of Council Regulation (EC) No 389/2006 in February 2006 to the third quarter of 2011. It included the examination of a sample of 34 contracts totalling approximately one third (97,5 million euro) of all budget allocations to the instrument from 2006-11.

III. Despite the difficult political context and a compressed timetable, the Commission managed to establish a programme which reflected the regulation's objectives. It was also able to quickly set up a programme management office and introduce suitable implementation mechanisms. The main weaknesses resulted from the programme support office not operating under more devolved procedures like EU delegations and from contracts for some key staff being limited to three years.

IV. The programme has assisted a great number of different beneficiaries across the TCc and some results have already been achieved. However, the planned construction of a seawater desalination plant, the programme's largest project (27,5 million euro), cannot be implemented which represents a significant setback for the programme. More generally, the sustainability of projects is often in doubt due to limited administrative and financial capacity of the TCc authorities and their delayed adoption of relevant 'laws'.

V. On the basis of the above observations the Court makes a set of recommendations to the Commission covering different possible scenarios based both on developments in the reunification process and the level of future EU assistance:

- If there is no settlement in the short term and it is decided that further significant funding should be provided to the TCc, the Commission should take a number of steps to strengthen its management of the assistance programme (see paragraph 64).
- If it is decided not to support a further large scale assistance programme, an action plan should be prepared to scale down or phase out the Commission Task Force's operations (see paragraph 65).
- If clear progress is made in the reunification process, the Commission should make early preparations for a programme to enable the whole country to benefit from EU funding following reunification (see paragraph 66).

² The phrase 'northern part of Cyprus' is a geographical term used to designate the areas of the Republic of Cyprus in which the Government of the Republic does not exercise effective control.

INTRODUCTION

Background

1. Cyprus became independent in 1960. The Treaty of Guarantee signed the same year by Greece, Turkey, the United Kingdom and the representatives of the Greek Cypriot and Turkish Cypriot communities intended to guarantee the basic provisions of the constitution and the territorial integrity and sovereignty of Cyprus. However, disagreements over the revision of the constitution soon surfaced and led to a political breakdown in 1963 and an upsurge in inter-communal violence. After United Nations (UN) Security Council Resolution 186 in March 1964, the UN Peacekeeping Force in Cyprus (UNFICYP) was established and is still in place with a current strength of approximately 1 000 troops.
2. The existing *de facto* division of Cyprus dates back to Turkey's military intervention in the northern part of the island in July 1974. This followed years of inter-communal struggles and a short-lived military coup by sections of the Cypriot National Guard led by Greek officers.
3. In the aftermath of the Turkish military intervention the UN Security Council expanded UNFICYP's mandate, which now includes supervision of the *de facto* cease fire and maintenance of a buffer zone along the 'green line' which marks out the northern and southern parts of the island. As a result of the 1974 events, the vast majority of Greek Cypriots and Turkish Cypriots live separately on the respective sides of the buffer zone. The resulting property issue has been one of the most difficult problems to solve as part of the ongoing efforts to reach a settlement (see paragraph 32).
4. The self-proclaimed 'Turkish Republic of Northern Cyprus' was declared on 15 November 1983 but is recognised only by Turkey. UN Security Council Resolution 541 (18 November 1983) states that the attempt to create the 'Turkish Republic of Northern Cyprus' was invalid. The UN recognises the

sovereignty of the Republic of Cyprus according to the terms of its independence in 1960.

5. At its meeting in Helsinki in December 1999, the European Council decided that a political settlement would not be a precondition for the accession of Cyprus to the European Union (EU), although it underlined that a settlement would facilitate the accession process. In December 2002, the European Council decided in Copenhagen that Cyprus would be admitted as a new EU Member State, while reiterating its preference for the accession of a unified Cyprus.

6. However, in an April 2004 referendum the Annan Settlement Plan was rejected by 76 % of the Greek Cypriots voting, while 65 % of Turkish Cypriots voting approved it. The Republic of Cyprus therefore joined the EU on 1 May 2004 with the island still *de facto* divided. While the whole island legally is part of the EU, the *acquis communautaire* is suspended in the northern part, an area over which the Republic of Cyprus does not exercise effective control. This constitutes a unique political, legal and diplomatic context.

7. A new round of UN-sponsored talks was launched in September 2008 and is still ongoing. The United Nations Secretary General and the leaders of the Greek Cypriot and Turkish Cypriot communities agreed to meet for a fifth time in January 2012.

EU financial assistance

8. Following the 2004 referendum the Council (General Affairs and External Relations), a week before the accession of the Republic of Cyprus to the EU, requested the Commission to submit a proposal for an aid programme. In its conclusions the Council stated:

“The Turkish Cypriot community has expressed their clear desire for a future within the European Union. The Council is determined to put an end to the isolation of the Turkish Cypriot community and to facilitate the reunification of

Cyprus by encouraging the economic development of the Turkish Cypriot community. The Council invited the Commission to bring forward comprehensive proposals to this end, with particular emphasis on the economic integration of the island and on improving contact between the two communities and with the EU.³

9. On 7 July 2004, the Commission proposed a package of two regulations: one for a financial support instrument to encourage the economic development of the Turkish Cypriot community and a 'direct trade' regulation. It proved, however, difficult for the Council to agree on the adoption of this package and the two regulations had to be decoupled⁴.

10. The Council Regulation for the instrument of financial support was eventually adopted on 27 February 2006⁵ with an initial allocation of 258,8 million euro. This was in fact the amount which had been earmarked for the Turkish Cypriot community for the implementation of EU policies in Cyprus if a political settlement was reached before accession. Smaller additional amounts totalling 33,5 million euro were allocated over the period 2009 to 2011. The funding allocation to the instrument's objectives is set out in the **Table**. A detailed list of the projects funded under each objective is given in **Annex I**. As at 30 September 2011 some 69 % of the total contracted amount for the instrument had been paid by the Commission.

³ Council Conclusions on Cyprus, DG E I 8907/04. Brussels: Council of the European Union, 27.4.2004.

⁴ No progress has been made for the adoption of the 'direct trade' regulation. The movement of persons, goods and services from the northern to the southern part of Cyprus is regulated by the 'Green Line Regulation' which entered into force on 1.5.2004 (Council Regulation (EC) No 866/2004 of 29 April 2004 on a regime under Article 2 of Protocol No 10 of the Act of Accession (OJ L 161, 30.4.2004, p. 128).

⁵ Council Regulation (EC) No 389/2006 of 27 February 2006 establishing an instrument of financial support for encouraging the economic development of the Turkish Cypriot community and amending Council Regulation (EC) No 2667/2000

Table – Financial allocations by objective (as at 30 September 2011)

(Million euro)	Planned	% of total planned	Contracted	Paid	% paid of total contracted
Objective 1 Developing and restructuring of infrastructure	129,25	44,2 %	135,02	76,49	56,6 %
Objective 2 Promoting social and economic development	84,65	29,0 %	64,87	49,41	76,2 %
Objective 3 Fostering reconciliation, confidence building measures and support to civil society	23,50	8,0 %	19,90	17,61	88,5 %
Objective 4 Bringing the Turkish Cypriot community closer to the EU	12,50	4,3 %	8,62	7,49	87,0 %
Objective 5¹ Preparing the Turkish Cypriot community to introduce and implement the <i>acquis communautaire</i> and unallocated TA and Programme Reserve Facility	21,35	7,3 %	15,69	14,15	90,2 %
Sub total Operational part	271,25	92,8 %	244,10	165,15	67,7 %
Management (Staff and Missions), Logistics	21,05	7,2 %	15,30	13,64	89,1 %
Total	292,30	100,0 %	259,40	178,79	68,9 %

¹ Objective 5¹ here includes unallocated technical assistance and a programme reserve facility to which 1,74 million euro has been allocated.

AUDIT SCOPE AND APPROACH

11. The audit addressed the overall question:

“Is the Commission managing the EU instrument of financial support to the Turkish Cypriot community effectively?”

This question focused on whether:

of 5 December 2000 on the European Agency for Reconstruction (OJ L 65, 7.3.2006, p. 5).

- (a) the Commission had been able to draw up an assistance programme which reflected the instrument's objectives and had put appropriate arrangements in place for implementing it;
- (b) the individual projects financed in the framework of the programme are achieving their intended results and whether they are likely to be sustainable.

The audit did not seek to assess whether the programme is contributing to the instrument's political objective of reunification.

12. The audit gathered evidence for its assessment through documentary review, interviews and three on-the-spot audit visits to Cyprus in 2011. In particular, the audit examined a sample of 34 contracts selected from nine of the main projects out of 24 projects funded through the programme and covering all five of the instrument's policy objectives. The contracts audited totalled 97,5 million euro or one third of the total budget allocations to the instrument (292,3 million euro). The complete list of contracts covered by the audit is given in **Annex II**.

OBSERVATIONS

The Commission faced significant constraints in the setting up and implementation of the programme

13. The audit assessed whether the Commission had effectively managed the setting up of the programme. To do this it examined whether it had established clear, logical and timely priorities and actions focused on the main objectives of the instrument and based on the needs of the TCc. It also examined whether the Commission, in setting up the specific implementation structures and procedures for this programme, had taken account of previous Commission experience, had evaluated different possible options, and had ensured it had adequate expertise to implement the programme.

Interventions reflected the programme’s objectives despite the wide range of sectors to be covered, the regulation’s delayed adoption, and the absence of a multi-annual perspective

14. The overall objective of the assistance financed by the instrument according to Article 1 of the Council Regulation is to facilitate the reunification of Cyprus. This is to be done “by encouraging the economic development of the Turkish Cypriot community with particular emphasis on the economic integration of the island, on improving contacts between the two communities and with the EU, and on preparation for the *acquis communautaire*”. Article 2 of the regulation lists a wide range of more specific objectives which the assistance is required to cover (see **Box 1**). This broad formulation of the objectives meant that assistance had to be funded across a wide range of sectors which represented a considerable implementation challenge for the Commission, including in relation to allocating the necessary human resources. An approach focused on a more limited number of objectives would have allowed the Commission to better target the assistance.

Box 1 – Objectives of Council Regulation (EC) No 389/2006

Article 1

Overall Objectives and Beneficiaries

The Community shall provide assistance to facilitate the reunification of Cyprus by encouraging the economic development of the Turkish Cypriot community with particular emphasis on the economic integration of the island, on improving the contacts between the two communities and with the EU, and on preparation for the *acquis communautaire*.

Article 2

Objectives

Assistance shall be used to support inter alia:

- (a) the promotion of social and economic development including restructuring, in particular concerning rural development, human resources development and regional development,
- (b) the development and restructuring of infrastructure, in particular in the areas of energy and transport, the environment, telecommunications and water supply,
- (c) reconciliation, confidence building measures, and support to civil society,
- (d) bringing the Turkish Cypriot community closer to the Union, through inter alia information on the European Union's political and legal order, promotion of people to people contacts and Community scholarships,
- (e) preparation of legal texts aligned with the *acquis communautaire* for the purpose of these being immediately applicable upon the entry into force of a comprehensive settlement of the Cyprus problem,
- (f) preparation for the implementation of the *acquis communautaire* in view of the withdrawal of its suspension in accordance with Article 1 of Protocol No 10 of the Act of Accession.

15. All the audited interventions contributed to varying degrees to the regulation's objectives in Article 2. The focus on infrastructure and economic development of the TCc was intended to ensure that the level of development of the TCc economy compared to that of the Greek Cypriot community would not be an obstacle to a political settlement. The largest financial allocations were made to the water and sanitation and rural development sectors. This reflected the priority needs, the absorption capacity in the different sectors, and the results of the specific feasibility studies carried out (see **Table** and **Annex I**).

16. The 'reconciliation and confidence-building' objective also represented an important complementary means of supporting the overarching reunification objective. However, the actual amount of the financing decision of December 2006 was 35 % lower than the initial proposal of July 2004. This shift reflected the outcome of consultations with TCc leaders who considered the TCc's infrastructure and economic development to be the instrument's primary objectives.

17. The Commission in its assistance programmes generally makes widespread use of capacity building support to accompany its projects in order to strengthen national administrations and improve the sustainability of projects funded. However, the Commission's scope for developing such approaches in this programme has been significantly reduced because the TCc administration is not officially recognised internationally. Thus, for example, the Commission has not been able to use twinning contracts which are its preferred capacity building instrument in countries preparing to adopt the *acquis communautaire*⁶. In cases where the Commission used technical assistance from consultancy companies for capacity building, the extent to which such technical assistance

⁶ Twinning contracts involves experts from Member States administrations working alongside civil servants in the beneficiary countries to transfer know-how.

could work together with the TCc authorities was also limited by the political circumstances (see also paragraph 45).

18. The long time required for the adoption of the Council Regulation (see paragraph 9) meant that the financing decisions for the initial allocation of 259 million euro had to be developed and approved in the course of just one year. A series of preparatory activities which had been planned for 2004-05 could not take place and the Commission had to finance important feasibility studies through a budget of only 2 million euro made available under a 2003 Special Aid Package for the northern part of Cyprus⁷. The time pressure during the project preparation phase was one reason for the major problems encountered in the water desalination plant project (see paragraphs 38 to 40).

19. The delayed approval also had a negative impact on the preparation of contracts to implement the projects, in particular the technical specifications for tenders, which instead of being spread over the four and half years between July 2004 and December 2009, had to be completed in three years before the contracting deadline expired. This posed a particular challenge for infrastructure projects in the water sector (see **Box 2** (c)). As a result, of the total allocations to the contracts covered by the audit, some 62 % were only contracted in 2009, while as many as 44 % were not contracted until December 2009, the month that the deadline expired.

20. Due to the delayed adoption of the regulation it was not possible for the Commission to take advantage of the envisaged multi-annual programming framework for 2004-06. Moreover, funding since 2006 has been made available only on an ad hoc and limited basis (see paragraph 10).

21. This absence of a multi-annual programming framework has not been conducive to effective management of the programme. In particular, it has meant that the Commission has not been able to plan ahead and sequence its

⁷ See footnote 1.

interventions for maximum impact and to move funding between different sectors of intervention according to how well they are performing and lessons learnt. The assistance to the telecommunications sector (see paragraph 35) and to the scholarships programmes (see paragraph 53) are two areas which have experienced particular difficulties in this regard. The lack of a multi-annual perspective also makes human resource management more difficult (see paragraph 27).

The effectiveness of the Commission's local support office has been undermined by several factors

22. The Commission faced a major challenge in finding a suitable structure for implementing the programme. While EU funding in Member States is normally implemented through national bodies, this was not possible for this programme given that the Republic of Cyprus does not exercise effective control over the northern part of Cyprus. At the same time, however, it was also not possible to set up an EU delegation to implement the assistance because delegations can only be established outside the EU and the whole island is legally part of the EU (see paragraph 6). It was originally foreseen in the regulation that the assistance would be implemented using the European Agency for Reconstruction (EAR), through which the Commission had implemented much of its assistance in the Western Balkans since 2000, but a decision to close the EAR meant that this was also not an option⁸.

23. Faced with this challenge the Commission drew on its wide experience to identify the most appropriate alternative institutional set-up. The model chosen was a headquarters-based task force with a local programme support office - the European Union Programme Support Office (hereafter EUPSO) - in the

⁸ Council Regulation (EC) No 1756/2006 of 28 November 2006 amending Regulation (EC) No 2667/2000 on the European Agency for Reconstruction (OJ L 332, 30.11.2006, p. 18). In a December 2005 report to the Council and the Parliament, the Commission proposed to discontinue the European Agency for Reconstruction, but nevertheless to extend its existence until 31.12.2008.

northern part of Cyprus. This was inspired by the technical assistance offices used by the Commission in the West Bank and took into account the costs and benefits of different approaches as well as the political context⁹. The location of EUPSO in the northern part of Cyprus enabled the assistance programme to monitor implementation more closely and better respond to the needs of the project beneficiaries.

24. The Commission was able to quickly establish the EUPSO through a service contract signed in December 2006 with GTZ¹⁰. This contractor was already to provide logistical support for technical assistance in the northern part of Cyprus under an existing agreement¹¹.

25. Nevertheless EUPSO's management of the programme has been constrained by the fact that it has not been able to operate in the same way as EU delegations which typically manage EU assistance programmes. In the absence of a head of delegation, all key decisions have to be referred back to Commission headquarters. This also applies to tendering, contracting and payment procedures as they have not been devolved to EUPSO in the way that they are in EU delegations and which slows down operations. Moreover, within DG Enlargement four different units are involved in authorising contracts and

⁹ The Task Force is led by a Head of Unit in the Commission's Directorate-General for Enlargement. The EUPSO is under a Programme Officer who reports to this Head of Unit. The Task Force consists of 8 officials and 26 contract staff, of whom 2 and 20 respectively are on long term mission in EUPSO. They are assisted by 12 support staff from GTZ (see paragraph 24).

¹⁰ GTZ (*Gesellschaft für Technische Zusammenarbeit*) was renamed GIZ (*Gesellschaft für Internationale Zusammenarbeit*) on 1 January 2011. It is a private contractor but brings together expertise from German government agencies.

¹¹ This was for the EU's Technical Assistance and Information Exchange Instrument (TAIEX). TAIEX delivers public short-term technical assistance and expertise, helping users to understand and draft EU-compliant legislation. Organisationally, it is part of DG Enlargement and physically located in Commission headquarters. TAIEX is supporting the TCc to introduce and implement the *acquis communautaire* through a 13,7 million euro TA facility funded by the instrument (see [***Annex I***](#)).

payments. A 2009 evaluation of the programme also highlighted the lengthy verification procedures resulting from the centralised nature of the approval process.

26. EUPSO, unlike EU delegations, does not have its own press and communication section and therefore cannot issue its own press releases. Instead, EUPSO consults with the EC Representation in the Republic of Cyprus, which is located in the part of Nicosia over which the Republic of Cyprus exercise effective control, on all material produced for publication by the EU projects. While there are potential benefits in this arrangement given the politically sensitive context, there is no detailed operational agreement on the procedures for such consultations and delays of up to two months have been encountered in obtaining the EC Representation's clearance of documents (see also paragraph 55).

27. A further constraint faced by EUPSO is that, according to the Staff Regulations¹² of the European Union, headquarters-based contract agents can only be employed for a maximum of three years. This contrasts with the five year contract duration, sometimes with the possibility of renewal, for contract agents in delegations. As a result of this shorter contract duration, the Task Force has lost capable and experienced staff even when the projects they managed were not yet completed. Moreover, EUPSO currently has considerable difficulties attracting staff with the appropriate profile to replace them, as the Commission can only offer one-year contracts owing to the uncertainties over the future financing of the instrument (see also paragraph 20).

¹² Staff Regulations of Officials and Conditions of Employment of Other Servants of the European Union.

Programme implementation procedures not always effective

28. The Commission has taken appropriate steps to evaluate the most suitable implementation methods for individual projects. As it cannot enter into financing agreements with the TCc authorities because they are not officially recognised by the international community, the Commission has primarily implemented the assistance by entering into contracts directly and acting as the sole contracting authority. In addition, the Commission jointly managed some interventions with the United Nations Development Programme (UNDP) and this approach has proved appropriate for launching the EU assistance because it allowed it to build on previous UN activities. There is nevertheless a need to review whether these initial start-up advantages are still relevant given the experience the Commission has now built up before funding new EU interventions through the UN.

29. The monitoring arrangements put in place by the Commission have generally been adequate. EUPSO task managers and heads of section followed up and took corrective action with partners and contractors for the projects covered by the audit. EUPSO was supported where necessary by programme management units and technical assistance experts. Its cooperation in the area of monitoring for projects implemented through joint management with the UNDP has, however, posed problems. The audit found significant weaknesses in the contribution agreements with the UNDP for local and urban infrastructure, the Joint Committee of Missing Persons and demining operations where performance indicators were often not appropriate or not reported on consistently.

30. The Commission recognised from the outset that providing assistance to the TCc involved considerable financial and operational risks. An evaluation carried out in 2009 identified the most significant risks to the programme's relevance, efficiency, effectiveness, impact and sustainability for each of the instrument's objectives.

31. This evaluation has provided a sound basis for the Task Force's risk management and the implementation of an assurance strategy. The Commission has taken several measures to mitigate the need for corrective controls and to reduce exposure to additional demands or penalties from contracting parties. There remains a post-project risk related to the way in which liabilities connected with the ownership and operations of infrastructure investments are transferred to beneficiaries that are not officially recognised¹³.

32. A particular risk relates to the fact that an estimated 78 % of privately owned land in the northern part of Cyprus legally belongs to Greek Cypriots¹⁴, whose consent was required for EU-funded infrastructure investments on their land. The Commission has established procedures to verify property ownership in cooperation with the Department of Lands and Surveys of the Republic of Cyprus. While there were initially legal challenges to this process and significant delays, processing times have since been reduced.

33. The Commission, despite considerable efforts, did not effectively manage the implementation risks for the 27,5 million euro contract for the construction of a seawater desalination plant in Sirianokhori/Kumköy (see **Box 2**).

Box 2 – Management of Implementation Risks:

The Construction of a Seawater Desalination Plant

(a) The Commission was aware of the risk that if a company with Greek Cypriot workers won a tender under the assistance programme, they might have difficulties performing the contract because of potential restrictions on their access rights to the northern part of Cyprus. This risk materialised for the largest contract to be financed under the programme, the Sirianokhori/Kumköy seawater desalination plant.

¹³ An observation made by DG Enlargement's Internal Audit Capability.

¹⁴ COM(2007) 536 final of 18 September 2007: Annual Report 2006-2007 on the implementation of Community assistance under Council Regulation (EC) No 389/2006 establishing an instrument of financial support for encouraging the economic development of the Turkish Cypriot community.

(b) In the procurement notice for the works contract for the seawater desalination plant it is stated that the tenderer must provide a performance guarantee for the completion of the contract of 10 % of the contract value no later than 30 days after receiving the signed contract or else the contract becomes void. Yet, the contractor never provided it. In accordance with the procurement notice, the Commission should therefore have terminated the contract already on 17 January 2010, in which case the 27,5 million euro would have been de-committed.

(c) By contracting the works at the latest possible moment (the contracting deadline expired on 18 December 2009) the Commission also missed an opportunity to offer the contract to another tenderer. The procurement notice states that “if the selected tenderer fails to provide such a guarantee within this period, the contract will be void and a new contract may be drawn up and sent to the tenderer which has submitted the next cheapest compliant tender”. As the contracting deadline had expired, this was no longer an option.

(d) The Commission only started the high-level dialogue with the TCc political leaders in June 2010, seven months after the contract was signed in December 2009. While the TCc leader responded on 17 June 2010, expressing his political commitment to the project, access restrictions were only partially removed in August 2010. If the Commission had started the dialogue already in December 2009, this would have allowed more time to tackle the access issue.

(e) As a mitigating measure, the Commission introduced an addendum to the contract in June 2010, which would legally enable it to cancel the contract without penalties if it could not obtain assurances from the beneficiary concerning the contractor’s access rights. The Commission subsequently terminated the contract on 22 December 2011.

Sustainability of projects at risk despite some results

34. The Court audited a sample of contracts (see paragraph 12 and ***Annex II***) covering the instrument’s five objectives to assess whether they were achieving their intended deliverables and results and whether the results achieved are likely to be sustainable.

Objective 1: Development and restructuring of infrastructure

Telecommunications sector

35. The objective of EU support to the development and restructuring of the telecommunications infrastructure is to eventually bring the telecommunications sector in the northern part of Cyprus into line with EU standards in accordance with the *acquis communautaire*. The support is intended to provide a network where everyone can have access to modern telecommunication services, and which can easily be interconnected with the telecommunications network in the areas under the effective control of the Government of the Republic of Cyprus. Although behind schedule most of the equipment had been delivered by 30 June 2011. The accompanying technical assistance contract was facing significant delays, mainly because TCc 'laws and regulations' had not been adopted according to the planned schedule.

36. As for other sectors (see below), in the absence of financing agreements, the Commission has implemented the programme without an obligation for the beneficiary to implement the necessary reform actions before the signing of contracts for the supply of equipment. There is therefore a risk of sector reforms not being implemented, despite the programme's considerable investment in equipment. Initial announcements from the TCc leadership in May 2011 about restructuring the sector were met by strike action and demonstrations by workers at the 'TCc Telecommunications Office'.

37. Based on the experience of reforms of the telecommunications sector in other countries, including EU Member States, it can also be questioned whether 18 months was a realistic timeframe for this project. In addition, the financial sustainability of the 'TCc Telecommunication Office' as a service provider is undermined by the TCc central administration's management of the Office's finances.

Water sector

38. The construction of the seawater desalination plant at Sirianokhori/Kumköy is not only the main project in the water sector but also the largest intervention funded under the instrument, amounting to approximately 10 % of total contracted funding. The plant was intended to provide 23 000 m³ of clean drinking water per day covering the needs of an estimated 100 000 people. The design of the plant changed considerably during the project formulation process. The original proposal had been to build a plant to treat brackish groundwater but this approach was dropped because of concerns over compliance with the Water Framework Directive.

39. Despite its importance, very limited progress was made on the implementation of the contract, mainly due to the Greek Cypriot workers of one of the consortium's contractors being denied access to the site by the Turkish armed forces and the unresolved issue of the performance guarantee (see **Box 2**). According to the contract conditions, the Commission, as contracting authority, is responsible for providing access to the construction site but in practice this is outside its control.

40. The failure to implement this project represents a significant setback for the overall assistance programme. Water supply is becoming an increasingly critical issue for the island following a 40 % decrease in the mean annual rainfall in the past 30 years. Moreover, as one of the purposes of the project was to stop the ecologically unsustainable use of groundwater reserves, the cancellation of the project means that this serious environmental issue will not be addressed. The aquifer is under increasing threat from saline intrusion due to over-pumping and pollution from human and agricultural activities.

41. Two smaller water infrastructure projects have been more successful.

(a) An EU-funded contract, which represents 50 % of a wider project to renew the water distribution network in Nicosia, has renovated 87 km of the network in the north of Nicosia. However, the Commission did not establish

any indicator to assess the effectiveness of the project in terms, for example, of the reduction in leakages or annual repair costs.

- (b) The construction of the new Mia Milia/Haspolat Waste Water Treatment Plant (WWTP) aims to modernise wastewater treatment in the whole of Nicosia and the surrounding area. Due to the existing plant's bi-communal organisation, the project also supports reconciliation and confidence building. The builder of the WWTP is contracted to maintain and operate the plant for ten years after handover to ensure that capacity needs will continue to be met. However, the 'joint entity' to be formed by the two communities to manage and supervise this contract has still not been set up, which poses a risk to the project's sustainability.

42. Equipment for water sampling, analysis and laboratory information management has also been funded to provide additional capacity to carry out water quality analysis for all drinking water and waste water services in the northern part of Cyprus in accordance with the relevant EU directives. Although all the equipment was supplied as envisaged, it is not clear whether the project objectives will be achieved as the laboratory is not currently performing according to EU standards. While additional training of beneficiary staff was planned under a capacity building support contract to help ensure the continued use of the supplied equipment, it was not clear at the time of the audit when this training would be provided and if the necessary human resources would be allocated.

Objective 2: Promotion of social and economic development

Rural development sector

43. The expected results of the rural development sector programme included the preparation of a rural development plan, increased administrative capacity to programme and implement an EU-aligned policy, the implementation of grant schemes for on-farm investments and farm diversification in line with these new policies, and the improvement of village conditions.

44. Both a rural development plan and local development strategies of the kind used in the EU-Leader programme have been established. More than 200 individual farmers or entrepreneurs have benefited from a grant to enable them to upgrade their operating facilities and move closer to EU standards. In addition, nearly 40 community development grants have been made to local bodies and nongovernmental organisations (NGOs). Grant beneficiaries have received Commission-funded technical assistance support during the preparation and implementation of their projects and through the grant schemes have learnt modern bookkeeping, procurement and monitoring practices.

45. Nevertheless, the capacities of the local administrations and the final beneficiaries continue to need strengthening. The transfer of know-how from the technical assistance provided to the TCc authorities responsible for rural development has been hindered by the fact that the technical assistance does not work in the offices of the TCc authorities because of the political situation. At the same time ownership of the new Rural Development Plan, and, in particular, of the local development strategies which are intended for use by Member States in the framework of the EU Leader programme, is still weak. Sustainability is therefore unlikely to be achieved without additional support in the coming years. While further EU interventions are indeed being developed they now face competition from Turkish funding in the sector but direct coordination with Turkey is not possible in the current circumstances.

Local and urban infrastructure

46. EU support to modernise local and urban infrastructure is intended to help revitalise the northern part of Cyprus, including through the opening of new crossing points on the Green Line. Approximately 40 individual interventions have been financed through the UNDP under the two phases of the programme, including some high profile ones with significant impact such as the opening of two key crossing points (Ledra Street in Nicosia and Kato Pyrgos and Karavostasi - also known as Limnitis/Yeşilirmak) and the

restoration of the Bedestan, a major cultural heritage and tourist site in the north of Nicosia (see **Box 3**). Most of the individual actions have experienced delays although, in many cases, these delays have been linked to political difficulties and problems with property checks, which are largely out of the hands of the Commission and the UNDP.

47. Sustainability of the interventions is potentially undermined by the limited participation of the Turkish Cypriot community. There is no formal mechanism at project level where the TCc is represented, including in the project steering committee. At the level of the interventions, while the UNDP has cooperated closely with the local bodies at municipal level to involve them in project management, the UNDP remains the only contractor which means that these local administrations have not gained experience as contracting authorities. The issue of sustainability is not explicitly addressed in the UNDP reports with the exception of the Bedestan project (see **Box 3**).

Box 3 – Results: Upgrading of Local and Urban Infrastructure

Opening of crossing points

According to Article 2 of the Green Line Regulation, the line shall be crossed only at crossing points authorised by the competent authorities of the Republic of Cyprus. Today there are seven such crossing points, two of which, Ledra Street and Kato Pyrgos and Karavostasi (also known as Limnitis/Yeşilirmak), were opened in the framework of the project in April 2008 and October 2010 respectively.

The opening of new crossing points facilitates contacts between the two communities and promotes mutual understanding. A total of 1,6 million crossings were registered during the latest eight month reporting period: 26 % by Greek Cypriots from government-controlled areas to the northern part of Cyprus, 46 % by Turkish Cypriots

from the northern part of Cyprus to the government-controlled areas, and 28 % by EU citizens other than Cypriots and nationals of non-EU countries¹⁵.

Restoration of the Bedestan

The Bedestan was initially built as a Byzantine Church but was transformed into a closed market in the 16th century. By the 1930s, the building had fallen into disuse. When the EU-funded project started, it was in very poor condition, with a collapsed roof and various other structural damage. The works were completed in two phases: structural work between 2004 and 2006, and conservation and restoration work between 2005 and 2009.

In November 2009, the Bedestan was reopened to the public as a cultural centre and the inauguration ceremony was attended by representatives from both communities. The project was awarded the European Union Prize for Cultural Heritage/Europa Nostra Award in the research category.

Objective 3: Fostering of reconciliation, confidence building measures and support to civil society

48. Support has been provided to the Joint Committee on Missing Persons to try to bring closure in relation to this painful aspect of the history of Cyprus and thereby contribute to the process of reconciliation between the Greek Cypriot and the Turkish Cypriot communities. During the period covered by the first 1,5 million euro agreement (March 2007 to May 2009), 155 remains out of an estimated 1 958 missing persons were identified and returned to their families. Funds for future activities will continue to depend on the availability of funding from donors of which the EU is the most significant. At this stage no clear end goal or exit strategy has been formulated for the support to the Joint Committee on Missing Persons.

¹⁵ COM(2011) 284 final of 30 May 2011: Seventh Report on the implementation of Council Regulation (EC) No 866/2004 of 29 April 2004 and the situation resulting from its application covering the period May 2010 until December 2010.

49. The Commission also used the instrument to finance seminars organised by the Council of Europe Academy of Political Studies to give both Turkish Cypriot and Greek Cypriot participants a better insight into some of the common challenges which the island will be facing in the future. These seminars have contributed to better integrating Turkish Cypriot leaders although they have not always been well attended. The Commission has not taken any specific action to ensure the sustainability of the 'European Forum Cyprus', an alumni network for participants in these seminars.

50. 'Civil Society in Action' and 'Civil Society Support Team' programmes were launched with the aim of strengthening civil society organisations and the development of a civil society culture in the TCc. Both programmes have been able to build capacity but further support is required to strengthen operational and financial management capacity in Turkish Cypriot civil society organisations.

51. EU assistance has made a major contribution to demining in Cyprus. Almost all minefields in the buffer zone have now been cleared and since 2007 the EU has financed 6,5 million out of a total of 9 million euro invested in this effort. Among the benefits of the demining have been the facilitation of trade and population movement as a result of the opening of new crossing points (see **Box 3**). It has also helped confidence building through the cooperation between the Turkish and the Republic of Cyprus armed forces during the demining process.

Objective 4: Bringing the Turkish Cypriot community closer to the EU

52. The EU scholarship programme is one of the areas of EU assistance best known and most valued by the TCc. It has played a useful part in reducing the

isolation of the TCc by enabling 400 students and teachers to live and study in another Member State for one year¹⁶.

53. However, the programme's effectiveness and sustainability are hindered by the lack of a multi-annual perspective. The timing of the call for proposals is determined not by operational needs but by when Commission financing decisions are taken. The fact that there is no guarantee that the programme will continue from one year to another means that potential applicants cannot plan ahead (in particular those who cannot consider spending one year abroad without a grant).

54. It is not possible to assess the extent to which the overall objective of the project has been met because an ex-post survey among the individual beneficiaries has not yet been carried out. The contracting for the latest call concerning academic year 2011/12 has encountered serious delays, due mainly to a temporary shortage of staff in EUPSO (see paragraph 27). The Commission has not been able to sign any contract before the end of August 2011, just before the start of the academic year.

55. The European Union political and legal order information project ('InfoPoint') aims to bring the TCc closer to the EU through information activities and by improving understanding of the EU and of efforts towards a settlement and reunification. The project has already achieved some significant results, including the creation of the open access 'InfoPoint' office and a website¹⁷ in English and Turkish. Nevertheless diverging views between the EC Representation in Nicosia and the Task Force on a number of subjects in the framework of the project steering committee have led to the postponement of decisions and subsequent implementation delays. Thus, for example, the

¹⁶ This corresponds to approximately 1 out of 450 people living in the northern part of Cyprus.

¹⁷ See European Union Infopoint Nicosia, <http://www.abbilqi.eu>.

launch of the project's website was delayed by 16 months because of such problems.

Objective 5: Preparation for the *acquis communautaire*

56. The Commission has also funded projects to prepare for the *acquis communautaire*. The Court examined one of the largest of these projects for air quality monitoring. Despite problems encountered (see **Box 4**), which are also illustrative of challenges faced by other projects, both the technical assistance and all the equipment were delivered.

Box 4 – Implementation problems in the Air Quality Monitoring project

The final report by the technical assistance for the air quality monitoring project addressed the following implementation problems, which pose a risk to the project's results and their sustainability:

- (a) the start of the project was delayed four months after contract signature while waiting for the installation of four new air quality monitoring stations under the first of two supply contracts;
- (b) two other EU-funded technical assistance projects were working with the TCc 'Environmental Protection Department' (EPD) at the same time, which meant close coordination was necessary to avoid having four experts simultaneously trying to work with just two 'EDP' staff. However, this situation did arise for a few weeks;
- (c) fewer individuals than planned took part in the training due to the 'EPD's' budget constraints.

57. By including 12 months of 'after sales service' in the supplies contract the Commission has made an effort to address the project's sustainability. The local authorities' decision to engage the technical assistance contractor for continued operational and maintenance support also represents an attempt to ensure sustainability. A new 'environmental law' which complies with EU legislation has been adopted and the TCc beneficiary has developed a concept paper which sets out the budgetary and staff implications of implementing the

'law'. Nevertheless the overall sustainability is at risk due to the severe budget constraints faced by the TCc 'Environmental Protection Department'.

CONCLUSIONS AND RECOMMENDATIONS

Conclusions

58. The Commission succeeded in developing a programme where the objectives of the instrument were reflected in the interventions funded and largely appropriate implementing arrangements were put in place. The programme has already achieved some positive results but their sustainability is often in doubt, particularly given the uncertainty over future EU funding.

59. The Commission had to manage the difficult political context and the challenges posed by the broad formulation of the regulation's objectives, its late adoption and uncertain timeframe. Despite this, it has been able to develop a programme which addresses and appropriately prioritises all sectors referred to in the regulation's objectives. It also found a way in the face of significant constraints to quickly set up a programme management office in the northern part of Cyprus and use largely suitable implementation methods and risk mitigation measures. The main weaknesses in the management of the programme resulted from the local support office not operating under more devolved procedures in the same way as EU delegations and from the staff contracts being too short for them to manage the projects financed from start to finish. In addition, monitoring in the framework of joint management with the UN was not sufficient.

60. The programme has assisted many different beneficiaries across the TCc, including farmers, students and those using the new crossing points, and some important results have already been achieved. However, it has not been possible to implement the single largest project, the construction of a seawater desalination plant (27,5 million euro). This represents a significant setback for the programme and may also have serious environmental consequences. More generally, the sustainability of projects is often in doubt due to the limited

administrative capacity, the delayed adoption of relevant 'laws and regulations' and the uncertainties over future funding on the part of the TCc authorities.

61. At the time of the audit it was still unclear whether or not significant further funding for the EU assistance programme would be made available. This uncertainty makes the programme management more difficult and has a negative impact on its effectiveness and sustainability.

62. Despite the efforts of the EU in setting up and implementing the assistance to the TCc, the ultimate objective of the instrument, the reunification of Cyprus, only can be achieved if the two communities involved have the political will to do so.

Recommendations

63. The specific recommendations on the Commission's management of EU assistance to the Turkish Cypriot community necessarily depend on developments in the reunification negotiations and EU policy in this regard. The recommendations seek to take into account different possible scenarios.

64. In the current situation, where a settlement for the reunification of Cyprus has not been reached and if it is decided that a further EU assistance programme should be funded, the Commission should implement the following measures:

- (a) put in place a mechanism with a multi-annual perspective in order to ensure better planning, implementation and sustainability;
- (b) identify ways to ensure appropriate flexibility in the length of employment of staff working for the Task Force;
- (c) devolve management from Commission headquarters to EUPSO where this will increase the efficiency of the programme;

- (d) develop formal procedures to ensure better coordination between the EC Representation in Nicosia and the Task Force in order to make information from EUPSO and the projects more readily available to the public;
- (e) better define future contribution agreements with partner organisations, notably the UNDP, in order to ensure proper financial and operational reporting, including more relevant and up-to-date performance indicators;
- (f) take into account not only new projects but also the need to help secure the sustainability of existing projects when deciding on the allocation of any future funding;
- (g) give a particular priority to thoroughly preparing a new project to address the major issue of the limited water supply;
- (h) require the TCc beneficiaries to put in place the necessary legal framework, human and financial resources, and reforms of public administration and financial management to support the effective and sustainable implementation of assistance.

65. If it is decided not to support a further large scale EU assistance programme, an action plan should be prepared to scale down or phase out the Task Force's operations.

66. In order to prepare for the scenario where a political settlement leads to the end of the *de facto* division of the island, the Commission should develop a proposal for a programme to enable the whole country to benefit from EU funding following reunification.

This Report was adopted by Chamber III, headed by Mr Karel PINXTEN, Member of the Court of Auditors, in Luxembourg at its meeting of 6 March 2012.

For the Court of Auditors

Vítor Manuel da SILVA CALDEIRA
President

BREAKDOWN OF ALL INDIVIDUAL PROJECTS/SECTOR PROGRAMMES AS AT 30 SEPTEMBER 2011

Objectives and projects	Planned (euro) ¹	Contracted (euro)	Paid (euro)	Paid / contr. (%)
Objective 1: Developing and restructuring of infrastructure				
<u>Sub-objective 1 - Protecting the environment</u>				
Project 1.1 - Sector programme for updating the quality and management of water supply and sanitation services	71 400 000	83 852 225	40 619 611	48 %
Project 1.2 - Support to the Turkish Cypriot community as regards management and protection of potential Natura 2000 sites in northern part of Cyprus	5 000 000	5 176 480	3 855 268	74 %
Project 1.3 - Solid waste sector programme for the Turkish Cypriot community	21 200 000	19 367 570	10 750 517	56 %
Project 1.4 - Feasibility study for the rehabilitation of the Lefke mining area	900 000	906 500	906 500	100 %
<u>Sub-objective 2 - Improving management of the energy sector</u>				
Project 1.5 - Upgrading the management of the energy sector	5 000 000	6 035 972	5 841 195	97 %
Project 1.6 - Development and restructuring of the energy infrastructure - Part II	8 750 000	5 341 486	5 135 356	96 %
<u>Sub-objective 3 - Improving traffic safety</u>				
Project 1.7 - Improving traffic safety	3 000 000	2 724 511	2 266 958	83 %
<u>Sub-objective 4 - Telecommunications</u>				

Objectives and projects	Planned (euro) ¹	Contracted (euro)	Paid (euro)	Paid / contr. (%)
Project 1.8 - Development and restructuring of telecommunications infrastructure	14 000 000	11 617 413	7 113 606	61 %
Sub-Total	129 250 000	135 022 157	76 489 010	57 %
Objective 2: Promoting social and economic development				
Project 2.1 - Rural Development Sector Programmes I & II	37 350 000	29 837 192	19 941 407	67 %
Project 2.2 - Upgrading of local and urban infrastructure	7 000 000	7 000 000	7 000 000	100 %
Project 2.3 - Upgrading of local and urban infrastructure - Part II	8 000 000	9 784 225	8 850 803	90 %
Project 2.4 - Human Resources Development Sector Programme	9 200 000	8 080 948	6 542 745	81 %
<i>Project 2.5 - Micro and Small Enterprises Loan programme - cancelled in 2009 (Funds from this project were reallocated to the TA/EX project, ICT/SME, Water/Waste water projects)²</i>	9 000 000	0	0	
Project 2.6 - Sustainable economic development sector programme	6 000 000	6 971 860	3 913 291	56 %
Project 2.7 - Supporting private sector development within the Turkish Cypriot community	8 100 000	3 198 200	3 160 000	99 %
Sub-Total	84 650 000	64 872 425	49 408 246	76 %
Objective 3: Fostering reconciliation, confidence building measures and support to civil society				
Project 3.1 - Reconciliation, confidence building measures and support to civil society	14 000 000	13 404 835	11 115 091	83 %
Project 3.2 - De-mining assistance programme	6 500 000	6 495 894	6 495 894	100 %

Objectives and projects	Planned (euro) ¹	Contracted (euro)	Paid (euro)	Paid / contr. (%)
<i>Project 3.3 - Support to the development of new trends in history teaching for reconciliation and stability in Cyprus - cancelled in 2008 (Funds from this project were reallocated to the civil society projects)</i>	1 000 000	0	0	0
Support for the cultural heritage monuments of great importance for the communities of Cyprus	2 000 000	0	0	0
Sub-Total	23 500 000	19 900 729	17 610 985	88 %
Objective 4: Bringing the Turkish Cypriot community closer to the European Union				
Project 4.1 - Community scholarship programme	8 000 000	6 256 875	5 536 216	88 %
Project 4.2 - Promotion of youth exchanges and other people-to-people contacts	3 000 000	1 047 892	904 893	86 %
Project 4.3 - Information on the European Union political and legal order	1 500 000	1 313 100	1 053 100	80 %
Sub-Total	12 500 000	8 617 867	7 494 209	87 %

Objective 5: Preparing the Turkish Cypriot community to introduce and implement the <i>acquis communautaire</i>					
Project 5.1 - Technical Assistance to support legal transportation as well as implementation of the <i>acquis</i> through the TAIEX instrument - Part II (<i>Component A - Assistance through TAIEX</i>); (<i>Component B - small scale equipment facility</i>) + Part I	17 150 000	13 699 997	12 911 242	94 %	
Project 5.2 - Capacity building in the environment sector	2 460 000	1 140 690	1 117 554	98 %	
Unallocated Technical Assistance and Programme Reserve Facility (and wrongly encoded on Decision 2006/018-150) ³	1 740 000	850 203	621 579	73 %	
Sub-Total	21 350 000	15 690 890	14 650 375	93 %	
Total 1	271 250 000	244 104 068	165 152 825	68 %	
Overall technical assistance for the implementation of the programme					
Sub total a (<i>Studies, expertise, office management logistics</i>)	11 400 000	8 436 605	6 776 955	80 %	
Sub total b (<i>Staff and mission costs</i>) Decision 2006/018-621, Decision 2006/018-316, Decision 2006/018-317	9 650 000	6 865 323	6 858 993	100 %	
Total 2	21 050 000	15 301 928	13 635 948	89 %	
Overall total	292 300 000	259 405 996	178 788 773	69 %	

¹ Planned amounts are as indicated in the financing proposals attached to Commission decisions.

² The project could not go ahead due to difficulties to reaching agreement with Kreditanstalt für Wiederaufbau (KfW) in the special conditions prevailing in the northern part of Cyprus.

³ This is referred to as 'Objective 6' in the financial reports from the Task Force. Funds from the Programme Reserve Facility were transferred on the basis of the Commission Decision (2009)2928 to the following projects: CMP (2 million euro), de-mining (1,5 million euro). 1,2 million euro was reallocated from the Unallocated Technical Facility to the TAIEX project.

OVERVIEW OF AUDITED CONTRACTS

Contract type	Contract period	Contract title	Contracted amount ¹ (euro)	Paid amount ¹ (euro)
Project 1.1. Sector programme for upgrading the quality and management of water supply and sanitation services				
PMU/SUP	Nov. 2009–May 2010	Supply of water sampling, analysis and laboratory information management equipment	580 500	580 500
PMU/WKS	Feb. 2009–Nov. 2010	Renewal of water distribution network in the northern part of Nicosia	2 640 000	2 375 624
PMU/WKS	Dec. 2009–Feb. 2012	Construction of seawater desalination plant	27 517 814	0
UNDP/C.A	Jan. 2010–July 2013	Construction of new Mila Milia/Haspolat waste water treatment plant	8 192 242	4 657 046
Project 1.8. Development and restructuring of telecommunications infrastructure				
-/SUP	Oct. 2009–Oct. 2012	Upgrading of the telecommunications infrastructure network	9 828 453	5 897 072
-/SER	Dec. 2008–Dec. 2011	Development and restructuring of telecommunications infrastructure	1 598 750	1 098 750
Project 2.1. Rural development sector programme				
PMU/SER	May 2008–July 2011	TA to support rural development policy	2 868 200	2 265 878
-/SER	Sept. 2008–Sept. 2012	TA to support implementation of the rural development sector programme	1 994 080	1 595 264
PMU/SUP	Dec. 2009–June 2011	Supply of equipment for veterinary laboratories	422 154	422 154
PMU/GRS	Nov. 2009–Jan. 2011	Adataş (Rural development grant scheme call 1, No 127937)		
			15 192	15 192

Contract type	Contract period	Contract title	Contracted amount ¹ (euro)	Paid amount ¹ (euro)
	Oct. 2009–Oct. 2010	Andaç (Rural development grant scheme call 1, No 127937)	52 435	452 435
PMU/GRS	Dec. 2009–Aug. 2011	Çatalköy – Fight Against Insects	144 098	72 049
	Dec. 2009–Dec. 2011	Bü yükönuk Culture House	158 400	126 720
	Dec. 2009–Dec. 2011	Serdarlı Culture and Art House	85 998	68 798
Projects 2.2-2.3. Upgrading of local and urban infrastructure				
UNDP/C.A	Nov. 2006–Sep. 2010	Upgrading of local and urban infrastructure	8 249 869	7 424 869
	Dec. 2007–Oct. 2011	Upgrading of local and urban infrastructure Part II	9 784 225	8 850 803
Project 3.1 – Reconciliation, confidence building measures and support to civil society				
UNDP/C.A	March 2007–May 2009	Support to the CMP	1 469 566	1 469 566
CoE/C.A	Aug. 2007–May 2011	Council of Europe Academy Pol. Studies	600 000	351 000
-/SER	Feb. 2008–Feb. 2011	TA to support the development of reconciliation measures and to support civil society in the TCC: the CSST	1 499 000	1 349 631
	Aug. 2009–Dec. 2010	Post Research Institute: Education for Peace III (CSA call No 126199)	89 310	82 437
-/GRS	May 2009–May 2011	KYTD: Celebrating Diversity and Volunteerism across Cyprus (CSA call No 126199)	166 909	133 528
	May 2009–May 2011	MRG-KISA: Minority rights: a contribution to the Cyprus problem (CSA call No 126199)	197 313	157 851
Project 3.2 – Demining				
UNDP/C.A	Jan. 2007–Feb. 2009	Landmine and Ordnance Clearance in Cyprus IV	3 995 894	3 995 894
	Jan. 2010–Dec. 2011	Landmine and Ordnance Clearance in Cyprus V	2 500 000	2 500 000
Project 4.1 – Community scholarship programme				
-/GRS	Jan. 2007–April 2007	Call for Interests - Community scholarships programme 2007/08 (Call 1)	396 160	396 160

Contract type	Contract period	Contract title	Contracted amount ¹ (euro)	Paid amount ¹ (euro)
	Oct. 2007–April 2008	Call for interests - European Community scholarships programme 2008/09 (Call 2)	1 564 919	1 537 988
	Nov. 2008–Feb. 2009	European Union Scholarships III Programme For the Academic Year 2009/10 Local Grant Scheme (Call 3)	2 346 580	2 271 597
	Dec. 2009-Feb. 2010	Scholarships for the Turkish Cypriot community Programme for the Academic Year 2010/11 (Call 4)	1 313 440	1 051 796
	Feb. 2011-April 2011	Scholarships for the Turkish Cypriot community Programme for the Academic Year 2011/12 (Call 5)	-	-
Project 4.3 – Information on the European Union political and legal order				
-/SER	Feb. 2009–Feb. 2012	Setting up of an open access information point on the European Union	1 300 000	1 040 000
Project 5.2 – Capacity building in the environment sector				
-/SUP	June 2009–Feb. 2011	Supply of Air Quality Monitoring (AQM) Equipment	645 450	645 450
-/SER	June 2009–Sept. 2010	TA for AQM activities in the northern part of Cyprus	197 983	183 121
GTZ contracts for support to EUPSO				
-/SER	July 2006–June 2008	TA in running a PSO in the northern part of Cyprus (GTZ.A)	3 476 000	2 836 524
-/SER	June 2008–June 2012	Setting up of a PSO in the northern part of Cyprus (GTZ.B)	1 496 795	1 496 795
Total			97 387 729	57 474 492

¹ As of 30 September 2011, excepted for grant contracts: 31 March 2011.

WKS= Works contract

SUP= Supplies contract

SER= Service contract

C.A. = Contribution agreement

PMU= Project Management Unit

UNDP=United Nations' Development Programme

CoE=Council of Europe

GRS= Grant scheme

REPLIES OF THE COMMISSION TO THE SPECIAL REPORT OF THE EUROPEAN COURT OF AUDITORS

EUROPEAN UNION ASSISTANCE TO THE TURKISH CYPRIOT COMMUNITY

EXECUTIVE SUMMARY

III. The Commission admits that not operating under more devolved procedures is a constraint, but has made considerable efforts to work with the options available to provide the most appropriate alternative institutional set-up.

IV. The loss of the sea water desalination plant project was an unfortunate setback. After extensive efforts to rescue and proceed with the project, the Commission had to act to protect its financial interests and terminated the construction contract. No payments have been made under this contract. The Commission agrees with the Court's conclusion on the risks to sustainability and the reasons for it and will continue to help the Turkish Cypriot community to develop administrative and technical capacity.

V. First indent - The Commission largely agrees with the Court's recommendations. The Commission attempted to find the best practical solution considering that the establishment of a Delegation within EU territory is not possible. Since the audit, further efficiency improvements have been achieved. When considering further devolution of management, however, the Commission must balance the possible efficiency gains against the risks of reducing the supervision from headquarters, given the particular circumstances of the assistance to the TCc.

V. Second indent - The Commission is committed to providing continued assistance to the Turkish Cypriot community and to working towards reunification of the island of Cyprus. A phasing-out of the operations is not currently planned and these will continue on an appropriate scale.

V. Third indent - Reunification is the central aim of the assistance programme. The Commission recognises that reunification would require a -review of the assistance to Cyprus. The Commission would make timely preparations for this scenario.

OBSERVATIONS

14. The scope of the aid programme is laid down in the Council Regulation as adopted by the Council. The Commission agrees that it was a programming and implementation challenge to cover the broad range of topics.

16. The 2004 proposal contained preliminary allocations only. This was a new programme for the Commission and, during the period of delay in the adoption of the Aid Regulation, further consultation took place with stakeholders. The allocations in the December 2006 Financing Decision were adjusted as a result and therefore somewhat different from those of the 2004 planning. The Commission prioritises the 'reconciliation and confidence-building' objective, and the final contracted amounts in 2009 included use of the programme reserve for demining activities and for support to the Committee on Missing Persons. By the end of 2009, including the commitments on Green Line crossing points, the 'reconciliation and confidence-building' objective was supported by commitments only about 18% below the level envisaged in 2004, rather than 35% less.

Besides this, another substantial amount was committed for the (bi-communal) Nicosia waste water treatment plant, which was included with reconciliation as a prime motivation.

In addition to the above, the entire allocation for 2010, which was €3 million, was devoted, through the Committee on Missing Persons, to the 'reconciliation and confidence-building' objective.

17. The Court's comments on the difficulties of providing effective technical assistance highlight one aspect of the challenging environment for the assistance programme.

21. The Commission agrees that a multi-annual perspective would facilitate the planning and implementation of assistance to the TCc, but this must be seen in the broader political context. The Commission strongly supports efforts towards a settlement of the Cyprus issue and reunification. Meanwhile, the Commission proposes to continue supporting the Turkish Cypriot community on the basis of the current Aid Regulation.

22. The Commission had to consider very carefully how to establish the most efficient management structure from the options available at the same time as it was developing the technical elements of the programme to be delivered.

23-25. Joint reply:

The Commission admits that not operating under more devolved procedures is a constraint, as the establishment of a Delegation in an EU Member State is not possible. The Commission has worked with the options available to provide the most appropriate alternative institutional set-up.

The Commission has taken measures to facilitate operations and financial circuits including derogations of normal procedures and regular missions from the Authorising Officer by sub-Delegation (AOSD) to Nicosia. A new IT structure was put in place at the end of 2011 to allow common file access between Nicosia and Brussels and the 2012 reorganisation of DG ELARG has streamlined the internal processes; the number of units involved in contracts and payments has been reduced from four to two.

The Commission has also to take into account the risks arising from operations in such a sensitive political environment.

26. The Commission Representation (ECR) in the Republic of Cyprus is formally consulted as part of DG COMM in the context of the Commission "inter-service" process. This ensures information flow, cooperation and coordination. The delays in the ECR's responses were also caused by the substantial workload.

The current staff reinforcement of the ECR – also due to the incoming Council Presidency of Cyprus– will further strengthen the cooperation with the other services of the Commission.

27. The situation of the contractual agents in EUPSO is indeed different from that of contractual agents in Delegations. As the Court notes, moreover, current legislation (Article 3b, Article 88, first paragraph, point b of the Conditions of Employment of Other Servants of the European Union) does not allow the engagement of contract staff for a total period of more than three years and does not provide for any derogation from that rule. In December 2011, the Commission proposed to change the Staff Regulations and the Conditions of Employment (COM 2011/890/final) to prolong the duration of the contracts to a maximum of six years. This proposal has still to be adopted. In reviewing the length of contracts, however, the Commission will have to take into account the availability of funds as well as the overall political situation in the context of the settlement talks.

28. The Commission will start an overall programme evaluation in 2012. The advantages of implementing some parts of the programme through the UNDP will be considered in this review.

29. Weaknesses in the first Committee on Missing Persons Contribution Agreement (joint management with UNDP) found by the Court have been addressed in later Agreements e.g. better definition of indicators related to EU funding, better definitions of numbers exhumed and identified, better general output-input relation and improved reporting.

30. Decisions on the management arrangements, including setting up the EUPSO office and the degree of "devolution", formed part of the risk analysis undertaken by the Commission.

33. No funds have been disbursed yet under the construction contract and the contract was terminated in December 2011, after considerable efforts to rescue the project, when there was no prospect of progress. The Commission's financial interests have been protected.

The risk management included designing a two-phase project starting with a pilot plant, but the developments that led to termination could not reasonably have been anticipated at the start of the project.

Box 2 – Management of Implementation Risks:

(a) The Commission evaluated the risk in the context of the selection of the company for the construction of the seawater desalination project. The outcome of this international open tender was fully based on established rules.

(b) The guarantee was not provided by the contractor. In the early stages this was primarily due to issues arising from the complex local context, which the Commission tried to solve. Even if the contract had been terminated in January 2010, it would not have been possible to recommit the money, since the contracting deadline had passed.

(c) The assistance to the Turkish Cypriot community was a new programme for the Commission. During the 3-year contracting window between 2006 and 2009 allowed by the regulations, the programme management and logistics, as well as the projects themselves, had to be developed. Given the need for thorough project preparation, the Commission considers that it would not have been possible to contract the works for the desalination plant at an earlier date.

(d) Commission staff were involved at all stages and started negotiations as soon as problems became apparent. A delay to the start of the contract, pending resolution of site access issues was formally agreed on 17 December 2009. Contacts with the TC authorities were numerous and, given the large size of the contract and the nature of the problems arising, it was clear that the TC leadership was fully aware of the situation. The high-level intervention from the Commission side (letter from the Commissioner to the leader of the Turkish Cypriot community of June 2010) followed after the elections in the Turkish Cypriot community.

35. The telecom liberalisation "law" was adopted on 11 January 2012. The assistance programme can now proceed with the completion of the hardware component and preparation for hand-over to the beneficiary.

36. The absence of a formal Financing Agreement with the (non-recognised) beneficiary was a risk of which the Commission was aware. The Commission has implemented a considerable aid programme within short contracting deadlines and a wide mandate to fulfil. Equipment and infrastructure were provided in the areas specifically mentioned in the Aid Regulation and where it was necessary to

make a real impact. In some areas it was necessary to try to deliver real benefits and encourage sector reforms in parallel.

37. This is the first experience by the TCc of major EU assistance. The complexity of the alignment to the *acquis* and the size of the reforms necessary in this context were underestimated by the beneficiary. The aid programme for the TCc is still relatively new and the major contracting took place only in 2009. The Commission services had no previous experience of working with the TC beneficiary.

38. The seawater desalination plant design change arose from stakeholder and expert consultations, and was related to concerns that the requirements of the Water Framework Directive would not otherwise be met.

39. The problems affecting the implementation of the construction contract for the desalination plant illustrate the difficult operational environment.

40. The failure of the desalination plant project is a disappointment. The environmental effects of the salination of the Morphou aquifer will be taken into account, however. The water sector situation is changing with significant new elements arising. Water and waste water investments remain in the draft assistance programme which is being drawn up for the coming years.

41.(a) Reliable baselines and indicators were not available for water distribution, which is one of the reasons why investments in the water laboratory were made, but the evidence is that there are considerable improvements in service and leak rates for Nicosia water, the latter being previously up to 50% in some areas.

41.(b) UNDP is implementing the Mia Milia/Haspolat project under joint management. The UNDP Deputy Director for Europe is aware of the need for the "joint entity" for the WWTP and, along with the Commission, is engaged in resolving this.

42. In addition to the training that was provided by the suppliers of the laboratory equipment, the Capacity Building project provided training in sampling and analysis to meet the requirement of the Water Framework Directive, Drinking Water Directive and Bathing Water Directive.

Training on the Laboratory Information System (LIMS) is planned for 2012. The laboratory was inspected and passed the accreditation audit for four procedures for heavy metals, pesticides, microbiology and food.

45. The Commission agrees that sustainability is a critical issue. Unless reunification occurs before, this issue will be taken up in the programming for 2012-13.

One of the challenges of the programme environment is the difficulty of working with a beneficiary that is not formally recognised.

46. The issue of property is a sensitive one and tracing the ownership history has proved a significant complicating factor in project implementation.

47. The TCc is not formally represented in the Project Steering Committee, but no project goes ahead without the agreement/approval of the relevant TC interlocutors. Implementation through the UNDP does somewhat restrict the experience gained by local bodies, but does give more confidence in the physical completion of projects. The problem of capacity development in local bodies is partly

addressed by the access to the Community Development grants, outside the UNDP Contribution Agreement.

48. The missing persons issue is sensitive and the work of the Committee on Missing Persons (CMP) work is much appreciated by both communities and strongly supported by the European Parliament. A significant proportion of the total number of "missing" has not been found or identified yet. The Commission has not yet planned an exit strategy, but is aware that, eventually, programme activities will decrease. It is important that the two communities take the initiative in this process.

49. Continuation of the European Forum Cyprus by building upon the alumni network is foreseen.

Members of the European Forum Cyprus (EFC) alumni network participated in the European Forum for Democracy in Limassol in October 2011.

50. The Commission will consider the need for further capacity building in future programmes to the extent that funds are available.

53. The Commission agrees that a multi-annual perspective would facilitate the planning and implementation of assistance to the TCc, but this must be seen in the broader political context.

54. The ex-post survey on the scholarships referred to by the Court will be launched in 2012.

55. The Commission agrees that collaboration between DGs ELARG and COMM could be strengthened and is making supplementary efforts in this respect.

Box 4 – Implementation problems in the Air Quality Monitoring project

(b) Environment is very important from the point of view of the *acquis communautaire*. The programme therefore calls for significant support in this area.

CONCLUSIONS AND RECOMMENDATIONS

59. The Commission admits that there are constraints associated with running the EUPSO programme office without fully devolved management, but, since a Delegation could not be established, the most appropriate alternative institutional set-up was provided for. Measures have been taken to facilitate operations (see the response to point 23), including some streamlining since the audit was carried out.

Improvements have also been made to Contribution Agreements since the time of the audit.

60. The Commission's financial interests have been protected with the cancellation of the desalination plant project. No payments have been made under the construction contract. The failure of this project, despite the Commission's efforts to complete it, is, nevertheless, a setback to efforts to improve the water supply problem and the related issue of salination of the aquifer. The water and waste water sector remains high on the list of priorities for future support.

The Commission agrees with the Court's conclusion on the general risks to sustainability and will continue to support the Turkish Cypriot community with a view to enhancing administrative and technical capacity.

61. The Commission has committed itself to providing continued assistance to the Turkish Cypriot community. Reinforcing the sustainability of new and existing projects is a priority.

64.(a) The Commission agrees that a multi-annual perspective would facilitate the planning and implementation of assistance to the TCc, but this must be seen in the broader political context. The Commission strongly supports efforts towards a settlement of the Cyprus issue. Until this is achieved, the Commission intends to continue supporting the Turkish Cypriot community on the basis of the current Aid Regulation.

64.(b) The Commission agrees with this recommendation. The overall length of future contracts will depend on the outcome of the Commission's proposed change to the Staff Regulations.

64.(c) Since the audit, efficiency improvements have been made in Commission headquarters, (see for example point 23 above), which help to streamline finance and contract procedures. The Commission will consider the issue of devolution, taking into account both its potential advantages and risks in the particular circumstances of assistance to the TCc.

64.(d) The Commission accepts the recommendation on coordination with the Commission Representation (ECR) in Nicosia. There are already formal procedures for inter-DG cooperation at headquarters and the Commission is making further efforts to improve cooperation between the ECR in Nicosia and the Task Force on the ground.

The current staff reinforcement of the ECR – also due to the incoming Cyprus Council Presidency – will help to strengthen cooperation with the other services and this will also bring the benefit of achieving better coherence and consistency.

64.(e) The recommendation on improvements to Contribution Agreements is accepted by the Commission and these improvements have already been made including better definition of indicators related to EU funding, better definitions of numbers exhumed and identified, better general output-input relation and improved reporting.

64.(f) The recommendation on ensuring sustainability will be taken into account in completing existing projects and the programming of new interventions will reflect the steps taken by the TC beneficiary in creating an appropriate environment in terms of organisation, operation, maintenance etc.

64.(g) The Commission accepts the recommendation on water supply. A water sector evaluation has already been carried out since the audit.

64.(h) The Commission agrees with the Court's analysis in terms of the needs for the legal and administrative framework and continues to cooperate with the beneficiary in these areas. The Commission must, however, take into account the current political and legal context, which does not allow the imposition of any legal commitment on the TCc.

65. The Commission is committed to providing continued assistance to the Turkish Cypriot community and to working towards reunification of the island of Cyprus. A phasing-out of the operations is not currently planned and these will continue on an appropriate scale.

66. Reunification is the central aim of the assistance programme. The Commission recognises that a breakthrough in the reunification process would require a review of the assistance to Cyprus. The proposal for the next financial perspective contains a clause to this effect.