EU REPORT 2011

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Report on the EU Financial Management in the CR

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Content:

Introduction

This is the fourth consecutive *Report on the EU Financial Management in the Czech Republic* (also referred to as the *EU Report 2011*). Over the years, it has become a firmly established part of the annual publishing plans of the Supreme Audit Office (SAO). The timing of its publication is designed to follow directly on from the SAO Annual Report, which covers the implementation of strategic goals in the scrutiny of funds provided to the Czech Republic from abroad. The primary objective of the EU Report 2011 is to provide comprehensive information about the SAO's audit findings related solely to the revenues and expenditure of the European Union (EU) budget in the Czech Republic, placing them in the context of the implementation of priorities of EU policies and taking into account the financial significance of, above all, Cohesion Policy and the Common Agricultural Policy. The SAO's audit findings are analysed in the EU Report 2011 and subsequently confronted with the audit findings made by the European Court of Auditors (ECA) during its audit missions undertaken in the Czech Republic. To present a general picture of the standard of financial management of EU budget finances in the Czech Republic, the SAO's audit findings, i.e. findings made solely at national level, are also compared with the audit findings made by the ECA and, in some cases, the European Commission (the Commission) in connection with other EU Member States. The Cohesion Policy area was deliberately chosen for this comparison, as, according to the ECA, payments in this area aggregated for all Member States have been materially affected by errors for several years, with the most probable error rate of over 5% of certified expenditure.

The EU Report 2011 consists of three separate chapters following the structure used in previous editions. The first chapter informs about current developments in the financial management of the EU budget and about the structure of the EU budget, including its relationship with the Czech Republic. In a given time sequence starting with the Czech Republic's accession to the EU in 2004, expenditure channelled from the EU budget into the Czech Republic and revenues provided from the Czech Republic into the EU budget are set out and the net position is enumerated. The second chapter is devoted to sector matters. Against the backdrop of the legal and economic measures adopted in the EU and in the Czech Republic to support economic revitalisation it presents information about the SAO's audit findings related to the EU budget revenues and expenditure on tasks under the Common Agricultural Policy, Cohesion Policy and other EU expenditure. The fact that this is the fourth report means it is possible to compare the quantitative data obtained in individual years and to comment on development trends. The final chapter sets out the SAO's contributions to the development of Czech legislation and presents a process of the SAO's international activities linked to the EU authorities and the audit institutions of EU Member States. One new feature of the EU Report 2011 is the inclusion of a separate Summary, intended to provide readers selected key data and information with minimal accompanying commentary.

The data and information contained in the EU Report 2011 mainly concern the 2010 calendar year or were first published in that year. When compiling the EU Report 2011, data from official domestic and foreign information sources concerning 2010, or 2009 in cases where current year data are not yet official available, were used. First, audit findings from audits approved by the SAO and published in its bulletins issued quarterly in 2010 and at the start of 2011 are presented. These are supplemented by numerical data and commentaries obtained in close cooperation with the relevant units of the Ministry of Finance and the Ministry for Regional Development. The most important foreign sources used were the ECA's Annual Reports for 2009, ECA's special reports, and data from the Commission's Financial Report on the EU budget 2009.

The EU Report 2011 is primarily intended for the relevant committees of the Chamber of Deputies and the Senate of the Parliament of the Czech Republic and the institutions responsible for the financial management of EU budget funds in the Czech Republic. It is also intended for the experts and lay public; the national audit offices of EU Member States and the ECA are traditional recipients.

List of Abbreviations and Acronyms

AA	Audit Authority
ABAC	Accrual Based Accounting
BRH	Supreme Audit Institution of the Federal Republic of Germany (Bundesrechnungshof)
CAP	Common Agriculture Policy
CFP	Common Fisheries Policy
CMO	Common Market Organisation
DAS	Déclaration d´Assurance (Statement of Assurance)
EAFRD	European Agricultural Fund for Rural Development
EAGF	European Agricultural Guarantee Fund
EAGGF	European Agricultural Guidance and Guarantee Fund
ECA	European Court of Auditors
EDS/SPA	Evidence Subsidy System/State Property Admistration
EEPR	European Energy Programme for Recovery
EFSF	European Financial Stability Facility
EESC	European Economic and Social Committee
EIB	European Investment Bank
EP	European Parliament
ERDF	European Regional Development Fund
ESF	European Social Fund
EU	European Union
EUROFISC	network for the swift exchange of information in the fight against VAT fraud
EUROSAI	European Organisation of Supreme Audit Institutions
FIFG	Financial Instrument for Fisheries Guidance
FNS	Fraud Notification System
GDP	Gross Domestic Product
GNI	Gross National Income
IACS	Integrated Administration and Control System
IB	Intermediate Body
IMS	Irregularity Management System
IPA	Instrument for Pre-accession Assistance
ISPA	Instrument for Structural Policies for Pre-accession
ISPROFIN	Information system for the programme financing
IT	Information Technology
LAG	Local Action Groups
MA	Managing Authority
MoF	Ministry of Finance
MfRD	Ministry for Regional Development
NERV	Government‘s National Economic Council
OLAF	Office Européen de Lutte Anti-Fraude (European Anti-Fraud Office)

OP	Operational Programme
OP RDMA	Rural Development and Multifunctional Agriculture Operational Programme
PHARE	Poland and Hungary: Aid for the Restructuring their Economies
PHARE CBC	Poland and Hungary: Aid for the Restructuring their Economies, *Cross Border Cooperation*
RDP	Rural Development Programme
R&D	Research and Development
ROP	Regional Operational Programme
SAI	Supreme Audit Institution
SAIF	State Agricultural Intervention Fund
SAO	Supreme Audit Office
SAPARD	Special Accession Programme for Agriculture and Rural Development
SAPS	Single Area Payment Scheme
SIGMA	Support for Improvement in Governance and Management
SMART	Specific, Measurable, Achievable, Realistic, and Timely
SPD	Single Programming Document for the Prague Cohesion Region
TOR	Traditional Own Resources
CFP	Common Fisheries Policy
TEN	Trans-European Network
VAT	Value Added Tax
VIES	VAT Information Exchange System

Summary

Financial management and audit of the EU budget were in 2010 again influenced significantly by the continuing financial and economic crisis. With a view to preventing budget crises, a ***change to the Lisbon Treaty*** was proposed consisting in the creation of ***a permanent crisis mechanism*** intended to safeguard the financial stability of the eurozone as a whole.

A new European economic strategy called ***Europe 2020*** was adopted by the European Council to set the course for the coming ten years. This strategy specified three priorities and five objectives which should be achieved at EU level by 2020 and which Member States should translate into national targets.

Particular measures were adopted at EU level and by individual Member States in 2010 to mitigate the consequences of the crisis. The EU's measures mainly targeted energy, the rules governing financial management of the Structural Funds, the Common Agricultural Policy, state aid, and financial oversight.

The Czech Government responded to the continuing economic crisis by drawing up a strategy entitled ***Ways Out of the Crisis – Government policy in the short-term and medium-term outlook***. This was followed up by legislative measures designed mainly to reduce public debt level and adjust the system of financial flows related to the Structural Funds.

The adjusted **2009 EU budget** had overall revenues and expenditure of approx. ***€13 billion.*** As in previous years, the dominant share of revenues was GNI-based resources (approx. 70%). **Actual expenditure** was ***€112.3 billion*** and ***€118.4 billion*** after the inclusion of the created reserve. The largest shares of expenditure were held by the Preservation and Management of Natural Resources heading (approx. 49.2%) and the Sustainable Growth heading (41.3%).

The Czech Republic's contribution to the 2009 EU budget amounted to ***€1.374 billion***, representing approx. 1.2% of the EU's total budget revenues. This ranked the Czech Republic in 16th place in terms of EU Member States' absolute contributions. The growth in the Czech Republic's contribution stopped in 2009 as a result of the economic crisis; in absolute terms, the contribution stagnated at the 2008 level. ***The Czech Republic's drawdown*** from the EU budget was ***€2.949 billion***, the largest shares falling to the Sustainable Growth heading (approx. 69%) and Preservation and Management of Natural Resources (approx. 29%). EU budget expenditure effected in the Czech Republic accounts for approx. 2.5% of total payments, ranking the Czech Republic 12th in terms of drawdown by Member States. Total drawdown has grown every year since the Czech Republic joined the EU, although the rate of growth slowed slightly in 2009. ***The net position*** is ***€1.575 billion***, with the growth trend remaining in place.

VAT-based **revenue of the 2009 EU budget** was the third largest item (approx. 11%). In the light of the significance of tax evasion, EU legislation was adopted in 2010 bringing new rules primarily for information exchange via the ***EUROFISC*** network.

In the Czech Republic, ***an amendment of the VAT Act*** was passed to combat tax evasion; the amendment brings new principles and methodologies, for example regarding the transfer of tax obligations.

The SAO's audit work in the revenues domain again focused on VAT administration in 2010. ***Administration of Value Added Tax in the Czech Republic and the Federal Republic of Germany - Follow-up Audit Report*** was published at the beginning of 2011. The report from the parallel audit by the SAO and the BRH contains an assessment of how the recommendations from the previous parallel audit have been implemented and an analysis of the legal situation concerning audit of VAT in large taxpayers in the two countries.

Agriculture and natural resources was an area in which the Czech Republic received payments of ***€867 million*** from the ***2009 EU budget***; most of that sum went on the Common Agricultural Policy. The State Agricultural Intervention Fund (SAIF) - the paying agency -disbursed ***CZK 40.88 billion in total***, with ***CZK 15.54 billion*** of that amount coming from national finances and ***CZK 25.34 billion from the EU budget***. The largest payment items were ***direct payments*** (approx. CZK 25 billion), ***Rural Development Programme*** measures (approx. CZK 7.7 billion) and ***Common Market Organisation*** instruments (CZK 4.3 billion).

The SAO's audit work in the CAP domain in 2010 focused on the economy of payments of market intervention costs and export subsidies. The implementation system was assessed as functional, but shortcomings were declared in the performance of public administration controls and in the implementation of measures adopted with reference to findings from audit missions by EU authorities or audits conducted by internal audit units. Since the middle of 2010, ***the SAO and ECA have been conducting a coordinated audit*** of rural development programme measures (Axis II) and the jointly formulated audit findings should serve as a basis for DAS 2010.

In October 2010, the SAO and ECA jointly organised a ***seminar***, with broad international participation, on the subject of ***Experience with the development and carrying out CAP audits.***

Cohesion was an area in which the Czech Republic received ***payments of €1,974.9 million*** from the EU budget in 2009. Drawdown of the resources allocated for the ***2004-2006 programming period*** was practically ***100%*** and the number of completed projects reached approx. ***99%***. The situation with the drawdown of *Cohesion Fund* resources is similar: six projects scheduled for implementation in 2011 remain to be completed. For the ***2007-2013 programming period***, a number of measures were adopted both by the Commission and by the Czech Government to make drawdown more effective. Of the total ***allocation*** equivalent to ***CZK 782,227 million***, ***26%*** was paid out to beneficiaries by the end of 2010, including advance payments, and payment applications amounting to ***11.4%*** were sent to the Commission. Low drawdown of the allocation means there is a real risk in the case of six OPs that application of the ***n+3*** rule may result in ***automatic decommitment*** in ***2011***. Moreover, this risk is emphasized by the fact that, at the beginning of 2011, certification of expenditure of five OPs was suspended by the Paying and Certifying Authority (Ministry of Finance). The funding of the OP Enterprise and Innovation was also suspended by the Commission.

The SAO's audit work in the Cohesion Policy domain comprised six audits in 2010, three of which targeted transport infrastructure projects. The findings at the level of implementing bodies concern shortcomings in how programmes' monitoring indicators are set up and projects are assessed and selected, and include control system deficiencies. The predominant shortcomings of final beneficiaries are linked to public procurement and violations of the project implementation terms. The results of the SAO's audits are consistent with the ECA's findings in other EU Member States.

Other EU expenditure comprises a set of measures under which individual programmes under direct centralised management or shared management are financed. In ***2009***, beneficiaries in the Czech Republic obtained **€90.9 million**, i.e. approx. **0.8%** of the payments earmarked for this purpose in the EU budget.

Pre-accession instruments in the Czech Republic in 2010 consisted solely of **PHARE** (or PHARE CBC) programmes. The Commission has wound up just 19 out of a total of 38 completed programmes so far.

The last allocation drawdown took place in 2010 under the **Transition Facility.**

In 2010, the SAO dealt with **legal questions** linked to the financial management of EU finances as part of the interdepartmental comments process for draft legislation or by drawing attention to these matters in approved audit conclusions. In its audit findings it drew attention to legislative deficiencies related to the conclusion of contracts on the provision of grants under ROPs and pointed out that the Czech Republic's legal regulations do not cover the performance of financial corrections of irregularities detected before payments are made to beneficiaries.

The SAO's international activities in 2010 focused on coordinated audits and the exchange of experience as part of the work of Contact Committee working groups, as well as on participating in and organising of expert seminars.

A. General information

A.1 Current development in the EU budget implementation and control

This chapter deals with current developments in the implementation and control of the EU budget, mainly with regard to the continuing global financial and budgetary crisis.

A.1.1 Lisbon Treaty

The **Treaty of Lisbon** entered into force on 1 December 2009. Two draft amendments were submitted to the European Council in its first year of effect. The first proposal concerned the mandate of 18 new members of the European Parliament expected to join the European Parliament under the terms of the new wording of the *Treaty on the Functioning of the European Union*[1]. The second proposed change to the Lisbon Treaty[2] responds to the financial crisis and certain Member States' debt crisis. The change to the Treaty consists in the setting up of a European Stability Mechanism by eurozone countries. The underlying purpose is to protect the financial stability of the eurozone as a whole. This mechanism replaces the Financial Stability Fund and the European Financial Stability Mechanism, which will be terminated in 2013. It is not known yet what specific form the permanent stability mechanism will take, but the *General Features of the Future Mechanism*[3] annex indicates that the European Stability Mechanism will be based on the EFSF and will serve to provide financial assistance packages to eurozone Member States[4]:

In view of the lengthy legislative processes, the change brought about by the introduction of the Lisbon Treaty was not reflected in the **Financial Regulation**[5] until 2010, mainly with regard to the establishment of the European External Action Service. It should be noted that additional changes to the Financial Regulation grounded in the adoption of the Lisbon Treaty are currently in the approval phase.

1 *The Treaty on the Functioning of the European Union is the new name for the original Treaty establishing the European Community.*
2 Conclusions of the European Council (16-17 December 2010), EUCO 30/10.
3 General features of the future mechanism, Eurogroup report of 28 November 2010.
4 Financial assistance will, however, be provided only if the eurozone is under threat as a whole, if strict conditions are met and according to the rules of the current EFSF.
5 Regulation (EU, Euratom) No. 1081/2010 of the European Parliament and of the Council of 24 November 2010 amending Council Regulation (EC, Euratom) No. 1605/2002 on the Financial Regulation applicable to the general budget of the European Communities, as regards the European External Action Service.

A.1.2 Europe 2020 strategy

The economic crisis has affected practically the whole world, Europe and the EU being no exception. The long-term effect of the crisis has uncovered shortcomings and weaknesses in the EU economy. For that reason the Commission proposed a new economic strategy called Europe 2020[6]. The strategy's objective is to steer the EU economy out of the crisis and to set the course for the coming ten years. Europe 2020 identifies three priorities: smart growth (encouraging learning, innovation, promoting education and the digital society); sustainable growth (promoting efficient use of resources and boosting the EU's competitiveness); and inclusive growth (raising the employment rate, investing in skills, fighting poverty). Five headline objectives were set, which should be achieved at EU level by 2020 and which Member States should translate into national targets ("national reform programmes"):

- 75% of the population aged 20 to 64 should be employed.
- 3% of the EU's GDP to be invested in research and development.
- The "20-20-20"[7] climate change and energy targets should be attained.
- School drop-out rates to be reduced below 10%; at least 40% of 30-34 year olds should be completing tertiary education.
- At least 20 million fewer people in or at risk of poverty.

In June 2010, the Czech Government approved national targets[8] consistent with the strategy's headline objectives. The national targets presented to the Commission by the Czech Government aim for a total rate of employment of 75%, a national target of 2.7% of GDP to be invested in R&D, 32% of people aged 30 to 34 to be completing tertiary education and a school drop-out target rate of 5.5%. There should be a 30,000 reduction in the number people in or at risk of poverty. The Czech Government has not yet submitted to the Commission its national target for savings in primary energy source consumption.

The Commission will monitor progress in achieving the targets and implementing the strategy and will publish an annual report of the results. In the interests of coherence, the report will be published at the same time as the review of the Stability and Growth Pact[9], which will make it possible to pursue similar reform objectives for both strategies while remaining separate instruments.

In line with Europe 2020 and the Stability and Growth Pact, the Commission issued a report entitled *Annual Growth Survey*[10], which is the first step in the new form of closer coordination between Member States and is also part of the new "European semester"[11], i.e., a six-month cycle in which Member States' Governments will cooperate closely in the formulation of their countries' budgetary and economic policies. The report sets ten priorities addressing the Union's main economic questions, e.g., cutting public budget debt levels, pension reform etc.

A.1.3 European Commission's and European Court of Auditors' initiatives designed to improve financial management

A.1.3.1 Action Plan to strengthen the European Commission's supervisory role under shared management of structural actions

In 2008, the Commission adopted an Action Plan[12] to strengthen its supervisory role vis-à-vis Member States in connection with shared management of structural actions. The aim of the Action Plan was to reinforce the Commission's measures to tackle the high rate of errors affecting the payment of expenditure on structural actions and to resolve

6 Communication of the Commission: Europe 2020, a strategy for smart, sustainable and inclusive growth, COM(2010) 2020 of 3 March 2010.
7 The 20-20-20 target means reducing greenhouse gas emissions by 20%, increasing the share of renewable energy sources to 20% and increasing energy efficiency by 20%.
8 Government resolution No. 434 of 7 June 2010 "National Targets based on the Main Objectives of Europe 2020 Strategy".
9 The Stability and Growth Pact is a framework for coordinating national fiscal policies in the Economic and Monetary Union; its objective is to safeguard sound public finances. It was approved at a session of the European Council in Amsterdam in June 1997.
10 Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, Annual Growth Survey, COM(2010) of 12 January 2010.
11 The European Semester – above all, its introduction changed the timing of the submission of Member States' convergence and stabilisation programmes. These data had hitherto been presented in autumn, now it should be at the start of the year.
12 Communication from the Commission to the European Parliament, the Council and the Court of Auditors, Action Plan to Strengthen the Commission's Supervisory Role under Shared Management of Structural Actions, COM(2008)97 of 19 February 2008.

the shortcomings of Member States' management and control systems. The Action Plan was composed of 37 actions divided into 10 main areas. Further actions and programmes were added in 2008 and 2009.

In February 2010, the Commission issued the final report on the *Impact of the action plan to strengthen the role of the Commission under shared management of structural actions*[13], assessing the results and the first impact on the implementation of the action plan and on the implementation of additional actions by the Commission under the joint audit strategy for structural actions.

The Commission acknowledges in the report that the first assessment of impacts is merely preliminary, given the diverse nature of the actions and the fact that reducing error rates is a lengthy process. There are, however, at least three areas in which the Commission expects the actions carried out under the action plan to have a visible impact.

- The first audits of actions in the 2007-2013 programming period indicate that error rates decreased in the area of Cohesion.
- The Commission improved its supervisory role on the shared management of Funds[14].
- The Commission applied financial corrections in an effective way to reduce the risk of loss to the EU budget[15].

The Commission judged that it has *"produced results for all the actions and has laid the foundations for continued improvements"*. It therefore considers the Action Plan completed and the objectives achieved.

A.1.3.2 Improving the financial management of the EU budget: risks and challenges

In January 2010, the ECA published an opinion entitled *Improving the Financial Management of the European Union Budget: Risks and Challenges*[16]. This opinion aimed to summarise the main messages of recent annual and special ECA reports and to identify the main risks and challenges to reducing further the level of irregularity and improving the quality of EU spending.

The ECA identified cohesion, external aid, development, and enlargement, including pre-accession programmes, as the areas with the highest levels of payment irregularity. A high level of irregular payments was also found in the framework programme on research and technological development and in rural development expenditure.

The irregularities most commonly affect interim and final payments. They are the result of ineligible claims by beneficiaries, over-declaration of eligible costs and non-compliance with the conditions for payment, in particular public procurement rules. According to the ECA's findings, these errors have two principal causes: deficiencies in systems to control risks at the financial beneficiary level and the complexity of the eligibility rules and other conditions beneficiaries have to comply with.

The ECA's report highlights the areas the Commission should address to reduce the level of irregularity. According to the ECA, the Commission should target the specific systemic weaknesses the ECA had found in the areas with the highest levels of irregularity. It should continue to monitor the effects of actions already taken as well as improving the reliability of the assessments of the areas susceptible to risks and the quality of internal controls made in the Annual Activity Reports and declarations of Directors General of the Commission. There is also scope, in the ECA's opinion, for the Commission to seek to enhance the quality of the Annual Summaries drawn up by Member States in order to increase the assurance the Commission can derive from them. The Commission should also pay attention to improving the financial correction and recovery mechanisms related to the closure of the 2000-2006 programming period and Research Framework Programmes. Simplification should remain the top priority when reforming the rules and regulations governing existing and new spending programmes and schemes, because rules and regulations that are clear to interpret and simple to apply not only decrease the risk of error but can also reduce the control costs.

13 Communication from the Commission to the European Parliament, the Council and the Court of Auditors, Impact of the Action Plan to Strengthen the Commission's Supervisory Role under Shared Management of Structural Actions, COM(2010) 52 of 18 February 2010.

14 In this point, the Commission refers to the Annual Reports of the Directorate-General for Regional Policy and the Directorate-General for Employment, Social Affairs and Inclusion, which reveal a distinct improvement in the working of the systems in Member States in 2007 and 2008.

15 The Commission bases the effectiveness of these measures on the significant increase in financial corrections, where the value of financial corrections for 2008 and 2009 amounted to €3.8 billion, which is more than the value of financial corrections for the entire period of 2000 to 2007, which was €3.5 billion.

16 Opinion No. 1/2010 of the European Court of Auditors, Improving the Financial Management of the European Union Budget: Risks and Challenges.

The ECA recommends that when revising existing interventions and designing new ones the Commission should focus on applying the principles of clarity of goals, simplification, transparency, and accountability. It also advocates strengthening ex-ante evaluation of programmes and emphasises giving due consideration to the question whether a particular programme brings European added value. For the coming programming period it recommends that the key objectives should be to improve the quality of budgeting and of spending and to focus on outputs more than inputs. The ECA also recommends simplifying cost calculations, reviewing the level at which funds are managed, defining control systems in terms of their outputs, and developing further the application of the concept of tolerable risk.

A.1.4 Measures adopted by the EU and the Czech Republic in response to the financial and economic crisis

In response to the enduring financial and economic crisis, the EU authorities continued to look for ways to end it or mitigate its consequences. A number of measures to tackle the crisis were adopted within the EU. Here is a list of the measures that influenced the management of EU budget funds in Member States:

Energy – the EEPR[17] was established in 2009 to aid economic recovery. During 2010, however, it was discovered that the entire allocation would not be used up, so Regulation of the European Parliament and of the Council (EU) No. 1233/2010 introduced a new financial facility[18] to support energy efficiency and renewable energy initiatives. This facility should aid the drawdown of funds allocated to the EEPR so that the selected investment projects have a significant impact on economic recovery in the EU, increased energy security, and the reduction of greenhouse gas emissions.

Structural Funds and *Cohesion Fund* – a change to the financial management rules affecting the Structural Funds and the *Cohesion Fund*[19] was made in 2010. The aim is to facilitate access to funding, accelerate the implementation of programmes and simplify management. The key measures include the introduction of a single threshold of €50 million for all major projects that must be approved by the Commission; the possibility for major projects to be financed by more than one operational programme; greater use of financial engineering instruments; a loosening of the obligation to maintain investments; simplification of the rules for revenue-generating projects; extension of the deadline for use of commitments from 2007; and the payment of €775 million in advances to certain Member States (Estonia, Latvia, Lithuania, Hungary, and Romania).

Common Agricultural Policy – following the CAP "Health-Check", in January 2010 an additional budget of €3.9 billion was made available for rural development. A further €1 billion was added to that sum from the European Economic Recovery Plan. Most of the funds have been concentrated in biological diversity, water management, and broadband connection in rural areas. €42 million was earmarked for the Czech Republic.

State aid – in view of the gradual recovery of Member States' economies, the Commission decided to terminate as of 31 December 2010 the State aid scheme that made it easier for Member States to provide crisis-hit enterprises with aid of up to €500,000 without being in breach of the State aid rules[20]. Other measures governed by the Temporary Union Framework for State Aid Measures to Support Access to Finance in the Current Financial and Economic Crisis from 2008 were preserved in a reduced scope.

Protection of financial stability – with a view to making financial systems more resilient and preventing a future financial and banking crisis, the EU decided to introduce a new European system of financial oversight and new oversight bodies[21]. Now, the European Systemic Risk Board is responsible for "macro-prudential" oversight, while

17 Regulation (EC) No. 663/2009 of the European Parliament and of the Council of 13 July 2009 establishing a programme to aid economic recovery by granting Community financial assistance to projects in the field of energy.

18 Regulation (EU) No. 1233/2010 of the European Parliament and of the Council of 15 December 2010 amending Regulation (EC) No. 663/2009 establishing a programme to aid economic recovery by granting Community financial assistance to projects in the field of energy.

19 Regulation (EU) No. 539/2010 of the European Parliament and of the Council of 16 June 2010 amending Council Regulation (EC) No. 1083/2006 laying down general provisions on the European Regional Development Fund, the European Social Fund and the *Cohesion Fund* as regards simplification of certain requirements and as regards certain provisions relating to financial management.

20 Revision of Communication from the Commission - Temporary Union framework for State aid measures to support access to finance in the current financial and economic crisis (2011/C 6/05) of 11 January 2011.

21 E.g., Regulation (EU) No. 1092/2010 of the European Parliament and of the Council of 24 November 2010 on European Union macro-prudential oversight of the financial system and establishing a European Systemic Risk Board.

the European Banking Authority, the European Securities and Markets Authority, the European Insurance and Occupational Pensions Authority and the Joint Committee of European Supervisory Authorities are responsible for oversight at the microeconomic level.

Measures to tackle the crisis in the Czech Republic went ahead in 2010, following the course set by the National Counter-crisis Plan[22] and its Final Report from 2009[23]. In the domain of Cohesion Policy, in December 2009 the Government noted the Analysis of the Use of Structural Funds and the *Cohesion Fund* to Tackle the Consequences of the Economic Crisis – the details are given in Chapter B.3. In February 2010, the Czech Government approved a strategy entitled *Ways Out of the Crisis – Government policy in the short-term and medium-term outlook*[24]. The strategy aims *"to define the Czech Republic's strategy on the road to overcoming the consequences of the global economic crisis, or to overcoming its consequences in the domestic economy"*. The strategy is divided into three chapters: macroeconomic framework, Government policies and State budget. In total it contains 38 measures designed to tackle the economic and financial crisis. In the second half of 2010, measures were adopted to cut public debt. These mainly affect taxation (ending several incomes' exemption from tax, introducing a "floods tax" *et al.*); sickness and social insurance (changes in sickness contributions, cash help in maternity, birth allowance, changes in unemployment benefit *et al.*); building-related saving; the pay of representatives of the executive and judges; excise duties; real estate tax; political party financing; *et al.* To kick-start the economy, especially in the regions, State budget co-financing of ROP and OP Prague projects from 2011 was again approved, specifically in respect of projects approved before 22 September 2010[25].

A.1.5 Summaries of audits and declarations

At the beginning of 2010, Member States submitted their third consecutive annual audit summaries and declarations to the Commission for the 2009 budget year, as the Financial Regulation instructs them to by February 15 of the following year[26]. The national audit summaries set out the main results of audits undertaken by audit or certifying authorities; the Declaration of Assurance contains a summary declaration on behalf of the Member State, including information as to whether its management and control systems provide adequate assurance of the regularity of expenditure.

The Czech Ministry of Finance sent the summary of audits and the Declaration for the area of the Structural Funds and the State Agricultural Intervention Fund (SAIF) for the area of agriculture. The Commission accepted both summaries, even though both the Ministry and the SAIF failed to provide a Declaration of Assurance concerning the regularity of the management of EU resources[27]. Such a Declaration is a voluntary adjunct, however, and its absence did not affect the Commission's overall assessment.

The results of the annual audit reports and annual opinions regarding the Structural Funds in the 2010 budget year indicate that the Ministry judges the OP and ROP management and control systems to be effective in the majority of cases. In 14 cases out of 19, the Audit Authority states in its opinion that *"the management and control system set up in line with the applicable requirements of Articles 58 to 62 of Council Regulation (EC) No. 1083/2006 and Section 3 of Commission Regulation (EC) No. 1828/2006 for the given OP functioned effectively and thus provided adequate assurance that the expenditure statements submitted to the Commission are accurate, and thus also adequate assurance that the related transactions are legal and regular".* In some cases, however, it states that certain minor improvements were or are necessary. In four cases it issued a qualified opinion. In the case of OP Research and Development for Innovations it refused to issue an opinion because no audits of operations had occurred during the reference period and major staffing and organisational changes had taken place in the OP managing authority. These changes made to the management and control system

22 Resolution of the Government of the Czech Republic No. 204 of 16 February 2009, concerning the National Counter-crisis Plan.
23 Final Report, National Economic Council of the Government, September 2009.
24 Ways Out of the Crisis – Government policy in the short-term and medium-term outlook, approved by Czech Government Resolution No. 119 of 8 February 2010.
25 Resolution of the Government of the Czech Republic No. 64 of 19 January 2011 on the Rules for Co-financing European Union Resources from National Public Sources.
26 Council Regulation (EC, Euratom) No. 1605/2002 on the Financial Regulation applicable to the general budget of the European Communities.
27 Annual Activity Report for the year 2009. Directorate General Regional Policy, 2010; Annual Activity Report 2009, Directorate General for Agriculture and Rural Development, 2010.

approved by the Commission have not been subjected to detailed assessment yet, which made it impossible to judge their functionality.

A.1.6 Annual Reports of the European Court of Auditors concerning the financial year 2009

The ECA is the body established by the Treaty to audit EU finances. As an external auditor it helps to improve the EU's financial management and acts as an independent protector of the financial interests of EU citizens. Every year, the ECA issues an annual report on the implementation of the budget[28]. The general EU budget is approved every year by the Council and the European Parliament. The ECA's Annual Reports and special reports form the basis on which the European Parliament gives the discharge to the Commission, endorsing that the Commission duly complied with its obligations in implementing the budget. For the first time, the ECA sent its Annual Reports for 2009 to the Parliaments of Member States as well as to the Council and the European Parliament in accordance with Protocol No. 1 annexed to the Treaty of Lisbon. The central item in the Annual Reports is the ECA's Statement of Assurance (DAS) concerning the reliability of the European Union's financial statements and the legality and regularity of operations.

For the third year running, the ECA[29] stated that the EU's financial statements gave a true and fair view of the financial position, the results of operations and cash flows. Notwithstanding this positive statement, the ECA draws attention to the fact that shortcomings in the accounting systems of certain Directorates-General of the Commission still need to be resolved. Concerning the legality and regularity of operations the ECA found that, as in the previous years, revenues and commitments were in all material respects legal and regular and that supervisory and control systems were effective. That cannot be said of budgetary payments, however, as these, with the exception of two areas of spending (administrative expenditure and economic and financial affairs) were materially affected by errors.

The following table summarises the results of the overall assessment of supervisory and control systems for each section of the budget.

Table 1: Summary of 2009 findings on the regularity of transactions

Specific Assessments	Functioning of supervisory and control systems	Error rate range
Revenues		
Agriculture and natural resources		
Cohesion		
Research, energy, and transport		
External aid, development, and enlargement		
Education and citizenship		
Economic and financial affairs		
Administrative and other expenditure		

Legend:

Functioning of supervisory and control systems
- effective
- partially effective
- not effective

Error rate range
- less than 2 %
- between 2 % and 5 %
- greater than 5 %

Source: Annual Reports concerning the financial year 2009, table 1.2.

28 Annual Reports concerning the Financial Year 2009, European Court of Auditors, 9 September 2010.

29 Speech by Mr Vítor Caldeira, ECA, Presentation of the 2009 Annual Report to the Committee on Budgetary Control of the European Parliament, 9 November 2010, ECA/10/37.

If we compare the results of the audits conducted by the ECA in recent years, we find that the error rate[30] for payments as a whole has fallen continually in the previous years. Compared to 2008, however, there was an increase in the error rate for payments in the *Agriculture and Natural Resources*[31] policy group. Conversely, there was a marked fall in the error rate in *Cohesion*[32] payments.

The conclusions in the *Agriculture and Natural Resources* chapter of the ECA's Annual Reports are based partly on findings made during audit missions undertaken in the Czech Republic. The ECA tested the supervisory and control systems operating in the rural development expenditure domain. It rated the supervisory and control system in the Czech Republic as effective.

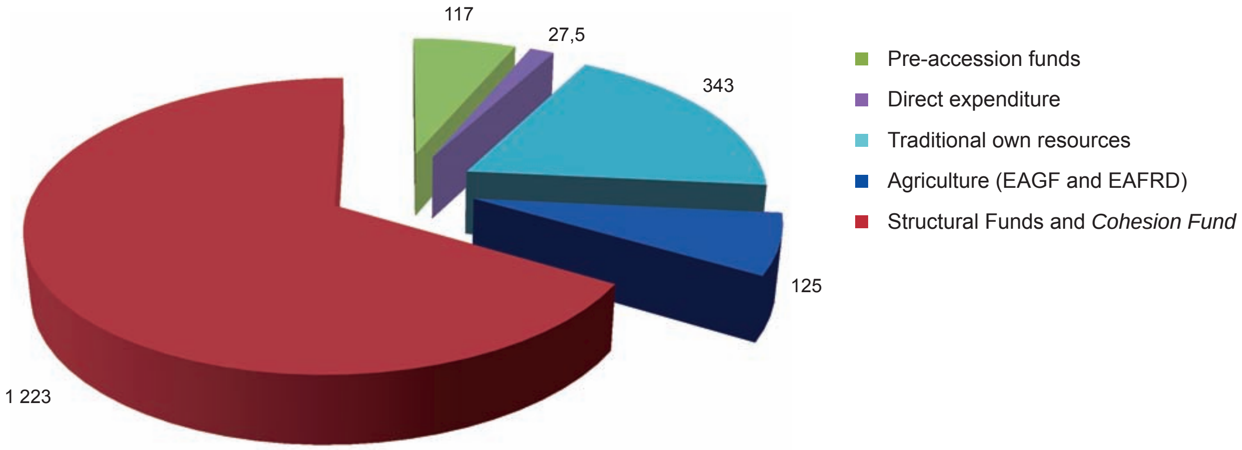
The *Cohesion Policy* area, the second biggest policy group accounting for almost a third of the EU budget, remains the only section of the budget in which the estimated error rate exceeds 5%. The details of this issue are set out in Chapter B.3.2.

A.1.7 Current development in the protection of the EU's financial management

Protecting the EU's financial interests and fighting fraud is an area the EU and Member States are jointly responsible for. In cooperation with Member States, the Commission draws up annual reports on the protection of financial interests, setting out statistical data and describing new actions taken to fulfil Member States' obligations in this area. The Commission added two special topics to the report for 2009[33]: "cooperation between the Commission and Member States in on-the-spot checks" and "measures taken by Member States for the recovery of irregular amounts". The information on these topics was obtained by means of questionnaires filled in by Member States.

The report for 2009 shows that in total 12,611 cases of irregularities[34] were reported in the areas of budget expenditure and traditional own resources. The total financial impact of these irregularities was €1,835.5 million. Graph 1 shows the financial impact of irregularities by areas of the EU budget.

Graph 1: Total estimated financial impact of irregularities in 2009 (€ million)



Source: Report from the Commission to the Council and the European Parliament, Protection of the European Union's financial interests-Fight against fraud – Annual Report 2009, COM(2010) 382 of 14. 7. 2010

Year-on-year comparison[35] reveals that the number of reported irregularities and the estimated financial impact grew significantly. This growth is explained by the introduction of the new IMS internet system that has made it possible for reports to be drawn up by many more users – this has naturally influenced the number of reported cases.

30 The error rates are calculated on the basis of a representative statistical sample of interim and final payments for 2009 (€23 billion) with a confidence level of 95%.

31 Based on testing of 241 payments, the most probable error rate is 2-5%, which is an increase from 2008 when the estimate was 2%.

32 Operations affected by errors amounted to 36% in 2009, 43% in 2008 and 54% in 2007.

33 Report from the Commission to the Council and the European Parliament: Protection of the Communities' financial interests – Fight against fraud – Annual Report 2009, COM(2010) 382 of 14 July 2010.

34 Implementation of the article 325 by the Member States in 2009 Accompanying document to the Report from the Commission to the European Parliament and to the Council – Protection of the financial interests-fight against fraud-Annual report 2009; SEC (2010) 897 of 14. 7. 2010

35 11,939 irregularities with a financial impact of €1,134 million were reported in 2008.

A first glance at Graph 1 shows that the greatest estimated financial impact came under the Structural Funds (109% growth over 2008). Although the Commission offers various reasons for this increase (a greater number of audits in connection with the end of the 2000-2006 programming period, reporting of irregularities by Romania and Bulgaria *et al.*), it acknowledges that the management and control systems in this area need to be improved further.

For the Czech Republic, 186 cases of irregularities with a financial impact of approx. €20 million were reported, which is consistent with the figures for 2008. Most of the irregularities concern the Structural Funds and traditional own resources.

In March 2010, OLAF launched the new FNS online system for reporting suspicions of fraud[36]. This system enables citizens and EU employees to file anonymous reports of suspicions of corruption or fraud and enables OLAF inspectors to communicate with the informants. OLAF expects the launch of this system to bring about simpler and more open cooperation with EU citizens, resulting in more notifications of suspicions of fraud or corruption. The possibility of communication with informants will also ensure more reliable notifications.

A.2 The EU budget structure and its relation to the Czech Republic

A.2.1 EU budget revenues

EU budget revenues comprise own resources and other revenues. Own resources can be divided into several groups:

- **Traditional own resources,** which are revenues from customs duties and sugar levies. These sums are levied by Member States, which keep 25% of the amount as compensation for their associated costs.
- **Resource based on value added tax,** which is paid out of the VAT base in Member States. The harmonised rate is 0.3%. The VAT base is limited to 50% of GNI in all Member States.
- **Resource based on GNI** is a variable amount and is used to make up the difference between budget revenues and expenditure. A single percentage rate is applied to all Member States' GNI; the rate is defined as part of the budgeting process.

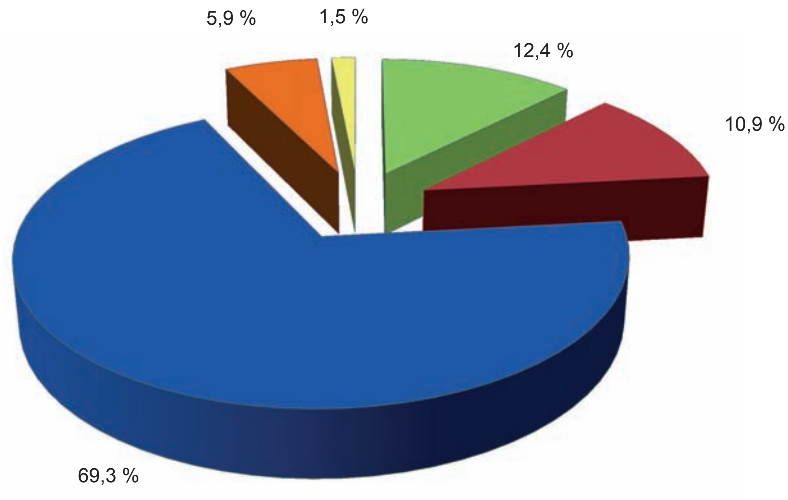
The own resources system is modified by various corrections for individual Member States. The most significant adjustment is the UK correction mechanism, which was adopted in 1984 to correct the imbalance in the UK's percentage share of allocated expenditure and the UK's share of own resources payments. This mechanism, however, also increases the own resources amount paid by other Member States, so in 1995 a cap was imposed on the payments of the biggest net contributors to the EU budget (Germany, Austria, Sweden, and the Netherlands) to compensate for the UK correction mechanism. For the 2007-2013 period, the rate applied to the calculation of the share of VAT was also reduced for those four countries. Limits on GNI-based annual contributions were also adopted for the Netherlands and Sweden. Corrections are applied to Denmark, Ireland, and the UK in connection with their refusal to participate in certain areas of legal and police cooperation.

"Other revenues" include fines linked to economic competition policy, surpluses from previous years, tax on the incomes of EU employees, and contributions by third countries to EU programmes.

Graph 2 shows the shares of the different resources in total EU budget revenues, which, after the transfer of the reserve from the previous year, amounted to €117.6 billion in 2009.

36 Press release OLAF/10/3 of 1 March 2010: *New system to report corruption and fraud anonymously.*

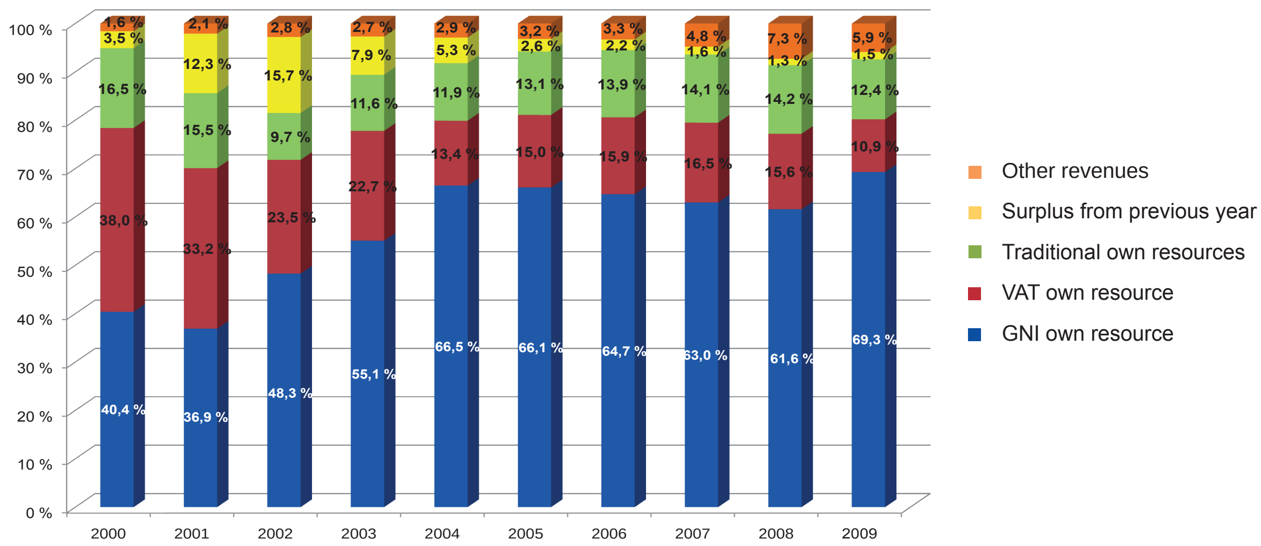
Graph 2: Structure of EU budget financing in 2009 (in %)



Source: European Commission – EU budget 2009 – Financial Report.

Own resources make up over 90% of EU budget revenues, but their structure has changed over the years. The VAT-based share has been falling while the GNI-based share has proportionately increased, as Graph 3 shows.

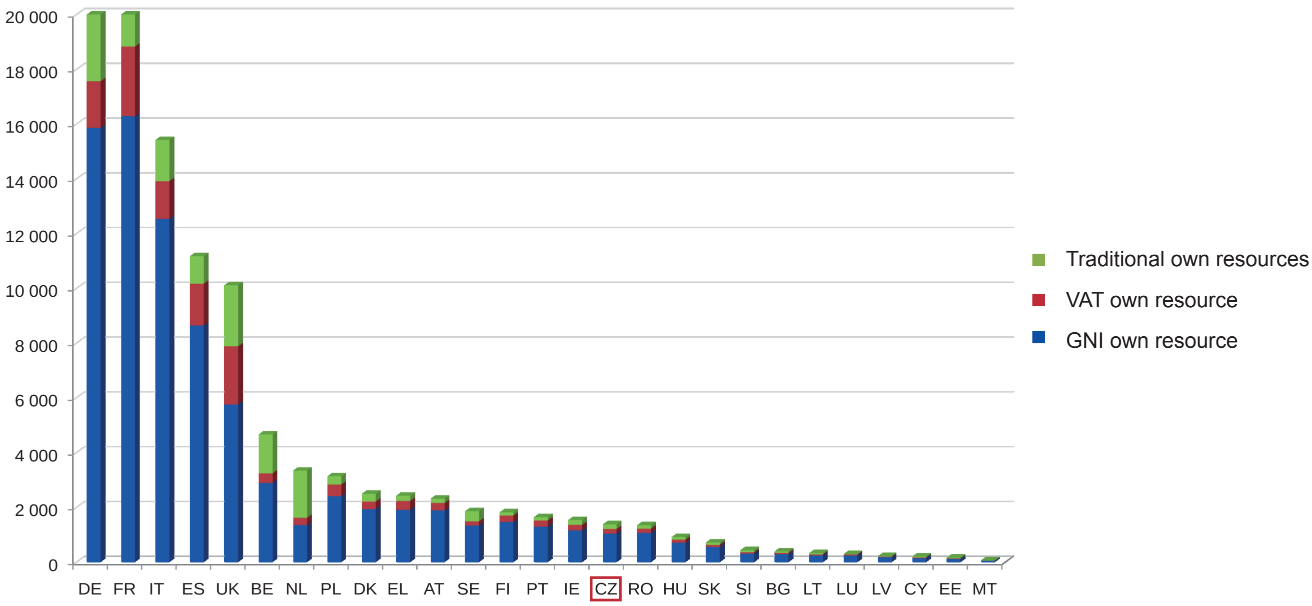
Graph 3: Structure of EU budget in 2000-2009 (in %)



Source: European Commission – EU budget 2009 – Financial Report.

Member States' shares in the funding of the EU budget and the structure of their contributions are shown in Graph 4.

Graph 4: National contribution by Member State collected on behalf of the EU in 2009 **(€ million)**



Source: European Commission – EU budget 2009 – Financial Report.

Used abbreviations: AT – Austria, BE – Belgium, BG – Bulgaria, CZ – the Czech Republic, CY – Cyprus, DE – Germany, DK – Denmark, EE – Estonia, EL – Greece, ES – Spain, FI – Finland, FR – France, HU – Hungary, IE – Ireland, IT – Italy, LV – Lithuania, LT – Latvia, LU – Luxembourg, MT – Malta, NL – the Netherlands, PL – Poland, PT – Portugal, RO – Romania, SE – Sweden, SL – Slovenia, SK – Slovakia, UK – United Kingdom

A.2.2 EU budget expenditure

EU budget expenditure is decided by the **Council of the EU and the European Parliament** based on a proposal by the Commission. The budget for the 2007-2013 period is defined by the financial framework, which sets binding limits.

The expenditure side of the EU budget is divided into six headings:

1) Sustainable growth, which is divided into two mutually related subheadings:

1a) Competitiveness for growth and employment, comprising spending on research, education, trans-European networks, social policy, the internal market, and related policies.

1b) Cohesion for growth and employment, consisting of finances earmarked for enhancing economic, social, and territorial cohesion.

2) Preservation and management of natural resources, covering the common agricultural policy and fisheries policy, rural development, and environmental protection measures.

3) Citizenship, freedom, security and justice, which is split into two subheadings:

3a) Freedom, security, and justice, encompassing justice, border protection, immigration and asylum policy.

3b) Citizenship, comprising public health, consumer protection, culture, youth, and dialogue with citizens.

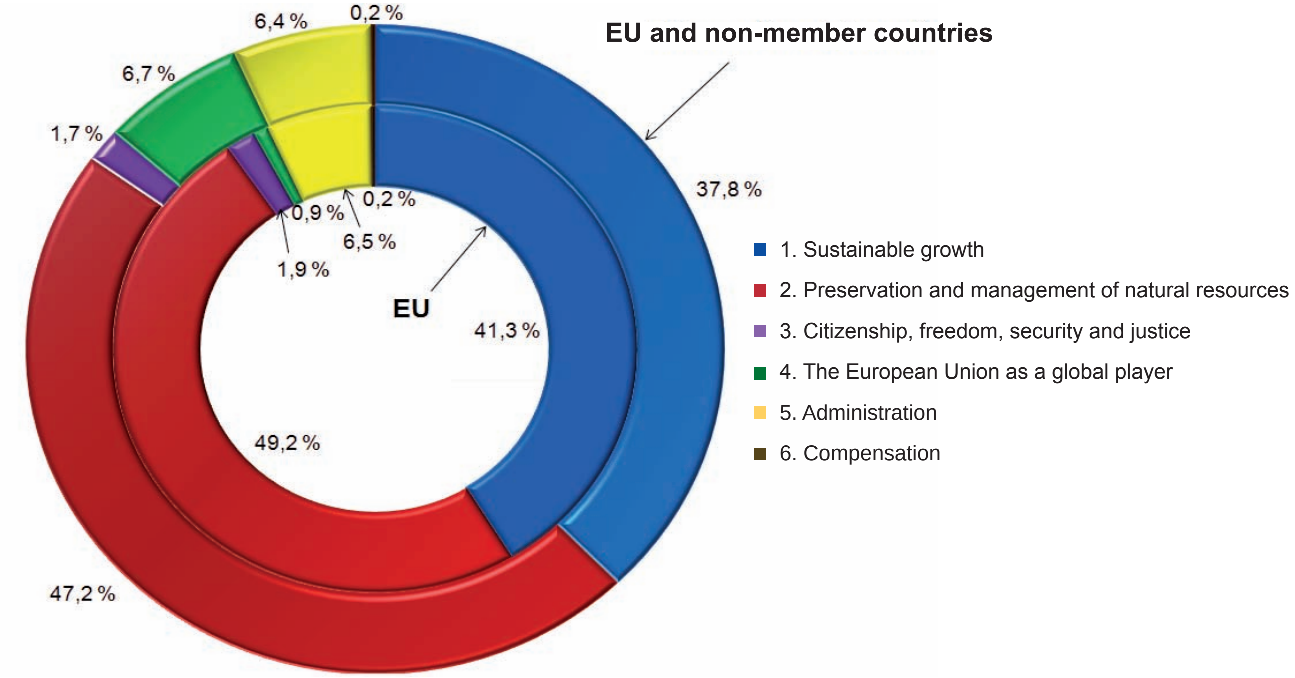
4) The EU as a global player, comprising all external policy measures, including pre-accession instruments. Graph 5 shows that most of the spending under this heading goes towards the EU's cooperation with third countries.

5) Administration, which includes the administrative expenses of all bodies, the pension system and European schools.

6) Compensations, earmarked for transfers to new Member States to balance their budget revenues and contributions.

Graph 5 breaks down the structure of EU budget spending in 2009 by the size of the headings. The inner graph contains data regarding payments provided solely to EU Member States and the outer graph shows the total costs of the EU budget, which amounted to almost €118.4 billion in 2009 (including the budget reserve earmarked for 2010).

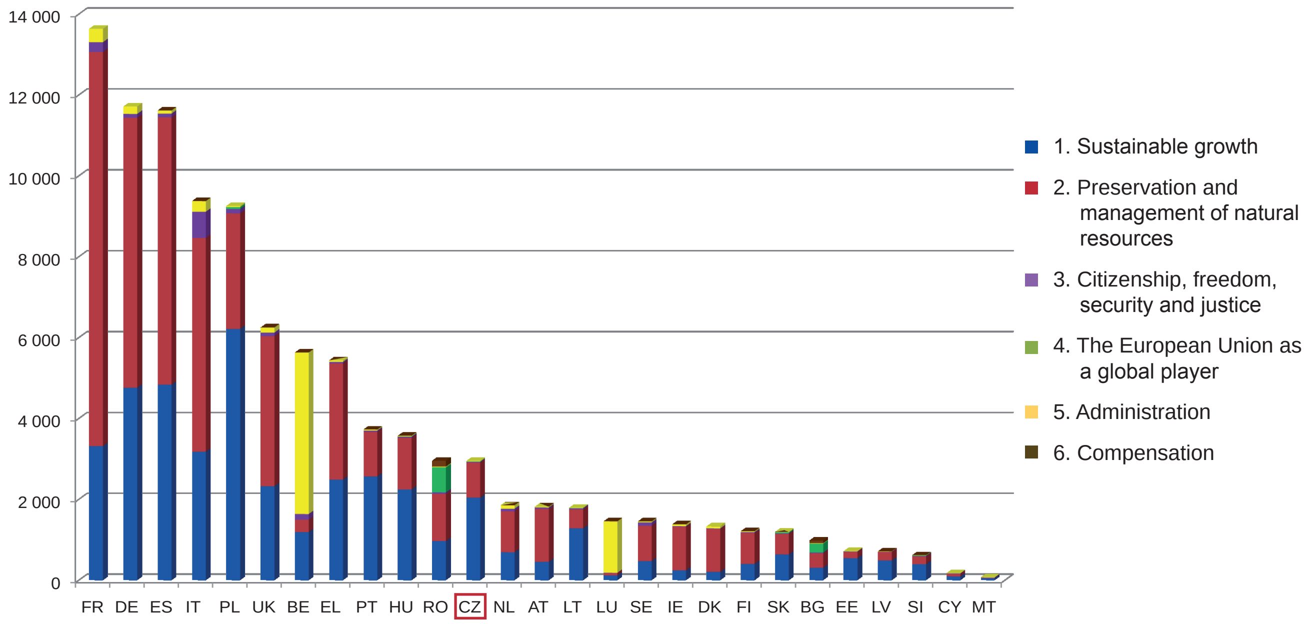
Graph 5: Share of expenditure headings in the EU budget in 2009 **(in %)**



Source: European Commission – EU budget 2009 – Financial Report.

The following graph depicts the level and structure of drawdown from the EU budget by Member States.

Graph 6: Drawing form the EU budget by individual Member States in 2009 **(€ million)**



Source: European Commission – EU budget 2009 – Financial Report.

A.2.3 The EU budget in relation to the Czech Republic

Joining the EU gave the Czech Republic an obligation to contribute to and an opportunity to draw funds from individual budget headings. Throughout its membership of the EU the Czech Republic has ranked as a "net beneficiary", i.e., a country whose revenue from the EU budget exceeds its contributions.

A.2.3.1 Contributions of the Czech Republic to the EU budget

The size of the Czech Republic's contribution to the EU budget grew every year up to 2009, when the impact of the financial and economic crisis was brought to bear. Table 2 shows the development of the Czech Republic's total contributions to the EU budget.

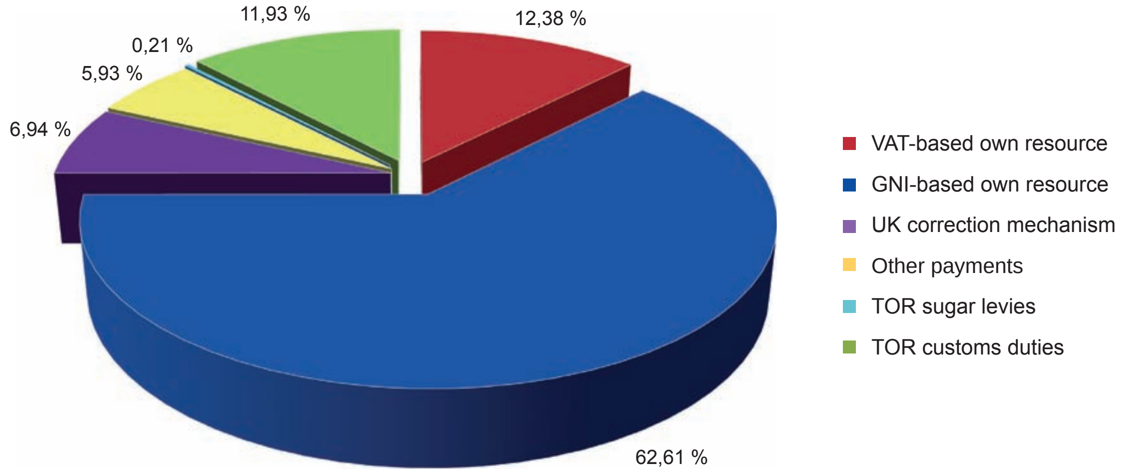
Table 2: Overview of Czech contributions to the EU budget in 2004–2009 **(€ million)**

	2004	2005	2006	2007	2008	2009
Traditional own resources	60.4	146.1	149.0	178.8	206.9	166.8
VAT own resource	80.1	150.6	173.7	199.9	221.4	170.0
GNI own resource	373.0	614.6	632.5	703.8	843.8	860.3
Correction mechanism	51.7	78.9	80.1	84.5	123.9	177.0
Total	565.2	990.2	1035.3	1167.0	1396.0	1374.1
Year-on-year growth		75.2 %	4.6 %	12.7 %	19.6 %	-1.6 %

Source: European Commission – EU budget 2009 – Financial Report.

The contributions, which reflect the state of Member States' economies, i.e. traditional own resources and VAT-based resources, fell in absolute terms below the 2007 level. The other components of total contributions to the EU budget increased commensurately. Graph 7 shows the detailed structure of the Czech Republic's contributions in 2009.

Graph 7: Share of Czech contributions to the EU budget in 2009



Source: European Commission – EU budget 2009 – Financial Report.

A.2.3.2 EU budget expenditure for the Czech Republic

Table 3 shows that, unlike contributions which fell slightly, drawdown from the EU budget continued to grow in 2009 despite a slowdown in the rate of growth.

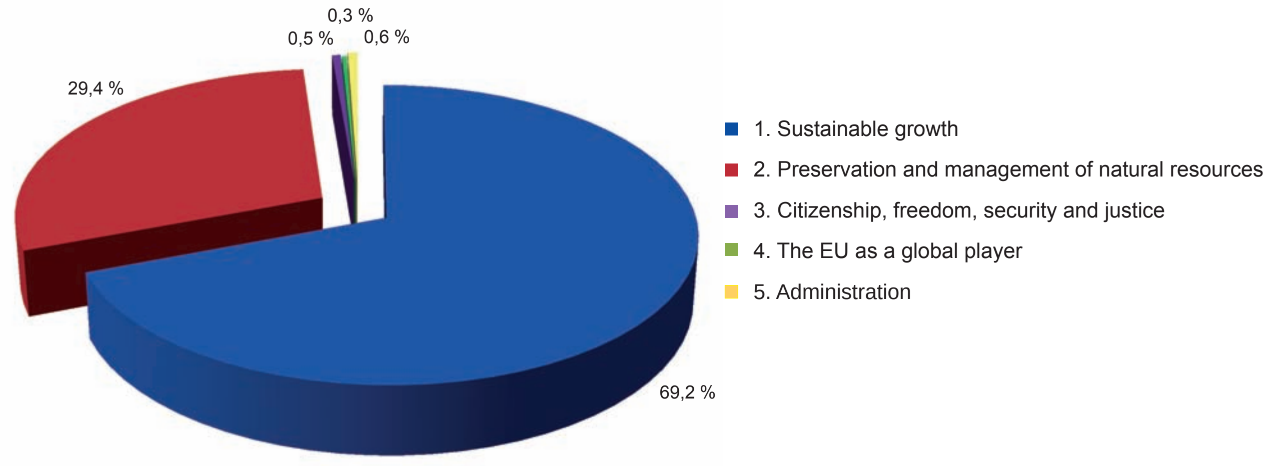
Table 3: Overview of EU budget funds provided to the Czech Republic in 2004–2009

	2004	2005	2006	2007	2008	2009
Total (€ million)	815.7	1,074.9	1,330.0	1,721.0	2,441.1	2,948.6
Annual growth (%)		31.8 %	23.7 %	29.4 %	41.8 %	20.8 %

Source: European Commission – EU budget 2009 – Financial Report.

The Czech Republic received the largest share of expenditure from the EU budget under the Sustainable Growth heading, which covers Cohesion Policy. This heading accounted for 69.2% of all the funds received, but compared to previous years this heading's share decreased as the share of Preservation and Management of Natural Resources, which covers the CAP, grew. Resources obtained under these two budget headings make up almost 99% of all EU budget expenditure flowing into the Czech Republic.

Graph 8: Share of EU budget expenditure in the Czech Republic in 2009 (in %)

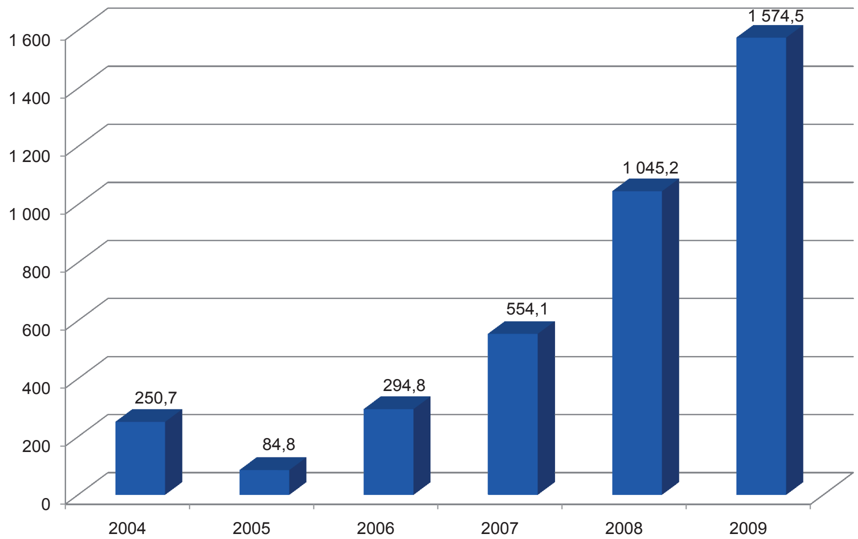


Source: European Commission – EU budget 2009 – Financial Report.

A.2.3.3 Net position of the Czech Republic in the EU

From the Czech Republic's accession to the EU to the end of 2009, the Czech Republic paid €6,527.4 million into the EU budget and obtained €10,331.5 million from it. That gave the Czech Republic a net position of €3,804.1 million. Graph 9 shows the development of the Czech Republic's net position in the years 2004 to 2009, based on official EU data. The year 2009 was affected by the continuing financial and economic crisis; nevertheless, increasing drawdown from the Structural Funds has increased the value of the Czech Republic's net position.

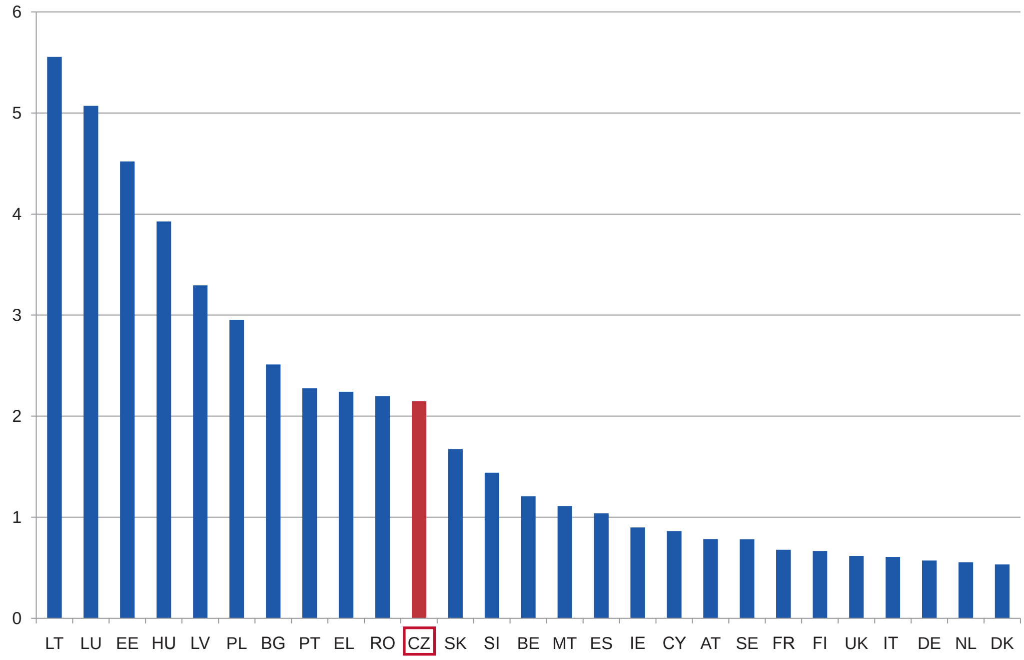
Graph 9: Net position of the Czech Republic in 2004–2009 (€ million)



Source: European Commission – EU budget 2009 – Financial Report.

The relative proportions of drawdown from the EU budget and contributions to the budget differ considerably from one Member State to another, as shown in Graph 10.

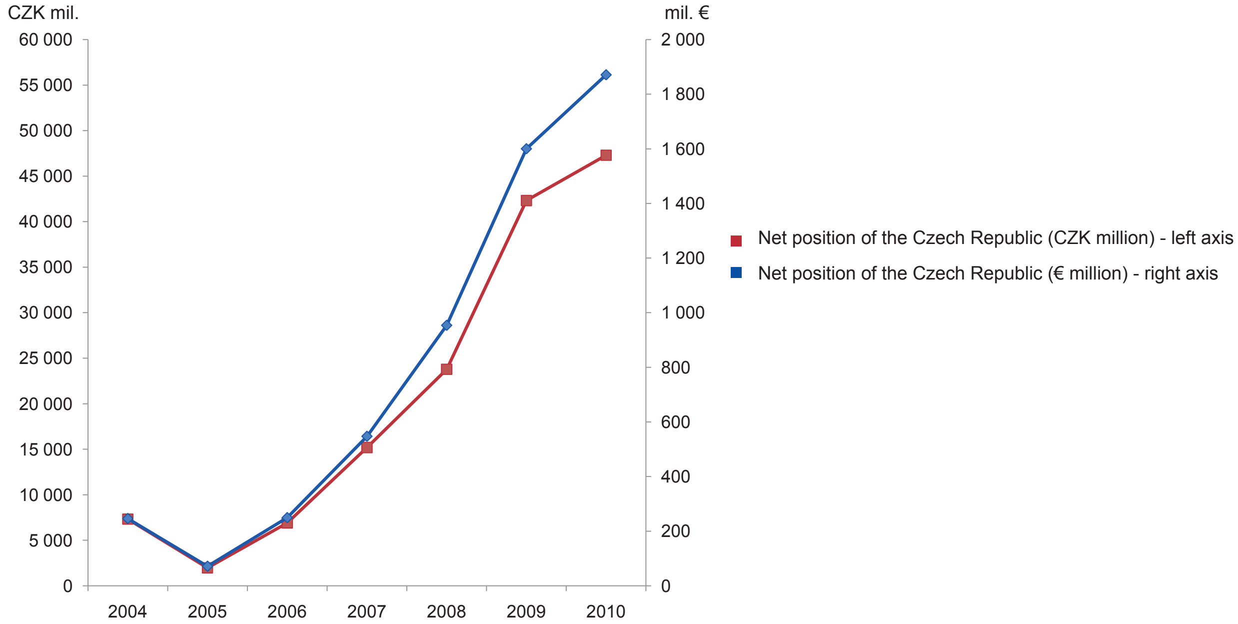
Graph 10: Proportion of drawdown from and contributions to the EU budget in 2009



Source: European Commission – EU budget 2009 – Financial Report.

Data from the Ministry of Finance provide more up-to-date information as they include data from 2010. Graph 11 shows clearly that the rate of growth of the net position slowed down in 2010, while the Czech Republic remained a substantial net beneficiary. The discrepancies between the graphs depicting the Czech Republic's net position in EUR and CZK are caused by changes in the CZK exchange rate: the Czech crown strengthened by CZK 1.2, approx. 5%, from 2009 to 2010, for example. The influence of the exchange rate was not so evident in the first years of the Czech Republic's membership of the EU, when the Czech Republic's net position in relation to the EU budget was below €300 million, but now, when it has almost reached €1.9 billion (€1.870 billion in 2010), the exchange rate is a significant factor.

Graph 11: Net position of the Czech Republic in 2004–2010 **(€ million and CZK million)**



Source: MoF, National Fund Department.

B. Sector matters

B.1 EU revenues

B.1.1 Measures to improve the fight against VAT fraud in the EU - current development

Taxes in general are a key source of public revenue. The most important tax for the working of the EU internal market is VAT. The estimated annual loss from VAT fraud in the EU is more than 12% of VAT-based revenue[37], which represents a budget loss of tens of billions of € over an entire programming period. The shortfall has to be compensated out of Member States' GNI-based resources[38]. This fact ultimately undermines the principle of equity. Constant attention is therefore paid to the fight against VAT fraud and various measures are adopted to prevent tax evasion. The following documents were adopted at EU level in 2010:

a) On 7 October 2010 **Council Regulation (EU) No. 904/2010 on administrative cooperation and combating fraud in the field of value added tax**[39] was adopted. This regulation lays down rules and procedures enabling the relevant authorities of Member States to cooperate and share all information that can help to assess VAT correctly, monitor the application of VAT, especially in the case of intra-Community transactions, and combat VAT-related fraud. It emphasises the use of electronic methods for working with information.

37 Report of the Economic and Monetary Committee of 17 July 2008 on a coordinated strategy to improve the fight against fiscal fraud.
38 ECA Special Report No. 8/2007 on administrative cooperation in the field of value added tax, point 2.
39 This Regulation repeals Regulation (EC) No. 1798/2003 on administrative cooperation in the field of VAT with effect from 1 January 2012.

The regulation will mainly affect:

- exchange of information upon request – governs the way the requested information is shared and the way enquiries necessary for information provision are conducted, including deadlines;
- information exchange without prior request – governs the procedure for transferring information if it is essential for the efficacy of the control system of the EU Member State of destination, if there is a reason to believe that a breach of VAT legislation has been or will be committed, or if there is a risk of a tax loss in the EU Member State of destination;
- the performance of simultaneous controls;
- the conditions for using information gained from third countries and the conditions on which information may be forwarded to third countries;
- the establishment of the electronic EUROFISC network for swift exchange of targeted information between Member States.

b) **Council Directive 2010/23/EU amending Directive 2006/112/EC on the common system of value added tax, as regards an optional and temporary application of the reverse charge mechanism in relation to supplies of certain services susceptible to fraud,** was adopted on 16 March 2010. Given the seriousness of VAT-related fraud, Member States are permitted to make temporary use of a mechanism shifting the tax payment obligation to, for example, a person to whom Assigned Amount Units are transferred within the meaning of Article 3 of Directive 2003/87/EC. The introduction of such a mechanism targeting services which, according to recent experience, are particularly susceptible to fraud, should not adversely affect the fundamental principles of the VAT system, such as fractioned payments.

c) **Council Directive 2010/45/EU amending Directive 2006/112/EC on the common system of value added tax as regards the rules on invoicing** was adopted on 13 July 2010. The conditions for sending electronic invoices were defined.

The fight against VAT fraud is also intensively dealt with by the EESC, whose "Opinion on the Proposal for a Council Regulation on Administrative Cooperation and Combating Fraud in the Field of Value Added Tax"[40] sets out the need for administrative cooperation in the fight against VAT fraud. It regards the creation of a common structure to combat VAT evasion (EUROFISC) as the most significant innovation, while simultaneously highlighting the need to establish cooperation and liaison with other bodies engaged in the fight against organised crime and money laundering.

The transfer of tax obligations is another important institute in the fight against fraud. In this context, the EESC issued an "Opinion on the Proposal for a Council Directive Amending Directive 2006/112/EC"[41], expressing agreement with the optional and temporary reverse charge mechanism for certain goods and services susceptible to fraud.

Although the VAT collection system has been modernised and simplified in the last ten years, the Commission came to the opinion that it has reached its limits. At the end of 2010, it therefore initiated a broad-based consultation process in the form of a set of questions[42]; the objective is to find a way to make the existing VAT collection system simpler, stronger, and more effective. Under the Commission's work programme, priority areas for further action should be presented at the end of 2011.

B.1.2 Measures to improve the fight against VAT fraud in the Czech Republic – current development

An amendment of the Act on VAT was passed on 9 February 2011. The amendment was promulgated under No. 47/2011 and entered into effect on 1 April 2011. It brings a whole series of changes, some of which are fundamental, and entirely new principles informed by the need to prevent VAT evasion. The main changes are:

- VAT deductions can be only claimed once the payer is in possession of a tax document;
- a buyer will be liable for payment of VAT in the case he knew, or should and could have known, that the supplier would not pay VAT;
- the place of performance of selected services (e.g. sport, culture, science, or education) will now be in the State in which the services are provided;

40 EESC Opinion 2010/C 347/11 of 17 February 2010.
41 EESC Opinion 2010/C 339/09 of 21 January 2010.
42 Green Paper, COM(2010) 695 final of 1 December 2010.

- in the case of failure to register, VAT is determined in an alternative manner, i.e. from the sum of all payments made without VAT;
- introduction of the reverse charge mechanism in the Czech Republic; this should apply to the supply of gold, metal scrap, emission allowances, and certain building and assembly work;
- an alteration of the method for deducting VAT in the case of a change in the use of assets;
- a restriction on the set of persons who may create a group registration.

B.1.3 Report on the audit on VAT administration carried out in cooperation with the SAI of Federal Republic of Germany

A follow-up audit of VAT administration was performed in 2009 under an agreement between the supreme audit institutions of the Czech Republic and the Federal Republic of Germany. The findings from this audit are set out in the *EU Report 2010*. *Administration of Value Added Tax in the Czech Republic and the Federal Republic of Germany - Follow-up Audit Report*[43]was drawn up in cooperation with Bundesrechnungshof's auditors in 2010. The follow-up audit report contains an assessment of progress in the implementation of the recommendations formulated in the joint report on the results of the parallel audits published in 2008. It also contains an assessment of VAT administration in the two countries as regards international assistance in recovering arrears and VAT administration in relation to large taxpayers. The two supreme audit institutions assessed progress in the implementation of the recommendations as follows:

- Recommendation 1: *The conditions for registering payers should be harmonised in the EU* – the two SAIs stated with regret that the idea of common minimum standards for registering and de-registering VAT payers had been abandoned. They continue to regard this objective as relevant to the prevention of fraudulent conduct in the field of VAT, however.
- Recommendation 2: *Monthly filing of recapitulative statements* – this measure was implemented in the Czech Republic through the Act on VAT with effect from 1 January 2010; in Germany, it was implemented on 1 July 2010, the difference being that whereas the Czech Republic, in line with the EU regulations, introduced an obligation to file recapitulative statements on a monthly basis as per the defined calendar, Germany did not.
- Recommendation 3, concerning solely the German side: *Pairing data in VAT returns and recapitulative statements in Germany with a view to achieving greater reliability of data in the VIES system and considering combining the two systems for VAT returns and recapitulative statements* – the German tax administration accepted the BRH's recommendation and set up a working group to examine possible solutions. The work is still ongoing and the BRH will keep a close eye on further developments.
- Recommendation 4: *Sharing successful criteria, components, and approaches to the risk management system in the EU* – the Czech Republic and Germany use different risk management systems, each with its own strengths and weaknesses. In this area, the SAO performed an audit of the EUROCANET[44] information exchange system, while the BRH concentrated on German involvement in the "Risk Management Platform". Germany uses different tried-and-tested tools to identify high-risk VAT payers and for that reason has not yet actively participated in EUROCANET.

In the field of international assistance in the recovery of unpaid VAT, all EU Member States follow the same European legislation, so the way in which requests for international assistance in recovering unpaid VAT are handled is the same in the Czech Republic and Germany. The SAO and BRH performed a comparison of the statistics for 2006-2008 that both Member States submitted to the Commission. The data contained in these statistics did not match. The SAO and BRH consider it advisable to reopen at EU level the debate on statistical reporting methods so that the statistics become comparable. They also share the opinion that reliable statistics should contain more information about VAT. Based on more detailed statistics, the Commission should draw up an analysis to help Member States to step up the effectiveness of their fight against VAT fraud. According to the opinion shared by the SAO and BRH that could help the Member States that are relatively unsuccessful in recovering unpaid VAT to attain the EU average.

43 Administration of Value Added Tax in the Czech Republic and the Federal Republic of Germany - Follow-up Audit Report, available at www.nku.cz, in the section "Publikace, dokumenty/Ostatní publikace".

44 EUROCANET - European Carrousel Network

The SAO and BRH also analysed the legal situation concerning VAT control in the case of large taxpayers in both countries. In addition, they gathered information from a questionnaire addressed to tax administrators concerning the areas they view as crucial for managing this issue. The responses obtained clearly indicate that the situation in the two countries is developing differently. To guide the selection of susceptible cases, the Czech Republic has created a system based on a large volume of relevant data (e.g., information from conducted tax inspections, data from balance sheets and profit and loss accounts). This ensures effective management and analysis of VAT control in general. A specialised tax office for large taxpayers is planned to be established in 2012. No such system exists in Germany yet, where attention is focused on the selection of individual relevant cases, primarily based on data from VAT returns and recapitulative statements. Analysis of these data is based on various risk management components, which will be strengthened. To conclude, the SAO and BRH expressed the expectation that the audit results will initiate a debate on approaches and strategies within Member States, between the Member States, and in the European Commission.

B.1.4 Protection of the EU's financial interests in the field of revenues and the fight against fraud

In the interests of strengthening the protection of the EU's financial interests, **Council Directive 2010/24/EU concerning mutual assistance for the recovery of claims relating to taxes, duties and other measures** was adopted on 16 March 2010. This directive fully replaces Council Directive 2008/55/EC with effect from 1 January 2012.

The directive emphasises the adoption of a uniform instrument to be used for enforcement measures in the requested Member State, as well as the adoption of a uniform standard form for notification of instruments and exchange of information without prior request concerning specific tax refunds. A general obligation to communicate requests and documents in digital form or via an electronic network is laid down, along with precise rules on the use of languages etc.

EUROSAI also pays considerable attention to the fight against fraud. A seminar on new approaches to tax evasion and VAT fraud was staged in Ljubljana from 6 to 9 June 2010. The participants in the seminar concurred on the need for intensive cooperation between SAIs and tax and customs administrations at national and international level; such cooperation is crucial to a successful fight against VAT fraud and reducing tax evasion.

A follow-up seminar on new approaches to the grey economy and possible IT solutions was held in Moscow from 8 to 10 November 2010. The participants confirmed the need for intensive cooperation between SAIs and tax and customs administrations at national and international level and stressed the need to make use of IT to analyse and check State budget revenues. The participants also agreed on the need to improve the IT skills of tax administration staff and SAI auditors and to broaden cooperation with IT experts in the fight against tax evasion.

B.2 Agriculture and natural resources

The preservation of natural resources, encompassing agriculture, fisheries policy, rural development and environmental protection measures, has been for long the biggest EU budget heading in terms of expenditure.[45]

B.2.1 Drawdown of finances for CAP and CFP measures in the Czech Republic in 2009

There were no changes to the CAP implementation structure in the Czech Republic in 2009. In 2009, almost CZK 40,884 million was paid out in the Czech Republic under the CAP; of that amount the national share was approx. CZK 15,540 million and EU co-financing approx. CZK 25,344 million. The following table shows expenditure in individual sectors of the CAP.

45 In the EU budget for 2009, this heading accounted for more than 45% of total expenditure, in absolute terms almost €51 billion.

Table 4: Overview of SAIF funds paid out for the main areas of the CAP in the Czech Republic in 2009 **(CZK million)**

Expenditure	Paid out funds		
	Czech Republic	EU	Total
Direct payments	10,027.723	15,029.340	25,057.063
Common Market Organization	2,274.816	2,019.775	4,294.591
Rural Development Plan	1,774.418	5,945.177	7,719.595
Horizontal Rural Development Plan	595.072	2,346.738	2,941.810
OP RDMA	0.085	0.337	0.422
Promotion of honey consumption	0.337	0.844	1.181
Promotion of organic farming	3.393	2.458	5.851
Loan financing – intervention buying	863.578	0	863.578
Total	**15,539.422**	**25,344.669**	**40,884.091**

Source: Annual Report of the SAIF for 2009 – parts 4.1 – 4.2.

B.2.1.1 Direct Payments

The following table shows a breakdown of the finances paid out in the biggest heading by volume – direct payments – in 2009:

Table 5: Overview of SAIF funds paid out for direct payments in the Czech Republic in 2009 **(CZK thousand)**

Direct payments	Paid out funds		
	Czech Republic	EU	Total
SAPS	0	13,770,915	13,770,915
Top-Up	10,027,723	0	10,027,723
Separate Sugar Payment	0	1,211,681	1,211,681
Energy crops	0	32,224	32,224
Separate Tomato Payment	0	14,520	14,520
Total	**10,027,723**	**15,029,340**	**25,057,063**

Source: Annual Report of the SAIF for 2009.

In 2009, the simplified system of direct payments, the Single Area Payment Scheme (SAPS), was still applied in the Czech Republic. The amount of funds provided to support beneficiaries from EU sources continued to be topped up from national sources to the level of direct payments in EU states that joined before 2004 (Top-Ups). A separate tomato payment was added as another direct payment in 2009.

B.2.1.2 Common Market Organization

One of the principal and oldest common agricultural policy mechanisms is CMO, which covers primary production[46] and products after primary processing. The role of CMO is to regulate the supply of products in a way preventing fluctuations in the supply and thus also in the prices paid to agricultural producers and the prices paid by processors or end consumers for these products. Various mechanisms are used to this end, for example production quotas, intervention buying, storage support, intervention selling, export subsidies, financial aid and appropriations, guarantees, and other payments.

46 Vegetable and animal products intended for further processing.

Table 6: Overview of SAIF funds paid out for CMO in the Czech Republic in 2009 **(CZK thousand)**

Type of measure	Paid out funds		
	Czech Republic	EU	Total
Financial Support	33,349	73,454	106,803
Export Subvention	21,623	163,752	185,375
Subsidies and levies	1,264,322	1,634,481	2,898,803
Intervetion	944,469	148,084	1,092,553
Other expenditure	11,053	4	11,057
CMO in total	**2,274,816**	**2,019,775**	**4,294,591**

Source: Annual Report of the SAIF for 2009.

B.2.1.3 Rural Development Programme

The following table gives an overview of the amounts spent on the RDP in 2009:

Table 7: Overview of funds paid out for RDP in 2009 **(CZK thousand)**

		Description	Czech Republic	EU	Total
Axis of the RDP	I	Improving the competitiveness of agriculture and forestry	651,840	1,955,520	2,607,360
	II	Improving the environment and landscape	593,699	2,374,727	2,968,426
	III	Quality of life in rural areas and diversification of rural economy	494,295	1,482,884	1,977,179
	IV	Leader	28,292	113,169	141,461
	V	Technical assistance	6,292	18,877	25,169
		TOTAL	**1,774,418**	**5,945,177**	**7,719,595**

Source: Annual Report of the SAIF for 2009.

As in the previous year, the greatest volumes of finances were paid out for *Agri-environmental measures* and Less Favoured Areas (both measures are part of Axis II), *Farm Modernisation* (Axis I) and *Renewal and Development of Villages, Civic Amenities and Services* (Axis III).

B.2.1.4 Other measures

- no expenditure was certified under **OP Fisheries** (2007-2013 programming period) up to the end of 2009;
- under the **Horizontal Rural Development Plan** (2004-2006 programming period) applications that were added to the programme up to the end of 2006 were paid, as these were multi-year commitments;
- payment for projects under **OP Rural Development and Multifunctional Agriculture** (2004-2006 programming period) was completed as of 31 December 2008. As it had not been possible to pay all the phases of projects (one forestry phase and five phases of follow-up care for established green cover), the remaining phases were paid in 2009 as well;
- as in the previous year, funds were also paid in 2009 on **agricultural product promotion**, EU co-financed, with a view to improving the marketing and sales of agricultural and food products;
- as regards intervention buying of agricultural commodities, **credit** provided by financial institutions was used according to the Act on the SAIF[47] and the relevant EU regulations.

B.2.2 Audits in the field of CAP and CFP

Two audits targeting the CAP and CFP were completed by the SAO in 2010. The first audit was added to the Audit Plan under the name “Support for Fisheries in the Czech Republic under Operational Programmes in the years 2004 to 2008”. The results of this audit were published in the first quarter of 2010 and were commented on in *EU Report 2010*. The other audit concerned the economy of spending on CMO measures. With the ECA, the SAO launched a pilot project of a coordinated audit, whose results should be used in drawing up DAS 2010.

47 Act No. 256/2000, on the State Agricultural Intervention Fund and amending certain other acts.

B.2.2.1 Funds earmarked to cover the costs of market interventions and export subsidies under Common Market Organisation

The aim of the audit[48] was to examine whether State budget and EU finances earmarked to cover the costs of market interventions and export subsidies in the context of the CAP were provided in compliance with the defined conditions and in an economical manner. In the audited period of 2007-2009, CZK1,890.5 million was spent on covering the costs of market interventions, food aid for the poorest and export subsidies. The SAO audited more than 27% of that amount. Revenues of CZK219.43 million from intervention sales were also subjected to scrutiny. The State budget and EU finances earmarked to cover the costs of interventions and export subsidies were essentially provided in compliance with the defined conditions and the implementation and control system for providing these finances was judged to be functional. The auditees were nevertheless found to have been in breach of certain regulations.

In some cases, the Ministry of Agriculture did not proceed in line with the Act on financial control[49], e.g., by:

- insufficient exercise of ex ante public administration control;
- failure to declare certain significant facts concerning an assessment of the proportionality and effectiveness of the introduced financial control system in its annual reports on the results of financial control;
- failure to make a systematic assessment of the progress in implementing measures adopted on the basis of findings made by foreign audit missions;
- failure to adopt measures in response to certain important findings made by internal audit.

As the accredited paying agency, the SAIF in some cases did not proceed in line with the relevant legislation, e.g. by:

- not rejecting non-standard supplies of skimmed milk powder that did not satisfy the requirements of Commission Regulation (EC) No. 214/2001;
- not demanding that storage operators submit to it monthly stock statements by the specified deadline in line with Commission Regulation (EC) No. 884/2006 and failing to impose penalties for breach of this obligation;
- failing to secure the signature of the auditee on certain control protocols, as required to do by Commission Regulation (EC) No. 884/2006 and the Act on State Control[50].

The programme of food aid for the poorest members of society was not designed in a way enabling wider use of this aid in the Czech Republic.

B.2.2.2 Coordinated audit

Based on a Memorandum of Understanding between the SAO and the ECA[51] on a pilot project on coordinated audits, an audit was begun with a view to checking whether State budget and EU finances earmarked for improving the environment and landscape (Axis II, Rural Development Programme for 2007-2013) were provided in accordance with the stipulated conditions.

Coordinated audit plans/programmes had been jointly elaborated by July 2010, including checklists that were used in the audit. From August 2010 to February 2011, a basic audit investigation was conducted to obtain adequate evidence for the audit's subject matter, so that a report could be filed on the following:

- the legality and regularity of the performed operations;
- the effectiveness of the management and control system in terms of preventing or detecting errors and correcting them in the context of the legality and regularity of performed operations.

At the time when this report was being drawn up, the on-the-spot audit was in its completion phase. At that point it was expected that the SAO and ECA auditors would agree on the formulation of the draft audit results based on the evidence obtained, the audit documentation[52] and the resolution of objections raised by the auditees. It was expected that this pilot project would be completed in May 2011. The ECA can use the results of the coordinated audit as a basis for DAS 2010.

48 Audit No. 10/01, Issue 4/2010 of the SAO Bulletin
49 Act No. 320/2001, on financial control in public administration and amending certain acts (the Act on Financial Control).
50 Act No. 552/1991, on State control.
51 Memorandum of Understanding between the Nejvyšší kontrolní úřad and the European Court of Auditors on a pilot project on coordinated audits, signed on 14 July 2010.
52 Statement of Preliminary Findings and/or Audit Protocols.

B.2.3 Audit work by EU bodies

B.2.3.1 Annual Reports of the European Court of Auditors concerning the financial year 2009

On 9 November 2010, the Official Journal of the EU published the ECA's Annual Reports on the EU budget for 2009. The report contains, among other things, the following key information regarding agriculture and natural resources:

- The ECA considered payments to be materially affected by errors, with the estimated error rate increasing from 2008 (estimated at 2-5%). The ECA regards the control and supervisory systems as only partially effective. Although the IACS is in principle a well-designed system and its introduction has brought significant improvements in administration, inaccurate data in databases, incomplete cross checks and incomplete follow-up of anomalies continue to be a problem.
- The rules governing rural development should be simplified further. Findings from the Czech Republic were mentioned among those, too. The ECA performed an assessment of the supervisory and control systems for Rural Development Programmes (EAGGF expenditure) in eight Member States, with the result that only the systems in the Czech Republic and two other countries were deemed effective. The supervisory systems covering this area in the other five states were only rated as partially effective.

The Czech Republic was mentioned in the context of errors in the determination of exchange rates during the transfer of EAFRD finances. The financial impact of these errors has already been corrected in the subsequent reporting statements.

B.2.3.2 ECA's special reports

B.2.3.2.1 Special Report No. 5 – Implementation of the Leader approach for rural development

Leader is an approach for implementing EU rural development policy via LAGs[53]. LAGs are associated with specific costs and risks but have the potential to create added value through a bottom-up approach and strengthening partnership. In its special report No. 5, the ECA mentions the following deficiencies:

- LAGs applied the Leader approach in a way that limited the potential for added value;
- LAGs awarded grants to projects without duly assessing their efficiency;
- procedures were not always transparent and did not sufficiently demonstrate that the LAGs took decisions on an objective basis, free from conflicts of interests;
- the Commission has not yet demonstrated the efficiency and effectiveness of expenditure, the added value achieved through following the Leader approach, the extent to which the known risks have materialised, or the real costs of implementation.

The Czech Republic was not scrutinised and is not mentioned specifically in the special report. The SAO audited the application of the Leader approach in 2008. The SAO audit found certain deficiencies that are consistent with the statements in the ECA special report, such as: monitoring indicators not sufficiently precise or incomplete; insufficient timetables for project implementation; and, in approx. 7% of the audited entities, no minimum time limits for coupling projects to the specified purpose. Moreover, the fact it was often unclear which version of the LAG Rules and LEADER+ Rules were applicable to specific cases did not benefit transparency.

B.2.3.2.2 Special Report No. 6 – Has the reform of the sugar market achieved its main objectives?

In 2006, the EU launched a far-reaching reform of the sugar sector with a view to making the sector competitive and stabilising markets while respecting international commitments. The reform consisted in reducing prices and a 30% reduction in overall production under quota, which led to the closure of 80 sugar factories. A restructuring fund and diversification support were established to mitigate the social and economic impacts of these measures. The ECA conducted an audit to verify whether the reform's objectives had been achieved. The ECA stated that the objective of reducing production to six million tonnes had largely been achieved and that prices on the EU sugar market had been stable so far. In the audit, which was conducted in eight Member States including the Czech Republic, the ECA identified a number of deficiencies and risks, for example:

- quotas were given up also by competitive factories;
- the current quota system has retained the previous system's rigidity and constraints;

53 A Local Action Group (LAG) may be, e.g., a public benefit company or a citizens' association.

- the level of production quotas is below the level of EU consumption and the EU is a net importer; the relocation of production facilities away from the EU has created a risk of dependency on imports, along with the associated negative impacts on the social structures of the affected areas;
- it is unlikely that the benefits of the reduction in the sugar price are passed on to consumers – most of the money saved is added to the profit margin of producers or distribution networks abusing their market strength;
- there are major differences in the level of restructuring support after deducting direct dismantling costs, because there was no clear specification as to what costs should be included in restructuring plans;
- diversification support was awarded according to very different criteria in different countries;
- no evidence was found that sugar refineries received support on the basis of objective criteria;
- the reform was designed to be budget-neutral – it is likely, however, that the total EU budget costs for the sugar sector will be **€1.2 billion higher** in the 2007-2013 period**.**

B.2.4 Protection of the EU's financial interests in the CAP area

B.2.4.1 Development trends

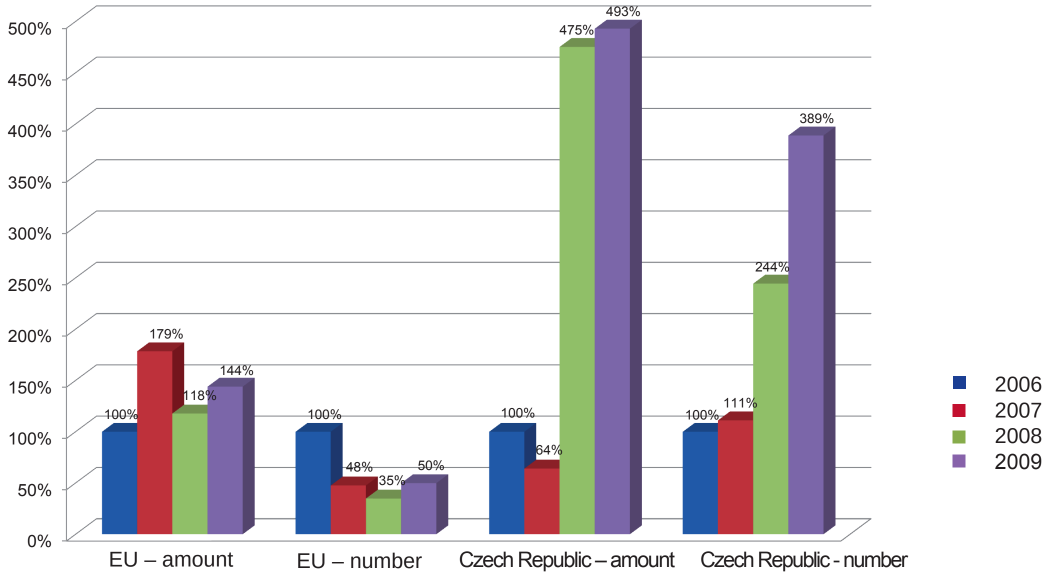
Under the scheme introduced by Commission Regulation (EC) No. 1848/2006, in 2009 Member States reported 1,621 new irregularities with a financial impact of €125 million, which represented 0.24% of the EU's agriculture budget (the rate in 2008 was 0.21%). Of that number, the Czech Republic reported 35 new irregularities with a financial impact of €793,000, i.e., 0.09% of agricultural expenditure in the Czech Republic. The following table and graph show the development trend for the number of irregularities and their financial impact.

Table 8: Number of irregularities and amount of financial impact in € since 2006

	2006		2007		2008		2009	
	Financial impact	Number	Financial impact	Number	Financial impact	Number	Financial impact	Number
EU	86,824,768	3,249	154,993,326	1,548	102,259,365	1,133	125,025,951	1,621
Czech Republic	160,915	9	103,168	10	764,680	22	793,364	35

Source: Report from the Commission to the Council and the European Parliament - Protection of the European Union's financial interests - Fight against fraud - Annual Report 2009.

Graph 12: Amount of financial impact and number of irregularities in the EU and in the Czech Republic in 2006 – 2009 (year 2006 is equal to 100 %)



Source: Report from the Commission to the Council and the European Parliament - Protection of the European Union's financial interests - Fight against fraud - Annual Report 2009.

The expectation[54] that the number of irregularities and their financial impact would fall was not realised in 2009. The Commission believes that the increase is caused by the introduction of IMS, which enables immediate reporting of irregularities via the Internet.

B.2.4.2 Impacts of irregularities on the EU budget in the years 2006-2009

Spending on the CAP in the years 2006-2009 attained a sum of €201 billion. €2.6 billion of that amount, i.e., 1.28% fell to the Czech Republic. 0.05% of the total volume of expenditure in the Czech Republic was affected by irregularities in that period; that is consistent with the EU average.

The following sectors displayed a higher level[55] of irregularities in the years 2006-2009: sugar (0.71%), pork, eggs and poultry (0.51%), rural development (0.29%), fruit and vegetables (0.27%), and promotion (0.23%).

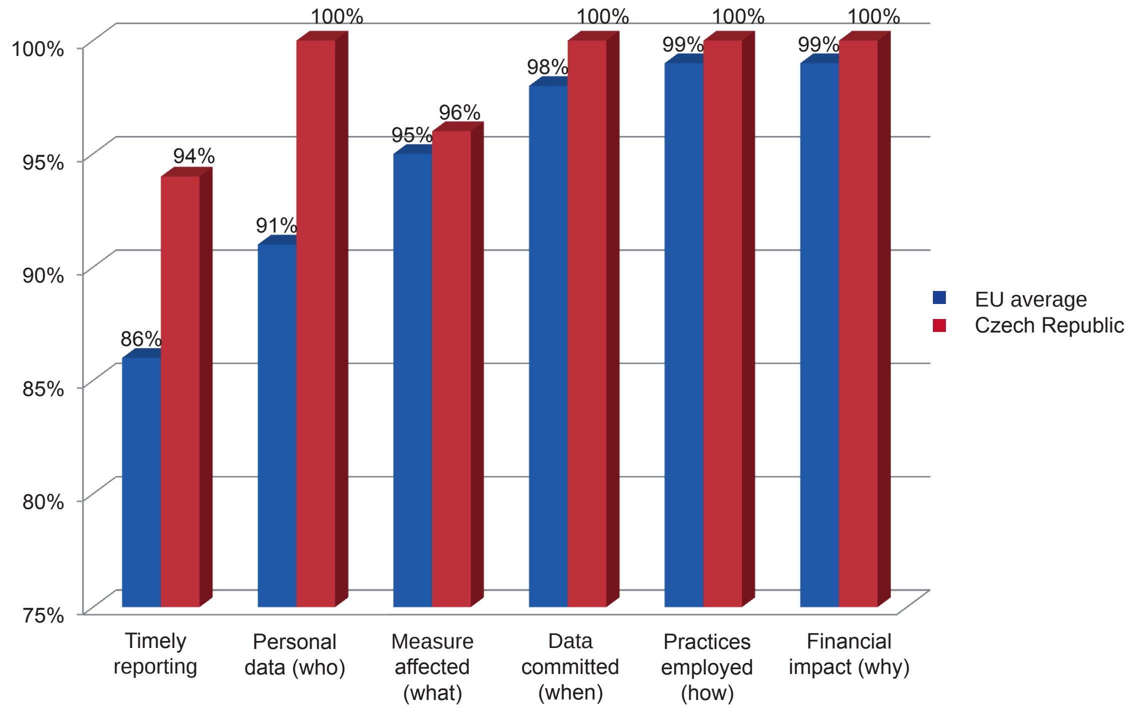
On the other hand, it continues to apply that a lower level of irregularities is found in the direct payments sector (0.01%)[56], which accounts for 55% of CAP spending. Food programmes also displayed a low rate (0.01%).

A total of €528,504 was paid back into the EU budget in 2009; a further €42,955 was declared non-refundable, and at year end, €457,252 remained to be returned, accounting for 0.04% of the total sum of €1,136,175,204 that was due to be paid back by all Member States. That rate is among the lowest in the EU.

B.2.4.3 Fulfilment of obligations related to reporting irregularities

The quality of reporting again improved in 2009 for the EU as a whole and for the Czech Republic: the average rate of fulfilment of the data content requirements was put at 95% (78% in 2007, 92% in 2008). Most Member States, including the Czech Republic, achieved a rate of fulfilment exceeding 90%. The following graph gives a comparison of the Czech Republic and the EU average:

Graf 13: Reporting discipline relating to irregularities communicated as regards expenditure for agriculture and fisheries in 2009 **(in %)**



Source: Report from the Commission to the Council and the European Parliament - Protection of the European Union's financial interests - Fight against fraud - Annual Report 2009.

54 Page 30 of Annex to the 2008 Report from the Commission on the protection of the European Communities' financial interests and the fight against fraud - Statistical evaluation of irregularities- own resources, agriculture, structural measures, pre-accession funds and direct expenditure - year 2008, SEC(2009) 1003 of 15.7.2009.

55 The rate is the percentage of the total volume of expenditure in the sector accounted for by the financial volume affected by errors.

56 These payments are covered by the IACS system, which is deemed a reliable control system. One reason for this fact is that a large quantity of direct payments to farmers does not exceed €10,000. If irregularities are found, these payments therefore do not satisfy the minimum value limit for the reporting duty (they are only reported if there is a suspicion of fraud in the case at hand).

Shortcomings in reporting nevertheless persist in the timely reporting (as the graph shows this is the biggest weakness affecting the Czech Republic's reporting) and in the measures affected.

B.2.5 Seminar on CAP audit

The SAO and ECA co-organised a seminar of EUROSAI and the Contact Committee of the the Heads of the SAIs of the EU Member States and of the ECA on 25-27 October 2010 under the name "**Experience with the development and carrying out CAP audits**". The seminar, detailed materials on which are available at www.nku.cz, focused on the following topics:

- audit of the CAP and its position within the audit activities of SAIs;
- planning and coordination of a CAP audit;
- techniques and methods of a CAP audit ;
- treatment of errors found by a CAP audit;
- possibility of performance audit of the CAP.

For all these topics, the main aim was to share experience and information, resolve the tasks facing CAP audits, and formulate and state the problems that cannot be resolved at an event of this type but which need to be debated.

Besides representatives of the SAO and the ECA, representatives from 22 SAIs attended the seminar. Representatives of the European Commission, the Ministry of Agriculture, and the SAIF as the paying agency for the CAP in the Czech Republic were invited.

Presentations concerning the experience of individual Member States in auditing the CAP, differences in approaches to assessing irregularities found by CAP audits, and presentations focusing on the coordination of these audits were particularly beneficial.

Above all, the seminar highlighted the need for better coordination and planning of audits to prevent duplication and overlaps with other audits performed by various authorities (e.g., the Commission, ECA, SAIs).

The possibility of introducing a "uniform audit model" for CAP audit in Member States was also discussed during the seminar, which could lead to a reduction in the number of on-the-spot checks performed by the ECA or in the number of Commission visits to Member States' paying agencies.

Discussion on the classification and assessment of irregularities revealed the different approaches taken by different audit bodies and the need to create a single methodology for classifying and assessing the deficiencies found, which could be applicable by all audit bodies and Member States.

The presentations focusing on the exchange of experience with performance audit revealed that with regard to the CAP most SAIs perform compliance audit or audit of sound financial management rather than performance audit. For a performance audit to be done successfully sufficient time should be paid to examining the key items of the audit and all the available techniques for achieving the best possible audit results should be used.

In a questionnaire-based survey conducted at the end of the seminar, 90% of the participants stated that the seminar's agenda was consistent with the specified goals.

B.2.6 CAP towards 2020

At the beginning of 2010, the Commission launched a public debate on the CAP. The following aims were formulated for this policy:

- **viable food production** (ensuring sufficient and safe foodstuffs in the context of growing global demand, economic crisis, and much greater market volatility);
- **sustainable management of natural resources and climate action** (farmers often have to put environmental considerations ahead of economic considerations but such costs are not rewarded by the market);
- **maintaining the territorial balance and diversity of rural areas** (agriculture remains a major economic and social driving force in rural areas and an important factor in maintaining a living countryside).

In November 2010, the Commission published a Communication[57] entitled "The Common Agricultural Policy towards 2020: Meeting the food, natural resources and territorial challenges of the future", which looks at future CAP instruments suitable for achieving its objectives.

- In the case of direct payments, the Communication highlighted the importance of redistribution, redesign, and better targeting of support based on objective and equitable criteria and with a view to making them more understandable to the taxpayer. These criteria should have both economic aspects (referring to the fact that direct payments act as "income support") and environmental aspects (taking into account the public goods that farmers provide); and the support should be better targeted at active farmers.
- As far as market measures are concerned, such as public intervention and support for private storage, there is a need to streamline and simplify them, and for introducing new policy elements to improve the functioning of the food supply chain. Although these mechanisms have been traditional instruments of the CAP, the reforms would gradually strengthen the market orientation of agriculture in the EU and the mechanisms would be restricted to safety-net measures to the extent that public stocks basically no longer exist. Whereas in 1991 market measures accounted for 92% of the CAP costs, in 2009 they took up just 7% of the CAP budget.
- **Rural development** policy has reinforced the economic, environmental, and social sustainability of the farm sector and rural areas, but there are strong calls for the aspects of **the environment, climate change, and innovation** to be fully integrated into all programmes horizontally. Attention is paid to the importance of direct sales and local markets and the specific needs of young farmers and new entrants. The integration of the Leader-based approach will continue. One new element in the future rural development policy should be **a risk management toolkit** to deal more effectively with income uncertainties and market volatility.

In an annex to the Communication the Commission published three broad policy options for the CAP. The options are listed in Appendix 2 to this EU Report 2011.

B.3 Cohesion

Within the meaning of Article 174 of the Treaty on the Functioning of the European Union, Cohesion Policy is an instrument for strengthening the EU's economic, social, and territorial cohesion, which aims at reducing disparities between levels of the development of various regions and the backwardness of the least favoured regions of the EU. In 2009, its share of budget expenditure was almost €34 billion, i.e., approx. 30.3% of total spending. This sum was the largest expenditure item in the EU budget after the "Preservation and Management of Natural Resources" heading.

B.3.1 Current developments in Cohesion Policy in the Czech Republic

B.3.1.1 2004-2006 Programming Period

By a decision of the Commission of 18 February 2009, the Czech Republic was enabled to continue drawing down finances allocated from the Structural Funds for the 2004-2006 programming period until 30 June 2009. The Czech Republic made use of this option for almost all OPs (with the exception of OP RDMA), for both single programming documents and for the Equal initiative.

B.3.1.1.1 State of drawdown of the allocation from the Structural Funds as of the close of accounts

The Czech Republic's total allocation in the 2004-2006 programming period was €1,692.595 million (i.e., approx. CZK 42 billion[58]). These funds were provided out of four Structural Funds (ERDF, EAGGF, ESF and FIFG). The following table shows the allocation and drawdown.

57 IP/10/1527 – source: http://ec.europa.eu/agriculture/cap-post-2013/communication/index_en.htm.
58 Using the European Central Bank's exchange rate for September 2010 (i.e., 24.808 CZK/€).

Table 9: Spending of allocation in the programming period 2004–2006 as of 31.12.2010

Operational programme	Allocation 2004–2006	Date of account closure	Statement of expenditure as of account closure day	Spent from allocation after inclusion of 10% flexibility		Not spent
	€		€	€	%	€
Joint regional OP	454,332,571	30.6.2010	456,115,706	452,905,428	99.7 %	1,427,143
OP Rural Development and Multifunctional Agriculture	173,901,427	28.2.2010	170,545,979	169,447,242	97.4 %	4,454,185
OP Industry and Enterprise	260,852,142	31.7.2010	258,898,126	258,898,126	99.3 %	1,954,016
OP Infrastructure	246,360,355	31.7.2010	250,802,124	246,360,355	100 %	0
OP Human Resources Development	318,819,283	31.7.2010	332,420,463	318,819,283	100 %	0
Objective 1 total	**1,454,265,778**	**-**	**1,468,782,398**	**1,446,430,434**	**99.5 %**	**7,835,344**
SPD for Objective 2	71,295,400	30.6.2010	71,576,872	71,295,400	100 %	0
SPD for Objective 3	58,793,363	31.7.2010	59,064,641	58,793,363	100 %	0
SPD total	**130,088,763**	**-**	**130,641,513**	**130,088,763**	**100 %**	**0**
EQUAL	32,100,930	31.7.2010	32,742,976	32,100,930	100 %	0
Interreg Poland*	34,502,947	25.2.2010	35,925,619	34,502,947	100 %	0
Interreg Saxony**	13,036,240	30.6.2009	13,309,945	13,036,240	100 %	0
Interreg Bavaria	8,600,000	30.6.2009	9,003,549	8,600,000	100 %	0
Interreg Slovakia	8,999,999	30.6.2009	9,470,931	8,999,999	100 %	0
Interreg Austria	11,000,000	30.6.2009	11,361,210	11,000,000	100 %	0
Initiatives total	**108,240,116**	**-**	**111,814,230**	**108,240,116**	**100 %**	**0**
Total	**1,692,594,657**	**-**	**1,711,238,141**	**1,684,759,313**	**99.5 %**	**7,835,344**

Source: MoF, Overview of the final drawdown from Structural Funds and the *Cohesion Fund* in the programming period 2004–2006 as of 31.12.2010.

* In the Interreg IIIA Czech Republic-Poland, there is also included the Polish part.

**In the Interreg IIIA Czech Republic-Saxony, a part of Saxony allocation has been moved to the Czech part of the programme.

It is clear from the table that 10 out of the total of 13 operational programmes used up their entire allocation; the remaining have a drawdown rate exceeding 95%. In total, EU finances worth **€1,684.76 million** were drawn down, which represents **99.54% of the allocation** to the Czech Republic under the Structural Funds **for the 2004-2006 programming period**. However, the payment of the final balance may be influenced yet by possible financial corrections by the European Commission or as a result of identified irregularities. The final payment requests for the individual programmes were sent to the Commission by the set deadlines. As of 17 March 2011, final negotiations were taking place for the majority of programmes (providing additional requested information). The details of the winding-up of programmes are given in Appendix 3.

Other important data that testify to the state of implementation of Cohesion Policy in the Czech Republic are the number of supported projects and the state of their implementation. In view of the winding-up of programmes, almost 100% of all projects with an issued decision, or signed contract, had been completed as of 31 December 2010, i.e., a total of 13,559 completed projects out of 13,742 with an issued decision (signed contract). 11,813 projects were completed under Objective 1, which is 98.5% of the total number of projects with an issued decision (signed contract). 99.3% of projects with a decision (contract) were completed under Objectives 2 and 3, i.e., 1,051 projects in total.

B.3.1.1.2 State of drawdown of the allocation from the Cohesion Fund and ISPA as of 31 December 2010

The closing date for the eligibility of expenditure in the case of *Cohesion Fund* or ISPA projects was 31 December 2010. 59 projects were approved for financing in total. Of that number, 53 projects had been completed by 31 December 2010; six projects have been granted extensions on expenditure eligibility up to 31 December 2011 by the Commission.[59] As the following table shows, the drawdown was €1061.98 million, which is 86.3% of the total *Cohesion Fund* allocation. The data given are cumulative, i.e., they are aggregated from the year 2000 and include ISPA finances. Given the extension of six projects' implementation period we expect further finances to be drawn in 2011.

Table 10: Overview of drawdown from *Cohesion Fund* as of 31. 12. 2010

	Total allocation	Drawn down	
	€	€	%
Transport	598,877,099	544,843,114	90.98 %
Environment	596,596,207	483,749,057	81.08 %
Technical assistance	5,040,891	3,395,475	67.36 %
Flooding	30,000,000	30,000,000	100.00 %
Total from *Cohesion Fund**	**1,230,514,197**	**1,061,987,646**	**86.30 %**

Source: MoF – Overview of drawdown from *Cohesion Fund* as of 31. 12. 2010

* ISPA incl.

B.3.1.2 2007–2013 Programming Period

The financing of Cohesion Policy measures is the biggest expenditure item in the EU budget earmarked for the Czech Republic in the 2007-2013 programming period. In 2009, Cohesion Policy expenditure of €1,974.9 million was paid, thus substantially exceeding the second largest item, which is expenditure on preservation and management of natural resources which took €867 million from the EU budget.

Measures to increase the efficiency of the drawdown of finances from the Structural Funds and the Cohesion Fund

The Czech Government adopted a number of measures to simplify administration and increase the effectiveness of the use of the Structural Funds and the *Cohesion Fund* at the time of continuing economic crisis, *inter alia,* instructing the regional development minister[60] and subsequently the finance minister[61] to draft legislative amendments with a view to simplifying the administration of the Structural Funds and the *Cohesion Fund*.

The following aspects from the proposed amendments have been approved so far:

- "lump-sum payments" were approved, thus simplifying expenditure reporting by end beneficiaries[62];
- the system for paying finances to beneficiaries was speeded up[63].

Another adjustment is a change to the Methodology for Financial Flows and Control of Programmes Co-financed from the Structural Funds, the *Cohesion Fund* and the European Fisheries Fund for the 2007–2013 Programming Period[64], part of which is an extension of the time limit for the transfer of funds from a provider to a beneficiary and the setting of a time limit for the transfer of funds to beneficiaries in an accompanying letter in a situation of "multi-level subsidies".

59 source: Ministry for Regional Development, National Coordination Authority.
60 The MfRD is the central methodological and coordination authority for economic and social Cohesion policy in the period 2007-2013.
61 In connection with the material entitled *Proposals for Legislative and Other Changes to Simplify the Administration of the Structural Funds and Cohesion Fund of the European Union in the Years 2007 to 2013*, which the Government noted by resolution No. 212 of 15 March 2010.
62 This change is based on the rules in Regulation (EC) No. 1080/2006 of the European Parliament and of the Council on the European Regional Development Fund and Regulation (EC) No. 1081/2006 of the European Parliament and of the Council on the European Social Fund governing reporting of indirect costs. The rules were implemented by Section 14 (7) of Act No. 139/2010 amending Act No. 218/2000, on budgetary rules.
63 The acceleration was achieved by repealing Section 7 (1) of Decree No. 449/2009, on the manner, times and scope of data submitted for assessment of the implementation of the State budget, the budgets of State funds, the budgets of self-governing territorial units, the budgets of voluntary associations of municipalities, and the budgets of cohesion regions' regional councils.
64 The revised version of the methodology entered into effect on 1 January 2011.

In addition, the "Binding Procedures for Awarding Contracts Not Falling under the Application of Act No. 137/2006, on Public Contracts", were updated for the 2007-2013 programming period, with a uniform system of penalties for violating the procedures put in place.

On 2 March 2011, the Government approved a draft amendment[65] that should facilitate the administration of finances from EU funds. Among them are, for example, a possibility for the ministry to decide that a project envisaged to be co-funded by the EU will be funded solely out of the State budget; making a subsidy transferable to another entity; the introduction of a forfeit deadline for the option of applying for waiving or partially waiving a payment for breach of budgetary good practice or the possibility of stipulating a lower payment than the wrongfully used financial amount in the case of a less serious violation of terms. The amendments are expected to be debated in the Czech Parliament in the first half of 2011.

There continue to be several areas where changes are being considered with a view to facilitating the drawdown of finances from EU funds; this covers, for example, the issue of the obligation to use ISPROFIN (ESS/SPA)[66], the use of financial engineering instruments, or strengthening the role of the State vis-à-vis regional councils in the area of the State's control powers.

Another area closely linked to the drawing of finances from the Structural Funds is the public procurement rules. On 5 October 2010, the anti-corruption sub-committee of the Government's National Economic Council (NERV) issued a document entitled *NERV Anti-Corruption Recommendations* containing an analysis of the current state of public procurement and 15 proposed measures to improve the state of affairs. Further to that document, the Czech Government is preparing a draft amendment of Act No. 137/2006, on Public Contracts, reflecting the proposed measures. The draft amendment has not been put before the Czech Parliament yet.

Increase of the allocation

Along with Poland and Slovakia, the Czech Republic is a country whose actual gross domestic product for 2007-2009 exceeded the Commission's estimate by more than 5% and is thus entitled to compensation for GNI-based contributions in the form of additional finances from the Structural Funds[67]. The Czech Republic thus gained an additional allocation of €237,045,801 for the years 2011 to 2013.

Table 11: Proposal for breakdown of additional funds

OP	Area	€ million*	%
OP Enterprise and Innovation	Service in the area (social services; public services and services for business subjects; infrastructure for cultural services)	45.0	19.0
Integrated OP		17.5	7.4
OP Enterprise and Innovation	Enterprise and Innovation (Eko Energy)	30.8	13.0
OP Transport	Transport infrastructure	47.4	20.0
ROP		77.5	32.7
OP Prague – Competitiveness	Regional competitiveness (innovation and enterprise)	5.4	2.3
OP Human Resources and Employment	Human resources	13.3	5.6
Total		**237.0**	**100.0**

Source: Distribution of Additional Finances Pursuant to Point 17 of the Interinstitutional Agreement, approved by Government Resolution No. 817 of 16 November 2010.

*The final amounts may be technically adjusted when the financial tables are drawn up so that the Commission´s accounting system accepts the sums.

State of drawdown of the allocated amount

In total, projects worth over CZK 433 billion have already been approved under the Convergence and Regional Competitiveness and Employment objectives; that represents approx. 55% of the total allocation. At least two

65 Act No. 218/2000, on the budgetary rules, and Act No. 250/2000, on the budgetary rules for territorial budgets.

66 Particularly in the case of operational programmes covering both investment actions and non-investment actions and in the case of OP Cross-border Cooperation Czech Republic – Poland, where payments are done in €.

67 Article 17 of the Interinstitutional Agreement between the EP, the Council and the Commission, on budgetary discipline and sound financial management (2006/C 139/01).

certifications of expenditure took place in all OPs since the start of the programming period. In 2010, there was no certification solely in the case of ROP Southwest, where the Paying and Certifying Authority decided to suspend the certification process in connection with an investigation into suspected irregularities in the project assessment process. 11.4% of the total allocation for all OPs under the Convergence and Regional Competitiveness and Employment objectives for the 2007-2013 programming period was drawn down (i.e., certified and submitted to the Commission). The following table gives a detailed picture of the state of implementation of the OPs as of 5 January 2010.

Table 12: Spending of the allocation for Convergence and Regional Competitiveness and Employment objectives in the Czech Republic in the programming period 2007–2013 as of 5. 1. 2011

Operational Programme	Allocation (CZK million)	Projects submitted		Projects approved		Funds paid out to beneficiaries (CZK million)	Request submitted for payment (CZK million)	Spent from allocation
		number	CZK million	number	CZK million			
OP Transport	171,653.1	203	207,727.7	118	166,159.7	94,364.1	28,735.4	16.7 %
OP Environment*	146,385.0	9,370	153,036.0	2,648	23,892.1	18,545.6	10,879.5	7.4 %
OP Enterprise and Innovation	90,440.1	8,982	96,307.8	4,827	44,567.5	14,526.6	8,742.7	9.7 %
OP Human Resources and Employment	54,483.3	641	52,282.8	395	41,439.3	8,255.8	5,669.0	10.4 %
OP Research and Development for Innovations	61,486.5	202	98,151.2	43	16,788.1	1,951.5	39.1	0.1 %
Integrated OP	47,039.4	7,499	47,960.5	6,413	24,991.6	4,364.9	2,620.0	5.6 %
OP Education and Competitiveness	54,290.3	4,635	54,698.3	1,946	21,638.4	8,784.9	847.4	1.6 %
OP Technical Assistance	7,367.6	113	6,585.6	83	3,557.3	882.7	502.2	6.8 %
Thematic OPs total	**633,145.3**	**31,645**	**716,749.9**	**16,473**	**343,034.0**	**151,676.1**	**58,035.3**	**9.2 %**
ROP Northwest	22,171.3	788	33,618.2	234	15,161.9	7,317.2	3,441.9	15.5 %
ROP Moravia-Silesia	21,308.5	1,144	27,235.7	391	9,407.5	4,913.5	3,691.7	17.3 %
ROP Southeast	21,037.3	1,183	30,434.4	499	15,074.8	9,487.6	7.119.6	33.8 %
ROP Central Moravia	19,654.6	1,334	24,979.8	436	9,295.7	8,254.3	6,404.9	32.6 %
ROP Northeast	19,619.7	1,129	35,949.4	395	13,715.3	8,909.9	6,070.1	30.9 %
ROP Southwest	18,426.6	2,349	46,710.9	393	9,731.4	5 512,0	660.6	3.6 %
ROP Central Bohemia	16,652.4	1,136	23,878.8	419	9,608.1	4,602.1	2,219.3	13.3 %
ROPs total	**138,870.4**	**9,063**	**222,807.2**	**2,767**	**81,994.7**	**48,996.6**	**29,608.1**	**21.3 %**
OP Prague Competitiveness	6,986.3	633	12,918.5	201	5,792.8	2,574.1	1,003.7	14.4 %
OP Prague Adaptability	3,225.4	2,334	12,387.0	482	2,466.1	1,358.6	420.6	13.0 %
OPs Prague total	**10,211.7**	**2,967**	**25,305.5**	**683**	**8,258.9**	**3,932.7**	**1,424.3**	**13.9 %**
Total	**782,227.4**	**43,675**	**964,862.6**	**19,923**	**433,287.6**	**204,605.4**	**89,067.7**	**11.4 %**

Source: MfRD – Monthly Monitoring Report on the Course of Drawing from the Structural Funds, *Cohesion Fund*, and National Resources in the 2007-2013 Programming Period, December 2010.

*Projects that were selected for the implementation by the OP Environment Steering Committee but did not have a signed contract by 5 January 2011 are not listed in the "Projects Approved" column.

The table shows the values solely for individual projects and global grants; grant projects are not included in the table as certification only takes place for individual projects and global grants.
Exchange rate: €1 = CZK 25.24 (monthly rate taken from Structural Funds Monitoring System); data in the "Spent from Allocation" column are converted using the exchange rate at the time of entry in the Viola IS, so the rate is not the same as the current monthly rate.

Table 12 includes “major projects”[68] that have been approved by the Managing Authority but have not been approved by the Commission[69] yet. Expenditure linked to the implementation of major projects can only be certified once the project has been approved by the Commission. In the interim between approval of the project at national level and approval by the Commission sums can be paid to beneficiaries under pre-financing based on a payment application.

The major projects in the Czech Republic affect three operational programmes: OP Transport, OP Environment, and OP Research and Development for Innovations. Of the major projects approved at national level, the biggest share of the total available allocation is found under OP Transport (78.2%) and OP R&D for Innovations (36.5%). For these OPs, the successful implementation of the major projects would have a significant impact on the drawdown of the allocation. Conversely, if these projects did not receive Commission’s approval the statement of expenditure would have to be corrected, with these sums deducted. In that case there is a greater need for a sufficient quantity of alternative projects and, by extension, a greater burden on the State budget, which has to finance projects not approved by the Commission out of national resources. The level of drawdown in the form of pre-financing is significant mainly in the case of OP Transport, where major projects worth approx. 48% of the allocation have been submitted for financing approval, but the Commission has approved only projects worth 9% of the total allocation so far. The state of approval of major projects is shown in Table 13.

Table 13: State of approval of major projects

Operational Programme	Allocation (CZK Million)	Approved at the national level (MA)			Submitted to the European Commission			Approved by the European Commission		
		number	CZK million	%	number	CZK million	%	number	CZK million	%
OP Transport	171,653	33	134,245	78.2 %	18	82,666	48.2 %	5	15,684	9.1 %
OP R&D for Innovation	61,487	6	22,433	36.5 %	5	19,183	31.2 %	0	0	0.0 %
OP Environment	146,385	7	6,781	4.6 %	7	6,781	4.6 %	4	2,865	2.0 %
Total	**379,525**	**46**	**163,459**	**43.1 %**	**30**	**108,630**	**28.6 %**	**9**	**18,549**	**4.9 %**

Source: MfRD – Monthly Monitoring Report on the Course of Drawing from the Structural Funds, *Cohesion Fund*, and National Resources in the 2007-2013 Programming Period, December 2010

Under the third objective of the 2007-2013 programming period named European Territorial Co-operation, almost 1,500 projects under all five cross-border cooperation OPs have been submitted to date; almost 800 of these projects have already been approved. The value of the approved projects amounts to more than 75% of the total allocation for the programming period. Here, too, certification of expenditure is ongoing; more than 13% of the total allocation has already been certified and submitted to the Commission.

“n+3” rule

Regulation of the European Parliament and of the Council (EU) No. 539/2010 approved a change to Regulation of the Council (EC) No. 1083/2006 consisting in the abolition of the “n+3” rule for the allocation for 2007 (amendment of Article 93 of the General Regulation). The budget commitment for 2007 was distributed evenly over the six following years of the programming period.

Thus, the first year when automatic decommitment may take place is 2011. To prevent this situation arising, individual OPs must, by the end of 2011, have certified finances amounting to approx. 15% of the total allocation for the programming period[70]. As of 5 January 2011, six OPs[71] had satisfied the n+3 rule, as had the majority of cross-border cooperation programmes. Eight programmes display a low level of drawdown. These are: OP Research and Development for Innovations; OP Education for Competitiveness; Integrated OP; OP Technical Assistance; OP Environment; OP Human Resources and Employment; OP Enterprise and Innovations; ROP Southwest. The national coordination authority, the Ministry of Regional Development, is conducting “enhanced risk management” with the managing authorities of six operational programmes with a view to putting in place

68 A major project is a project whose costs exceed €50 million.
69 Council Regulation (EC) No. 1083/2006.
70 The advance payment from the Commission, which is equal to 9% of the total allocation in the case of ESF and ERDF, and in the case of the *Cohesion Fund* 10.5% of the total allocation for the programming period, can be included in this sum.
71 OP Transport, ROP Moravia-Silesia, ROP Southeast, ROP Central Moravia, ROP Northeast, ROP Northwest.

measures to eliminate the risk of non-compliance with the n+3 rule (or the risk of automatic decommitment). Enhanced risk management has not been applied in the case of OP Enterprise and Innovations. One reason why ROP Southwest displays a low level of certified finances is that the Paying and Certifying Authority decided to suspend the process of expenditure certification in connection with an investigation into suspected irregularities in the project assessment process. In the period between December 2010 and March 2011, the Payment and Certifying Authority suspended the process of expenditure certification of four OPs, namely OP Environment, OP R&D for Innovation, ROP North-West, and OP Enterprise and Innovation.

B.3.1.3 2014-2020 Programming Period

In November 2010, the Commission published the "Conclusions of the fifth report on economic, social and territorial cohesion", setting out fundamental ideas for making the Cohesion Policy delivery system more streamlined, effective, and improving the assessment, performance, and results by more effective setting of targets. According to the report, Cohesion Policy is a major factor contributing to growth and prosperity. The Commission proposed that in future Cohesion Policy should concentrate on financing key priorities in line with the objectives of the Europe 2020 strategy (see Section A.1 of the EU Report 2011) in order to optimise the effect of this financing. At the turn of January and February 2011, the Fifth Cohesion Forum was held in Brussels, dealing mainly with the role of Cohesion Policy in implementing the Europe 2020 strategy. In summer 2011, the Commission should present legislative proposals concerning future Cohesion Policy.

On 3 November 2010, the Czech Government's Committee for the European Union issued Resolution No. 34 approving "The Starting Points of the Czech Republic's Position for Negotiating on the Form of EU Cohesion Policy after 2013". Further to that, on 26 January 2011 it approved the updated Framework Position of the Czech Republic on the Future of EU Cohesion Policy, responding to, among other things, the questions raised by the Commission as part of the public consultations on the Fifth Cohesion Report. Additionally, the regional development minister was instructed to work with the concerned members of the Government to submit to the Government a summary proposal for the future of EU Cohesion Policy after 2013 in the conditions of the Czech Republic by 31 July 2011. This material should also contain a proposal for development priorities for drawing on EU funds after 2013.

B.3.2 SAO's audit work

In the time between the beginning of 2010 and writing of this EU Report 2011, the SAO completed six audits whose subject matter touched on EU Cohesion Policy. Operational programmes from both the 2004-2006 programming period and the current period of 2007-2013 were audited. The following text sets out the key facts that were identified and published in the audit conclusions, with the exception of the audit entitled Funds earmarked for implementation of the Single Programming Document for Objective 2 for the Prague Cohesion Region[72], whose results were already commented on in the EU Report 2010.

B.3.2.1 Funds earmarked for railway infrastructure development

The purpose of this audit[73] was to scrutinise the provision, drawing, and use of finances earmarked for the construction of the 3rd and 4th railway corridors and for preparing the construction of high-speed lines. The volume of audited finances provided out of the *Cohesion Fund* for the construction of the two railway corridors was approx. CZK 8,739 million. The audit conclusion refers to deficiencies in the financial modelling of investment requirements and resources and also the fact that the Ministry of Transport did not have a clear concept of the construction of the high-speed lines. No deficiencies within the meaning of Regulation of the Council (EC) No 1083/2006 were found by this audit.

B.3.2.2 Finances earmarked for transport infrastructure projects under ROPs

This audit[74] sought to scrutinise whether the auditees were using transport infrastructure funds in line with the regulations, efficiently and economically, and whether the ROP implementation system displayed serious deficiencies jeopardising the drawdown of EU budget finances. In the period under scrutiny (i.e., from 2007 to mid 2010), almost CZK 10 billion was paid out under all seven ROPs on transport infrastructure projects. CZK 2.5 billion of that amount was audited during this audit. The audit conclusion sets out the following finding:

72 Audit No. 09/09, Issue 1/2010 of the SAO Bulletin.
73 Audit No. 09/19, Issue 2/2010 of the SAO Bulletin.
74 Audit No. 09/26, Issue 1/2011 of the SAO Bulletin.

- Minor deficiencies were found in the ROPs' implementation systems, but these were not shortcomings that would jeopardise the system for drawing EU finances.
- The inflexible subsidies decision-making system meant that throughout almost the entire budgetary period State budget finances provided by the Ministry for Regional Development to finance the ROPs were provided in higher amounts than was actually required. In 2007, the cohesion regions' regional councils used on average just 14% of the allocated funds; and in 2008 as little as 9%.
- The MfRD was in breach of budgetary discipline to the value of at least CZK 68,442,000 by failing to ensure that the interest revenues stemming from the deposited State budget finances earmarked for ROP pre-financing and co-financing were counted by the individual regional councils as part of the State co-financing share for the subsequent year.
- The MfRD did not specify which methodological documents issued by it, by the Audit Authority and by the Paying and Certifying Authority were binding for the regional councils.
- The Czech legal regulations do not specify precisely whether subsidies should be provided to beneficiaries in the form of a decision on the provision of a subsidy or by a contract, and what the fundamental substantive particulars of such an action should be. The regional councils use a private-law contract concluded under the Civil Code to provide subsidies. This legislative shortcoming gives rise to situations where evidently public relations are governed by private contracts.
- In the case of two regional councils, the project assessment system displayed significant deficiencies. As part of eligibility assessment, the Central Bohemia regional council failed to verify whether the submitted projects complied with the State aid legislation; in addition, until 2009 it did not perform substantive assessment on the basis of assessment criteria in line with the principle of sound financial management. The Southwest regional council did not ensure the separation of functions of the parties involved in the management and control by failing to arrange a substantive assessment of projects submitted in four calls by two independent assessors.
- In two ROPs, deficiencies were found in the set-up of the monitoring system.
- Deficiencies were found in the Central Bohemia regional council's system of controls prior to payment of subsidies to final beneficiaries. For example, there was no separation of the approval and control functions, or the internal regulations did not define control methods and the documents subject to control, particularly in the areas of State aid, public procurement, and accounting.
- In some cases, the managing authority's control systems failed. This mainly applies to controls covering the award of public contracts and control of the technical implementation of projects. Concerning public procurement, shortcomings were found consisting in, for example, not excluding a candidate from procurement proceedings even though it did not meet the tender terms, and the wrongful award of a public contract for additional building work. As regards the technical implementation of projects, the deficiencies included claiming for work not done and claiming for work that was not part of the project. Expenditure of CZK 22,824,800[75] was wrongfully paid.
- It was found in the case of four beneficiaries that they had notified the relevant regional council of changes in the project after these changes had been made, or had not notify the regional council at all.
- Deficiencies found in the irregularities reporting system included non-compliance with time limits, non-compliance with codes of practice and internal regulations, and not denoting a final beneficiary's conduct as an irregularity and subsequently not including it among the reported irregularities.

B.3.2.3 Finances earmarked for road building

The aim of this audit[76] was to examine the provision, drawing and use of finances for the preparation of road building operations and ensuring their economic and efficient implementation. Most of the findings concern the conceptual work of the Ministry of Transport or State budget finances. This audit only marginally touched on EU Structural Fund finances, finding that:

- During the preparation and implementation of the construction projects, fundamental changes were made to the approved economic and time parameters, in a number of cases without due assessment of these changes' impact on the economic effectiveness of the operations in question.
- The Ministry of Transport does not possess any material ranking construction projects in order of society's need for them and in relation to the realistic possibility of funding them.

75 The irregularity was found in ROP Central Bohemia, ROP Southeast, and ROP Northeast.
76 Audit No. 09/27, Issue 4/2010 of the SAO Bulletin.

B.3.2.4 Programmes under which winter sports resort construction and development projects are co-funded

The purpose of this audit[77] was to check whether the objectives of selected programmes were being achieved in connection with the co-financing of projects related to the construction and development of public skiing resorts. The most serious findings concerned programmes funded out of the State budget. The following findings applied to projects financed out of the EU Structural Funds:

- In the Joint Regional OP, the risk analysis conducted for individual projects did not cover the risks associated with the limited (seasonal) operation of skiing resorts and the influence of hydrometeorological and geographical conditions.
- Under INTERREG IIIA, whose objective was to encourage cross-border cooperation, the Ministry for Regional Development did not set up the system of indicators in a way ensuring that data were obtained on the quality of cross-border cooperation. The required qualitative indicator for the establishment of genuine partnership was thus not evaluated.
- One project for the reconstruction and completion of a skiing resort was supported out of INTERREG IIIA, even though the originally planned construction of an artificial snow system did not take place. Yet, the project was implemented in a location where, according to the feasibility study and data from the Czech Hydrometeorological Institute, below-average snow conditions did not create suitable conditions for skiing. The beneficiary then failed to fulfil the “number of users of the constructed/reconstructed infrastructure” and “volume of provided services” monitoring indicators.

B.3.2.5 Finances provided to improve the state of nature and the landscape[78]

This audit sought to scrutinise the provision, drawing, and use of finances earmarked for improving the state of nature and the landscape, including the system for assessing the expected and achieved results of programmes. Among other things, finances provided out of the ERDF under OP Infrastructure and OP Environment towards the renewal of the environmental functions of territories and improving the state of nature and the landscape were audited. The audit found the following:

- In 2008, the Ministry of the Environment optimised its subsidies programmes to support the preservation of nature and the landscape in connection with the option of drawing ERDF finances, partly to prevent duplications in national and operational programmes.
- Deficiencies were found in the set-up of monitoring indicators in both OPs. In the case of OP Infrastructure, one of the indicators was defined wrongly and only approx. 14% of the planned value was achieved. Some programme indicators of Priority Axis 6 of OP Environment have such low target values that they have already been met or even exceeded several times over and are thus unusable for assessing the programme’s success. For example, the value of the “area of revitalised territory” indicator was set at 1,000 hectares, but by October 2010, 1,225 hectares of territory had already been revitalised even though just a fraction of the allocation has been used. Some other monitoring indicators in OP Environment do not characterise the environmental benefit.
- Wrongful use of finances under OP Environment was found in the case of one beneficiary, which included expenditure on work not done in its eligible expenditure. This irregularity represented a value of less than 0.5% of the allocation from EU finances.

B.3.2.6 Analysis and generalisation of the results of the SAO’s audit work

Analysis of the SAO’s published audit conclusions shows that the following can be identified as the areas at the various implementation levels that most commonly displayed shortcomings:

Bodies implementing structural operations:

- the set-up of the system for monitoring indicators to check the effectiveness of programmes and assess the progress made in achieving the programme’s quantifiable goals (e.g., the unsuitability of selected indicators as regards their specificity and measurability, the absence of indicators for certain objectives)[79];

77 Audit No. 09/28, Issue 4/2010 of the SAO Bulletin.
78 Audit No. 10/12, Issue 2/2011 of the SAO Bulletin.
79 Audit No. 09/09, Issue 1/2010 of the SAO Bulletin, Audit No. 09/12, Issue 1/2010 of the SAO Bulletin, Audit No. 09/26, Issue 1/2011 of the SAO Bulletin, Audit No. 09/28, Issue 4/2010 of the SAO Bulletin, Audit No. 10/12, Issue 2/2011 of the SAO Bulletin.

- the project assessment and selection system (e.g., the application of assessment criteria that do not respect the principles of sound financial management, insufficient selection criteria that give little information about the quality of projects, wrongly devised system for assessing whether the initial investment conditions are met, failure to ensure independent assessments by two assessors)[80];
- legislation governing managing and control systems (e.g., insufficient rules on delegation of administrative control powers between implementing bodies)[81];
- checking by MA and IB (e.g., in IB the failure to check up on activities delegated, insufficient checks before making payments)[82].

Final beneficiaries:

- public procurement (e.g., deficiencies in tender documentation; unclear definition of tender conditions; failure to exclude contractors that did not satisfy the tender terms; errors in points scoring of bids; conclusion of contracts deviating from the tender documentation and winning bid; wrongly awarded additional work)[83];
- compliance with the terms laid down for project implementation (e.g., claiming ineligible costs that did not comply with the purpose of financing or claiming expenditure for work not done; failure to meet project completion deadlines; failure to inform about changes to projects; reporting shortcomings)[84].

Comparison of the analysis with the results of the analysis for the previous period (EU Report 2010) reveals that deficiencies persist in the same areas, at the level of both implementation bodies and final beneficiaries. More cases at final beneficiaries receiving payment for ineligible expenditure were found in this period than in the previous period.

B.3.3 Audit work by EU bodies

B.3.3.1 ECA's audit work

The ECA's Annual Report on the implementation of the budget for 2009[85] reveals that the probable rate of errors in the *Cohesion*[86] policy group is above 5% of certified expenditure. Despite this finding, the ECA welcomes the fact that the error rate in the area of Cohesion has decreased significantly from previous years. Yet, although the error rate has fallen in recent years, *Cohesion* remains the policy group most affected by errors. According to the ECA's estimate, 36%[87] of payments from 180 audited projects were affected by errors. Eligibility-related errors account for a substantial share of the estimated error rate[88]. In the audit sample, the main causes of eligibility errors were the inclusion of costs not eligible for payment, and serious failings relating to compliance with the public procurement rules. At least 3% of expenditure certified by the Commission should not have been paid, according to the ECA. That is a significant improvement from the figure of 11% in 2008.

According to the ECA, the most common causes of eligibility errors include:

- over-declaration of staff costs;
- unjustified application of negotiation procedure (i.e., irregular award of public contracts);
- direct award of contracts (i.e., irregular award of public contracts);
- unlawful use of contract award criteria.

80 Audit No. 09/09, Issue 1/2010 of the SAO Bulletin, Audit No. 09/12, Issue 1/2010 of the SAO Bulletin, Audit No. 09/26, Issue 1/2011 of the SAO Bulletin, Audit No. 09/28, Issue 4/2010 of the SAO Bulletin.
81 Audit No. 09/09, Issue 1/2010 of the SAO Bulletin, Audit No. 09/12, Issue 1/2010 of the SAO Bulletin.
82 Audit No. 09/09, Issue 1/2010 of the SAO Bulletin, Audit No. 09/12, Issue 1/2010 of the SAO Bulletin, Audit No. 09/26, Issue 1/2011 of the SAO Bulletin, Audit No. 09/28, Issue 4/2010 of the SAO Bulletin.
83 Audit No. 09/09, Issue 1/2010 of the SAO Bulletin, Audit No. 09/12, Issue 1/2010 of the SAO Bulletin, Audit No. 09/26, Issue 1/2011 of the SAO Bulletin.
84 Audit No. 09/09, Issue 1/2010 of the SAO Bulletin, Audit No. 09/12, Issue 1/2010 of the SAO Bulletin, Audit No. 09/26, Issue 1/2011 of the SAO Bulletin, Audit No. 09/28, Issue 4/2010 of the SAO Bulletin, Audit No. 10/12, Issue 2/2011 of the SAO Bulletin.
85 Annual Reports concerning the Financial Year 2009, European Court of Auditors, 9 September 2010; for the key information see Chapter A.1.6.
86 The “Cohesion” policy group includes policy area E – Employment and Social Affairs, and policy area 13 – Regional Policy.
87 In 2008 it was 43% and in 207 54%.
88 Point 4.20 of the ECA's Annual Reports concerning the Financial Year 2009.

Non-compliance with the public procurement rules accounts for 43% of all quantifiable errors and roughly three quarters of the estimated error rate[89].

Overall, the ECA judged the systems in the *Cohesion* policy group as only partially effective and submitted the following recommendations to the Commission[90]:

- encourage national authorities to rigorously apply the appropriate corrective mechanisms before certifying expenditure to the Commission;
- ensure that the substitution of ineligible expenditure with new expenditure (withdrawal) does not result in new ineligible expenditure being declared by Member States;
- ensure, through its supervision, an effective functioning of the national management and control systems for the 2007-2013 programming period.

B.3.3.2 Comparison of the ECA's and SAO's findings

The ECA's audit findings concerning the Czech Republic in 2009 are not particularly significant. The ECA only conducted one audit in the Czech Republic as part of the assessment of the recovery and financial correction system of INTERREG IIIA between Bavaria and the Czech Republic (ERDF finances). The audit did not find shortcomings in the reporting of recovered sums and sums withdrawn by the Commission, and assessed the system as partially effective. On the Bavarian side, shortcomings were found in reporting corrections and in registering errors, with the system for both these aspects assessed as partially effective.

The SAO did not perform an equivalent audit scrutinising the regularity of operations in 2009. INTERREG IIIA Czech Republic – Slovakia was the subject of an SAO audit to check whether the objectives of selected programmes were being achieved in connection with the co-financing of projects related to the construction and development of public skiing resorts[91]. In this audit, the SAO found deficiencies in project assessment and monitoring, for example.

As part of the systems audit, the ECA also examined whether 16 managing and audit systems in 13 Member States[92] complied with the principal points of the legal framework. It found that most of the audited OPs were late implementing the approved national audit strategy. Most of the audit bodies had not carried out a sufficient number of audits of payments sufficiently in advance for them to be used in the annual audit report for 2009. Fundamental differences in the extent of work performed on the auditing of systems up to the end of 2009 were also found. Several Member States had not performed any audit of systems before declaring expenditure to the Commission[93].

In most of its audits, the SAO selects the audit sample of operations by the multi-criteria method primarily (stratified selection), and does so for an audited period of more than one year as a rule. Even so, some audit findings can be generalised relative to an entire OP. By contrast, the ECA performs sample selection by statistical methods for a specific budgetary year and interprets its audit findings by extrapolation. The published findings may be compared despite the different approaches.

Analysing the audit findings made by the SAO in audits targeting Cohesion Policy projects and comparing them to the conclusions of ECA audits of a sample of projects in EU Member States (not in the Czech Republic) reveals some degree of similarity.

The ECA found that in one ERDF-financed project for the building of access roads and light constructions at the entrances of a national park the beneficiary had directly awarded a building work contract. What is more, the contractor invoiced works that were not covered by the contract. As the public procurement procedures were not followed, the ECA holds that the payments associated with this contract are irregular[94].

The SAO made a similar finding in its audits in 2010, repeatedly pointing out deficiencies related to compliance with the Act on Public Contracts and the payment of ineligible expenditure. For example, the audit of the ERDF-financed Central Bohemia ROP found that in procuring additional building work in several cases the beneficiary had not

89 Point 4.21 of the ECA's Annual Reports concerning the Financial Year 2009.
90 Point 4.38 of the ECA's Annual Reports concerning the Financial Year 2009.
91 Audit No. 09/28, Issue 4/2010 of the SAO Bulletin,
92 The Czech Republic was not included in the systems audit sample in 2009.
93 In most of the audited OPs the first expenditure was only certified to the Commission in the second half of 2009 - point 4.28 of the ECA's Annual Reports concerning the Financial Year 2009.
94 Point 4.20 Examples of eligibility errors – ECA's Annual Reports concerning the Financial Year 2009.

respected the Act on Public Contracts. The beneficiaries awarded the contracts directly to contractors chosen in the preceding tender procedure without issuing a written call to negotiation. In one of these cases, the beneficiary procured additional building work in the form of negotiation procedure without publication, even though the legal condition concerning the extent of procured additional work was not met[95].

B.3.3.3 Audit work by the Commission

In 2010, the Commission undertook nine audit and verification missions in the Czech Republic. These involved audits of OPs of the 2007-2013 programming period, most notably ROPs, OP Human Resources and Employment, and OP Enterprise and Innovations. The audited entities were the Audit Authority - Ministry of Finance, entrusted audit body and, to a marginal extent, managing authorities or intermediate bodies. Appendix 4 contains an overview of the Commission's audit and verification missions in 2009 and 2010.

The outputs from audits of systems or audits of operations in the selected sample, in the form of preliminary findings, were not available at the time of writing the EU Report 2011, as the results were the subject of discussion between the Czech Republic and the Commission.

B.3.4 Protection of the EU's financial interests in the field of Cohesion Policy

Cohesion Policy is implemented through shared management of the budget; for that reason individual Member States are responsible for preventing, detecting, reporting, and remedying irregularities.

Every year, the Commission publishes a report concerning the protection of the EU's financial interests and the fight against fraud. The report for 2009[96] paid greater attention than in previous years to the development of the entire programming period and not just to a single year. It did so to give a better picture of the working and implementation of Cohesion Policy measures. As Section A.1.7 of the EU Report 2011 sets out in detail, according to the Commission's data the year 2009 had the highest number of reported irregularities in recent years.

Most of the reported irregularities and suspicions of fraud were identified in the area of Cohesion Policy. The share of irregularities falling under Cohesion Policy far exceeds the policy's share of total EU budget spending, which shows that this is an area where managing and audit systems require further improvement.

The largest number of Cohesion Policy irregularities concerned ERDF and ESF finances (79% and 11% respectively). The highest rate of irregularities under the ERDF was found in the programmes of Objective 2. Five states reported the most irregularities in 2009: Italy, Great Britain, Spain, Portugal, and Germany.

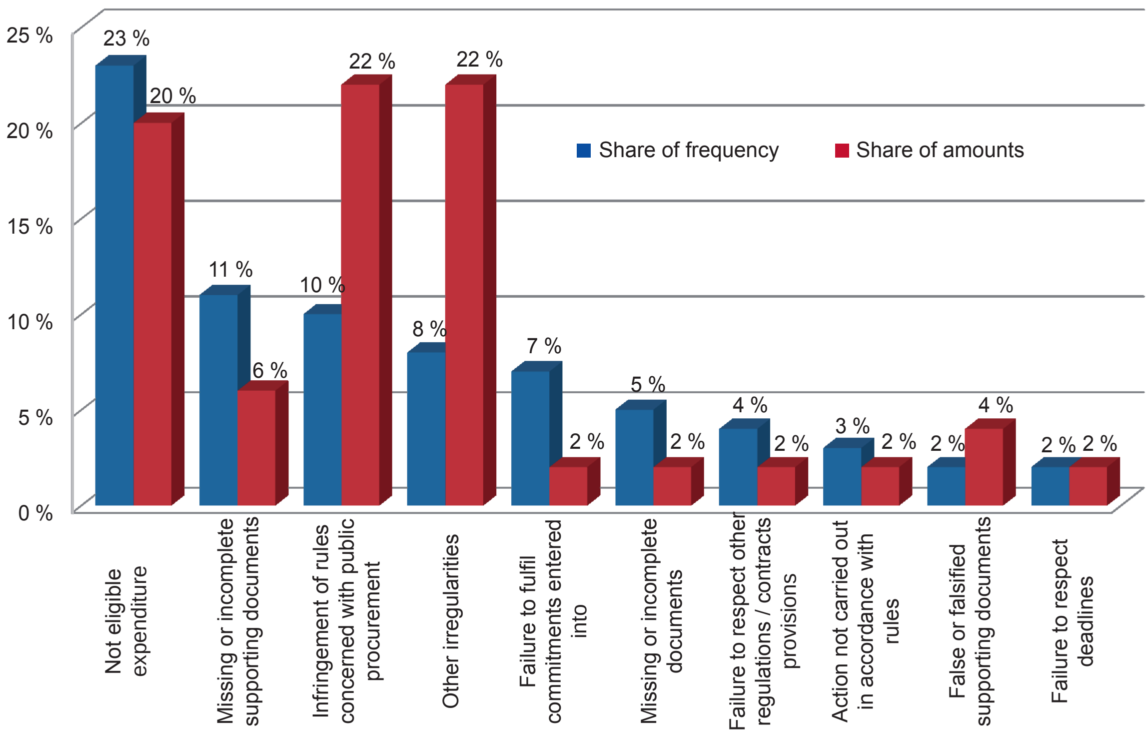
The data concerning the *Cohesion Fund* are still too fragmented to provide a reliable picture. The Commission is working on the full use of the IMS system for the *Cohesion Fund* and this is expected to improve the situation in the coming years. What can be said, however, is that the largest number of irregularities is found in environmental projects.

In the case of Cohesion Policy, the rate of recovery of sums affected by irregularities in the 2000-2006 programming period exceeds 50%. That may be significantly influenced, however, by Member States' practice of excluding projects in which irregularities were found from expenditure declarations sent to the Commission. In this way, the EU finances can be used again to fund other eligible projects and the burden of recovery is shifted to national budgets.

As in the previous years, in 2009, according to the Commission's data, the irregularities concerned not eligible expenditure (23%), missing or incomplete supporting documents (11%) and infringement of rules concerned with public procurement (10%). A constantly high percentage of irregularities is categorised as "other irregularities" (8%). This is the fourth most frequently stated irregularity code. Other irregularities take the biggest share of the financial value of irregularities (22%), alongside irregularities consisting in violation of the public procurement rules (22%) and ineligible data (22%). Graph 14 shows in greater detail the incidence of the most common kinds of irregularity.

95 Audit No. 09/26, Issue 1/2010 of the SAO Bulletin.
96 Report from the Commission to the European Parliament and the Council: Protection of the Communities' financial interests – Fight against fraud – Annual Report 2009, COM(2010) 382 of 14 July 2010.

Graph 14: Share of individual irregularities on the total number of irregularities and on financial value of irregularities in 2009



Source: Statistical Evaluation of Irregularities - Own Resources, Agriculture, Cohesion Policy, Pre-Accession Funds and Direct Expenditure -Year 2009, Accompanying document to the Report from the Commission on the protection of the European Union's financial interests and the fight against fraud – 2009, SEC(2010) 898 of 14. 7. 2010.

Most irregularities were detected by national administrative and financial controls (20.9%), followed by document checks (12.2%) and on-the-spot checks (9.4%). Irregularities detected without any specification of the detection method used are ranked in third place (11.4%).

One positive fact is that the number of irregularities detected by national administrative and financial audits increased from 2008 to 2009. This means that the majority of irregularities were detected by Member States before payments were made from European funds. In terms of the project implementation cycle, irregularities take place most frequently in the project implementation phase.

In 2009, 82 irregularities were reported to the Commission in the context of programmes in the Czech Republic co-financed out of the Structural Funds and the *Cohesion Fund* (79 out of the Structural Funds and 3 out of the *Cohesion Fund*); that was the same number as in 2008. The total value of the reported irregularities was €14,828,741; €12,903,821 of that sum concerned the Structural Funds and €1,924,920 the *Cohesion Fund*.[97] According to Ministry of Finance data, in 2009 the Commission performed a financial correction relating to a transport project financed out of the *Cohesion Fund* to the value of €52,452.

Of the 79 irregularities reported in the case of the Structural Funds, the largest number (45 in total) concerned the ERDF; 33 irregularities concerned the ESF. One irregularity was detected under the EAGGF.

Irregularities detected by the SAO

The SAO, as an external audit body, identifies the primary suspicion of irregularity and subsequently initiates responses[98].

97 Source: Annex SEC(2010) 898 to the Report from the Commission to the European Parliament and the Council: Protection of the Communities' financial interests – Fight against fraud – Annual Report 2009, COM(2010) 382 of 14 July 2010.

98 Section 34 (18) of Czech National Council Act No. 337/1992, on the administration of taxes and fees; Section 8 (1) of Act No. 141/1961, on judicial criminal proceedings (Criminal Code)

As part of the SAO's reporting duty, notifications were sent to the appropriate tax offices and the Central Bohemia Regional Council on the basis of the findings from audits Nos. 09/09[99] and 09/26[100]. These notifications quantified the value of significant deficiencies.

Audit No. 09/09 found irregularities in three projects concerning ineligible expenditure totalling CZK 450,387 financed out of the ERDF.

Audit No. 09/26 found irregularities in five projects concerning ineligible expenditure and violation of the public procurement rules totalling CZK 20,974,141 financed out of the ERDF.

B.4 Other EU expenditure

Other EU expenditure represents an extensive and diverse area of spending designed to support and deepen cooperation between Member States in various specific areas directly linked to EU policies. A general rule for obtaining support is the creation of a partnership between entities from various States and European added value, which gives projects transnational significance. This EU expenditure forms just a fraction of spending compared to expenditure on the CAP or Cohesion Policy. In the EU financial perspective for 2007-2013, this spending is mainly found in the *Sustainable Growth* and *Citizenship, Freedom, Security and Justice* headings. Appendix 5 of the EU Report 2011 contains an overview of programmes by heading of the financial perspective.

B.4.1 Other EU financial instruments in the Czech Republic

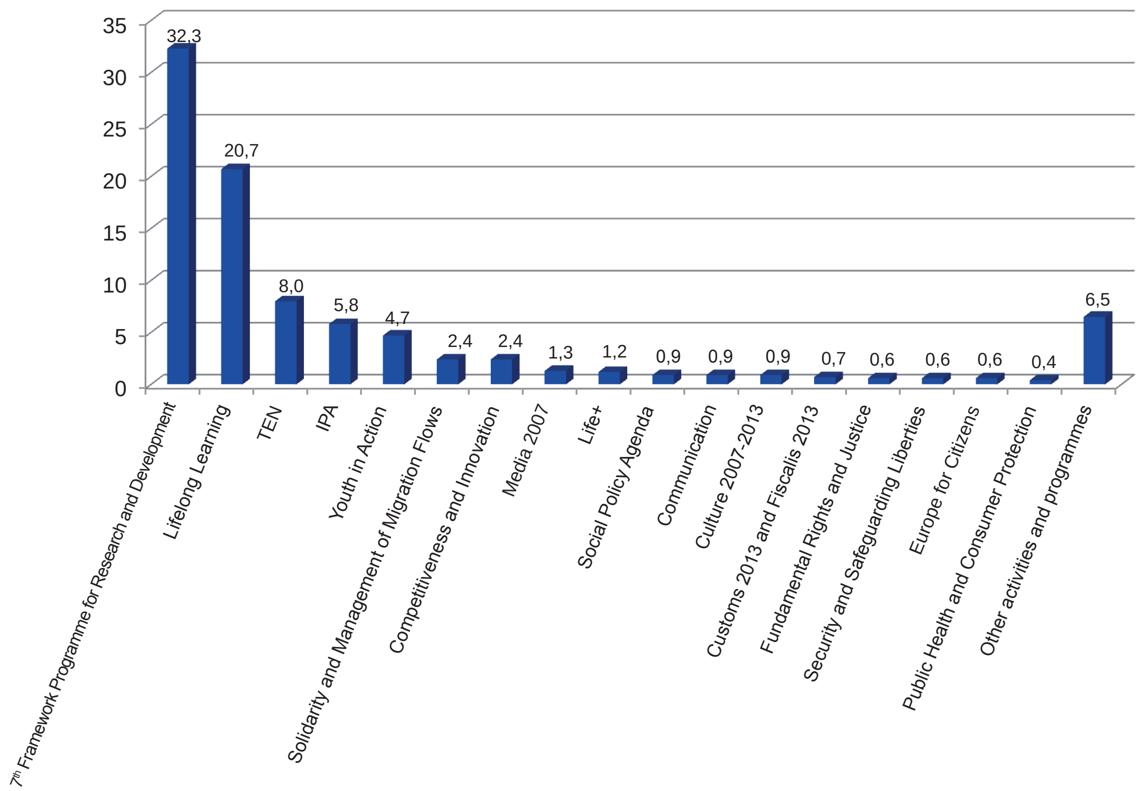
Unlike the Structural Funds that receive broad media coverage, the administration of these financial instruments is in most cases handled by agencies of the Commission in Brussels or Luxembourg. There are also exceptions, e.g., the Lifelong Learning programme, which are implemented directly in the Czech Republic through "national agencies". Other instruments have merely a contact point at the programme coordinators in the Czech Republic.

Finances are allocated to individual programmes not to individual States. For applicants from the Czech Republic this means that they have to stand up to international competition to succeed with their projects.

A close look at the use of other financial instruments in Member States in 2009[101] shows that beneficiaries in the Czech Republic obtained approx. €90.9 million under these programmes; that is an almost identical amount as in the previous year (€91.2 million) and the structure of expenditure is very similar as well. The following graph detailing the state of drawdown of "other financial instruments" in the Czech Republic in 2009 shows that the 7th Framework Programme for Research and Development was the biggest programme in this regard, followed by Lifelong Learning and projects co-financed out of the TEN budget. In addition, the share of drawing by beneficiaries from the Czech Republic relative to total expenditure from the EU budget remains unchanged at 0.82% of total expenditure received by all Member States[102].

99 Issue 1/2010 of the SAO Bulletin
100 Issue 1/2011 of the SAO Bulletin
101 European Commission – EU budget 2009 – Financial Report.
102 This share is calculated on the basis of EU expenditure effected solely in Member States, not total EU expenditure which also includes external expenditure. Expenditure on Community agencies was also not included in the calculation.

Graph 15: Use of other financial instruments in the Czech Republic in 2009 (€ million)



Source: Evropean Commission – EU budget 2009 – Financial Report.

B.4.1.1 Pre-accession instruments

At present, certain pre-accession assistance programmes financed under PHARE are coming to an end in the Czech Republic. The SAPARD[103] programme was wound up back in 2006, with the Czech Republic receiving the last payment in 2007. When the Czech Republic joined the EU, projects funded by the ISPA[104] pre-accession instrument were transferred to the *Cohesion Fund*; their financing is ongoing.

Although all PHARE projects undertaken in the years 1998 to 2006, whose total allocation was €514 million, have come to an end, but only those programmes declared wound-up by the Commission can be considered closed. Winding-up declarations are usually preceded by ex-post on-the-spot checks or a final audit, with any irregularities resolved and unused or incorrectly used finances returned. As of 31 December 2010, 19 out of the total of 38 PHARE[105] programmes implemented in the Czech Republic from 1998-2006 had been closed.

After the Czech Republic's accession to the EU, PHARE was followed by the 2004-2006 Transition Facility, with a total allocation of €36.06 million. Activities were ceased as of 15 December 2009 and payment of the remaining funds took place until 15 June 2010.

Appendix 6 contains an overview of allocations and drawing from the PHARE and Transition Facility programmes in the Czech Republic and their state as of 31 December 2010.

103 Special pre-accession programme for agriculture and rural development.
104 Instrument of pre-accession structural policies, under which large infrastructure projects were financed.
105 Source: Annual Report on the State of Use of Financial Mechanisms of the European Economic Area and Norway, the Czech-Swiss Cooperation Programme and Programmes Financed out of the EU Budget (Transition Facility) – Government ref. No. 692/10.

B.4.2 Financial management and control in relation to other EU financial instruments

Other EU financial instruments are covered by various forms of financial management of the EU budget. The most common form is called direct centralised management, where the Commission is responsible for the implementation of these resources. Indirect centralised management or shared management, where part of the responsibility is transferred to national authorities[106], is only used for certain instruments.

B.4.2.1 Audit work by the ECA

The ECA's Annual Reports concerning the financial year 2009 deals with other financial instruments not only in the DAS but also in the separate chapters that analyse audit findings in detail. As far as the legality and regularity of transactions underlying the accounts is concerned, the ECA issued an unqualified opinion only in respect of expenditure on "Economic and Financial Affairs". In the case of "Research, Energy and Transport" it stated that payments continue to be materially affected by errors and rated systems as only partially effective. Errors were detected mainly in cases where overstated staff and indirect costs were paid to beneficiaries taking part in research projects. The same situation is found in "External Aid, Development and Enlargement", where the errors are mainly linked to eligibility of expenditure and non-compliance with the public procurement rules. An adverse opinion was also issued for the budget area of "Education and Citizenship"[107].

The ECA did not undertake any mission dealing with other financial instruments in the Czech Republic in 2009. For that reason, the conclusions set out above are not founded on findings applying to the Czech Republic or beneficiaries from the Czech Republic.

In addition to the Annual Report, in 2010 the ECA published three Special Reports dealing with other financial instruments.

The first of these[108] covered the effectiveness of selected programmes supporting the 6th Framework Programme for Research. It was found that, while the programme of support for "design studies" was rated very positively and provided critical early-stage funding, support for "new infrastructure construction" only had a limited impact, and most projects would have gone ahead even without EU support.

The aim of another Special Report[109] was to judge the effectiveness of the Leonardo da Vinci mobility scheme. The report reveals that it is necessary to complete the system for measuring impact and to finalise SMART objectives as quickly as possible.

The last report[110] issued in 2010 dealt with railway infrastructure co-financing and its effectiveness in terms of performance. The ECA came to the conclusion that the priority projects have not been defined on the basis of an analysis of actual and anticipated traffic flows yet and that the axes to which they correspond do not represent definitive descriptions of the main trans-European rail axes. It was also found that technical specifications were often amended during construction and cost escalations were common.

B.4.2.2 Audit work by the SAO

In 2010, the SAO did not perform any audit dealing solely with other EU financial instruments. An audit whose purpose was to scrutinise the provision, drawing, and use of finances on the preparation of road construction[111] projects dealt with this issue in part. Some of the funding came from the EIB.[112] Details can be found in Chapter B.3.2.3.

106 Chapter D Internal Policies and Annexes 4 and 5 to the *EU Report 2008* explain in detail the different forms of management and the categorisation of financial instruments by management method.
107 Speech by Mr Vitor Caldeira, President of the ECA – www.eca.eu.
108 Special Report No 2/2010: Effectiveness of the Design Studies and Construction of New Infrastructures Support Schemes under the Sixth Framework Programme for Research, European Court of Auditors, 2010.
109 Special Report No 4/2010: Is the Design and Management of the Mobility Scheme of the Leonardo da Vinci Programme Likely to Lead to Effective Results?, European Court of Auditors, 2010.
110 Special Report No 8/2010: Improving Transport Performance on Trans-European Rail Axes: Have EU Rail Infrastructure Investments Been Effective?, European Court of Auditors, 2010.
111 Audit No. 09/27, SAO Bulletin 4/2010, p. 295.
112 In line with the SAO's audit powers in respect of the EIB it is authorised to audit only direct loans to the Czech Republic and loans to other entities which the Czech Republic guarantees.

B.4.3 Protection of the EU's financial interests

B.4.3.1 Instruments subject to direct centralised management by the Commission

In the case of financial instruments subject to direct centralised management of the Commission, wrongfully paid sums are recovered without action by Member States. This information is monitored in the Commission's ABAC accounting system[113]. 705 recovery orders were registered in the system in 2009; these concerned cases of irregularities and suspected fraud. The total financial impact of these orders on the EU budget was put at €27.5 million, with €1.5 million of that amount falling to 15 cases of suspected fraud.[114] Irregularities in the area of the EU's internal policies amounted to €23.1 million[115] (more than 80% of all irregularities), with most of these identified in education and culture, information society, and research and technological development. Cases where financed actions did not comply with the rules, expenditure was effected with no legal basis, or documents were missing had the greatest impact on the budget. These irregularities were most commonly detected as part of the Commission's administrative controls.

Seven irregularities were detected among beneficiaries from the Czech Republic in 2009; their total value was approx. €118,000[116]. None of these recovery orders was qualified as suspected fraud.

B.4.3.2 Pre-accession instruments

The obligation to report irregularities linked to pre-accession assistance is enshrined in financial memoranda, or memoranda signed by the existing and candidate EU countries on the one hand and the Commission on the other. These regular reports must possess certain requisite features, but States do not always comply fully with this. An analysis by the Commission of the irregularities reported by Member States in 2009[117] reveals that the most common errors are the incorrect or incomplete financial aspects of these reports, missing data on the practices leading to the irregularity, or data on the irregularity's classification (i.e., whether the irregularity is suspected fraud).

In 2009, the Czech Republic made important progress in the monitoring of data and classification of irregularities, as in the previous year the Czech authorities only performed this classification in one of the reported cases; in 2009, this obligation was fulfilled in all cases. The analysis also shows that there is a long delay in the Czech Republic between the occurrence of an irregularity and its detection (4.2 years) compared to the European average (2.5 years) and between the detection and reporting (6.2 months) compared to the EU average (5.8 months).

In 2009, the national authorities of EU Member States reported 706 cases of irregularities with a financial impact of €117 million, which represents an increase of 35% over 2008. More than 80% of the irregularities reported in 2009 were accounted for by Bulgaria and Romania. In total there were 262 cases of suspected fraud with a financial impact of €57 million. Most cases of suspected fraud were detected under SAPARD. Most of the reported irregularities were detected by ex-ante or ex-post audits. The irregularities with the biggest impact on the budget include the forgery of supporting materials, failure to respect the conditions set out in contracts and regulations, and violation of the public procurement rules.

For the year 2009, the Czech Republic reported two irregularities worth approx. €54,000 concerning PHARE. In one case it was found that the final beneficiary had not returned unused finances; the second irregularity involved a violation of the public procurement rules.[118]

In 2008, the Czech Republic had to return a total of €10.52 million to the Commission. Of this sum, €9.35 million was evaluated as ineligible expenditure paid out from the PHARE programme, or from PHARE revolving funds managed

113 The ABAC system, which contains information dating from 2008, only records irregularities where a request for the return of wrongful expenditure has been issued, known as recovery orders.
114 Report from the Commission to the European Parliament and the Council: Protection of the Communities' financial interests – Fight against fraud – Annual Report 2009, COM(2010) 382 of 14 July 2010.
115 Report from the Commission to the European Parliament and the Council: Protection of the Communities' financial interests – Fight against fraud – Annual Report 2009, COM(2010) 382 of 14 July 2010.
116 Annex SEC(2010) 898 to the Report from the Commission to the European Parliament and the Council: Protection of the Communities' financial interests – Fight against fraud – Annual Report 2009, COM(2010) 382 of 14 July 2010.
117 Annex SEC(2010) 898 to the Report from the Commission to the European Parliament and the Council: Protection of the Communities' financial interests – Fight against fraud – Annual Report 2009, COM(2010) 382 of 14 July 2010.
118 Report on the Results of Financial Controls in Public Administration for 2009, Ministry of Finance, 2010.

by the MfRD, respectively (see Chapter B.4.3 of the EU Report 2010). The Czech Republic agreed neither with the settlement of this sum, nor with the Commission's order and thus, based on the Government resolution No. 977 of 23 July 2008, the sum of €9.35 million was not paid. The Commission included the requested sum in the interim payments for programmes of the Structural Funds and the Czech Republic, in reaction to this act, filed an action to the European Court of Justice, or to the Court of First Instance reps., for annulment of such an act. On 15 April 2011, the General Court dismissed in its open session[119] this action against the Commission's order of 7 August 2008 on collection of sums that the Czech Republic has to pay back to the PHARE revolving funds. At the same time, it ordered the Czech Republic to settle the trial costs[120].

According to data provided by the Ministry of Finance, €1.66 million was returned to the Commission in 2009 and a further €2.26 million in 2010. All these irregularities were identified in the context of PHARE.

119 Based on the Lisbon Treaty, the Court of First Instance has been renamed to General Court.

120 Verdict of the General Court (Third Chamber) of 15 April 2011 in the Case T-465/08: Action brought on 15 October 2008 — Czech Republic v Commission

C. Other SAO's activities related to the EU's financial management

C.1 Legal matters

When performing audit work, the SAO checks that legal regulations are mutually consistent and that the legislation governing budget management, accounting, State statistics, and the performance of control, supervisory, and inspection work is satisfactory. It submits its suggestions for adjustments to the legislation to the appropriate authorities in the form of recommendations contained in approved audit conclusions or as part of the interdepartmental comments process initiated by the authors of draft legislation. In 2010, the SAO mentioned the following legal problems in its audit findings[121] and as part of the comments process:

C.1.1 Legislation on contracts on the provision of appropriations provided under ROP

The regional councils of Cohesion regions, which carry out the function of regional OP managing authorities, provide appropriations to projects based on "unnamed contracts"[122] under the Civil Code[123]. In this context, the SAO drew attention to the fact that the Czech legislation[124] does not explicitly regulate either the form of this act in law or its fundamental substantive particulars. There is thus an absence of categorical legislation on the form and substance of the appropriation awarding act for subsidies provided out of the budget of regional councils. Such legislation is standard for other types of subsidies co-financed out of the EU budget, however[125]. This legislative deficiency and the use of contracts under the Civil Code gives rise to situations where evidently public relations (e.g., public administration control of beneficiaries pursuant to the Act on

121 Audit No. 09/26, Issue 1/2011 of the SAO Bulletin.
122 These are contracts that are not specifically regulated by law as a contractual type.
123 Provision of Article 269 (2) of Act No. 513/1991, Commercial Code.
124 In particular Act No. 248/2000, on support for the regional development.
125 E.g., Section 14 of Act No. 218/2000, on budgetary rules and amending certain related acts (Budgetary Rules); Section 11 of Act No. 256/2000, on the State Agricultural Intervention Fund and amending certain other acts (Act on the State Agricultural Intervention Fund).

Financial Control or breach of budgetary discipline by beneficiaries pursuant to the Act on budgetary rules of territorial budgets[126]) are governed by private contracts.

C.1.2 Legislation governing financial corrections for irregularities detected before payment

According to the EU regulations, Member States are obliged to perform financial corrections required in connection with individual or systemic irregularities. These financial corrections consist in annulling an entire contribution to an OP from public funds or part thereof.[127] The Czech legislation explicitly regulates the performance of financial corrections for individual irregularities that were detected after payment or in the course of financing.[128] The SAO drew attention to the fact that the Czech legislation does not cover the performance of financial corrections for irregularities detected before payment is made to a beneficiary. These financial corrections have been hitherto governed solely by the methodological documents of the relevant support providers. Financial corrections performed before payment may have the same consequences for beneficiaries as those done after payment. In the interests of legal certainty for beneficiaries, the Czech legislation should clearly define the competence of the relevant authorities to perform financial corrections before payment; there should be legal rules for determining the size of penalty for the different kinds of irregularity; beneficiaries should be informed in advance of the size of these penalties; and it should be ensured that beneficiaries will not be punished twice for the same irregularity by different authorities empowered to perform financial corrections. Despite the ongoing legislative process, the relevant amendments have not been adopted in this area yet.[129]

C.2 International activities of the SAO

In 2010, as in previous years, the SAO's international activities linked to the EU authorities or the SAIs of EU Member States mainly concerned the financial management of EU budget finances and were linked to significant coordinated audit projects. The engagement the SAO's audit capacities in parallel or coordinated audits with international audit institutions is increasing constantly and occupies a significant place in the SAO's annual audit plans. Within the framework of international cooperation, the practical performance of audit work was complemented by organising of training events of pan-European scope.

C.2.1 Audit work

C.2.1.1 Audits conducted in cooperation with national SAIs

In 2010, the SAO continued its cooperation with the BRH of the Federal Republic of Germany in the field of value added tax administration, with the joint objective of scrutinising the procedures followed by the two countries' tax administrations in the context of international administrative cooperation (audit No. 09/11 "Administration of the Value Added Tax"). The audit also made it possible to check the state and development of measures adopted on the basis of the results of the preceding coordinated audit (audit No. 06/27). It focused on the handling of selected cases of business transactions effected between VAT payers from the Czech Republic and Germany and comparing the VAT control systems in the case of large enterprises in the two countries. The issue of mutual support when recovering VAT arrears was also covered by the cooperation. The output of the parallel audits is a joint report. The details can be found in Chapter B.1.3.

C.2.1.2 Audits conducted in cooperation with the ECA

In July 2010, the Presidents of the SAO and the ECA signed a Memorandum of Understanding, based on which a coordinated audit pilot project targeting the Rural Development Programme was commenced. This is a new

126 Provision of Section 22 of Act No. 250/2000, on budgetary rules for territorial budgets.
127 Article 98 of Council Directive (EC) No. 1083/2006 laying down general provisions on the European Regional Development Fund, the European Social Fund and the *Cohesion Fund* and repealing Regulation (EC) No. 1260/1999.
128 E.g., Sections 44 and 44a of Act No. 218/2000, on the budgetary rules and amending certain related acts (the budgetary rules).
129 Government resolution No. 745 of 20 October 2010 on the Report on Progress in Addressing Selected Legislative Areas with a view to Simplifying the Administration of the Structural Funds and the *Cohesion Fund* of the EU.

form of cooperation that is not widespread within the EU (the ECA only performs similar audits with the SAI of the Netherlands). The cooperation between the two audit institutions in the coordinated audit, with a jointly performed on-the-spot check, results in direct exchange of information, closer sharing of experience, and, given the coordinated approach, a reduction in the burden of audit work placed on the responsible implementing authorities and final beneficiaries in the Czech Republic. This cooperation is being undertaken under audit No. 10/29 “Funds earmarked for improving the environment and landscape under the Rural Development Programme”. The audit conclusions will be published at the end of 2011. This is examined in greater detail in Chapter B.2.2.2.

C.2.1.3 Audits performed in the context of cooperation with the Contact Committee

The completion of a multilateral parallel audit of the costs of control of the Structural Funds was planned for the end of 2010. The purpose of the audit is to map the current costs (including the possible use of technical assistance resources for control of the Structural Funds which EU Member States’ internal control authorities spend on the performance of audit work) and thus to judge their effectiveness and benefits. The SAO participated in this international project by including this objective in the broader framework of audit No. 09/26 “Funds earmarked for transport infrastructure projects under the regional operational programmes”. The SAO drew up a national report on the audit results and sent it in December 2010 to the Working Group on Structural Funds IV, composed of the SAIs of Germany, the Netherlands, and Slovenia.

C.2.1.4 Audit missions of EU institutions in the Czech Republic

The **ECA** fulfils the key role in the external audit of European Union budget finances. Besides the aforementioned coordinated audit project with the SAO, the ECA conducted four audit missions in the Czech Republic in 2010. During these missions, the SAO coordinated the exchange of information provided by the selected auditees. SAO auditors took part in the mission as observers. The audit missions were as follows:

- Audit concerning the European Agricultural Guarantee Fund, focusing on the single area payments scheme. The outputs were used as part of the basis for the DAS for the 2009 financial year.
- Audit concerning Commission Regulation (EC) No 259/2008 and the transparency of the CAP, intended to verify the discharge of the obligations set out in the said Regulation and to judge whether the published data contribute to increasing the transparency of the CAP. The audit results will be published in a special report.
- Audit concerning ROP Southeast co-financed by the ERDF. The audit’s outputs will serve as part of the basis for the DAS for the 2010 financial year.
- Audit concerning the European Agricultural Guarantee Fund, focusing on the single area payments scheme. The outputs will be used as part of the basis for the DAS for the 2010 financial year.

In four other cases, ECA auditors requested cooperation in the form of obtaining documents in which as a rule the SAO participates as a coordinator (e.g., questionnaire-based surveys or other forms of data gathering). The following audits were involved:

- Audit dealing with protected geographical indications and protected designation of origin in Member States.
- Audit concerning OP Transport co-financed by the ERDF.
- Audit concerning industrial and military site renewal projects co-financed by the ERDF.
- Audit concerning the implementation of the legislation in the field of hygiene regulations in slaughter houses.

As in the previous year, SAO auditors’ involvement in the **European Commission’s** audit missions in the Czech Republic took place on an exceptional basis and always in the role of observers. In 2010, they took part in an audit mission concerning restructuring and conversion in the wine sector. Improving mutual awareness of planned audits continues to be a priority.

C.2.2 Exchange of experience and other international cooperation

In keeping with tradition, the most important cooperation took place within the Contact Committee. At its session in 2010, the Contact Committee dealt mainly with the impact of the adoption of the Treaty of Lisbon on audit of EU finances, the role of national Parliaments with regard to the subsidiarity principle and the question of the EU’s financial management. Items under discussion were the planned revision of the EU Financial Regulation, which covers important questions from national audit institutions' perspective, such as the introduction of the tolerable error risk concept (Article 29 of the revised Financial Regulation[130]) or Member States' new control and audit obligations (Article 56 of the revised Financial Regulation, which may also impact on the work of SAIs).

Having reviewed the documentation already drawn up, prepared a proposal for a database of documents linked to public procurement and organised a seminar acquainting auditors with the important outputs, the **Public Procurement Updating Group** was closed down. The working group published *Public Procurement Audit*, containing information about basic principles, guidelines, and a model for public procurement audit, including checklists.

The **Working Group on Common Auditing Standards** was also closed down. Under instruction from the Contact Committee, in previous years it had drawn up recommended standards for financial audit, compliance audit, and performance audit with particular regard to the specific environment of the EU. The outputs approved by the Contact Committee have already been applied by the SAO when drawing up SAO's methodology.

At the Contact Committee meeting, the Supreme Audit Office and the SAI of Romania took over the chair of the **Joint Working Group on Audit Activities**, which is a joint working group of the Contact Committee and the Presidents' Network[131]. The purpose of this working group is to maintain working contacts and develop specific cooperation between the SAIs of the two groups of countries. In 2010 the joint working group took part in organising a workshop on audit and assessment of Public Internal Financial Control, for example. With SIGMA[132] it took part in the organisational, technical, and expert preparation of a meeting of the top-level representatives of the Presidents' Network (March 2011) and their work plan for 2011-2012.

Besides the working groups listed above, the SAO also plays an active role in the Working Group on Value Added Tax, the Working Group on National SAI Reports on EU Financial Management, and the Working Group on the Structural Funds IV. More information about the working groups' outputs can be found on the Contact Committee web site[133].

In October 2010, the SAO and the ECA jointly organised a seminar entitled "Experience with the development and carrying out CAP audits", with financial support from EUROSAI. The details of the seminar's objectives and the focus of its thematic blocks are given in Chapter B.2.5.

130 COM(2010) 815, final wording, issued on 22 December 2010.

131 The Presidents' Network brings together the Presidents of the SAIs candidate and potential candidate countries for the EU accession. Its current members are the SAIs of Turkey, the Former Yugoslav Republic of Macedonia, Croatia, Albania, Bosnia and Herzegovina, Montenegro, Iceland, Serbia, and the European Court of Auditors. The SAO was also a member before the Czech Republic joined the EU.

132 SIGMA (Support for Improvement in Governance and Management) is a joint initiative of the EU and OECD (Organisation for Economic Co-operation and Development), principally financed by the EU. SIGMA supports European candidate countries, potential candidates, and European Neighbourhood countries in their public administration reforms.

133 www.contactcommittee.eu, Status Outline 2010.

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E. Appendices

Appendix 1

Overview of SAO audits carried out in 2009 and 2010 focused partly or fully on funds from the EU budget		
Audit No.	Name	Published in SAO Bulletin (Issue/Year)
09/09	Funds earmarked for implementation of the *Single Programming Document for Objective 2 for the Prague Cohesion Region*	1/2010
09/11	Administration of the Value Added Tax	2/2010
09/12	Support for fisheries in the Czech Republic in accordance with Operational Programmes in 2004–2008	1/2010
09/19	Funds earmarked for railway infrastructure development	2/2010
09/26	Funds earmarked for transport infrastructure projects under the regional operational programmes	1/2011
09/27	Funds earmarked for building roads	4/2010
09/28	Programmes for co-funding projects for building and expansion of winter sports resorts	4/2010
10/01	Funds earmarked for costs of market interventions and export subventions in the Common Market Organisation	4/2010
10/12	Funds provided for the improvement of nature and landscape	2/2011

Source: SAO Bulletins.

Appendix 2

Options for the Future Common Agricultural Policy			
Option	**Direct payments**	**Market measures**	**Rural development**
1	Introduce more equity in the distribution of direct payments between Member States (while leaving unchanged the current direct payment system).	Strengthen risk management tools. Streamline and simplify existing market instruments where appropriate.	Maintain the Health Check orientation of increasing funding for meeting the challenges related to climate change, water, biodiversity, renewable energy, and innovation.
2	Introduce more equity in the distribution of direct payments between Member States and a substantial change in their design. Direct payments would be composed of: • a basic rate serving as income support, • a compulsory additional aid for specific „greening“ public goods through simple, generalized, annual, and non-contractual agri-environmental actions based on the supplementary costs for carrying out these actions, • an additional payment to compensate for specific natural constraints, and • a voluntary coupled support component for specific sectors and regions. Introduce a new scheme for small farms. Introduce a capping of the basic rate, while also considering the contribution of large farms to rural employment.	Improve and simplify existing market instruments where appropriate.	Adjust and complement existing instruments to be better aligned with EU priorities, with support focused on environment, climate change and/or restructuring and innovation, and to enhance regional/local initiatives. Strengthen existing risk management tools and introduce an optional WTO green box compatible income stabilization tool to compensate for substantial income losses. Some redistribution of funds between Member States based on objective criteria could be envisaged.
3	Phase out direct payments in their current form. Provide instead limited payments for environmental public goods and additional specific natural constraints payments.	Abolish all market measures, with the potential exception of disturbance clauses that could be activated in times of severe crises.	The measures would be mainly focused on climate change and environment aspects.

Source: Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions - The CAP towards 2020: Meeting the food, natural resources and territorial challenges of the future. COM(2010) 672 final of 18 November 2010 .

Appendix 3

State of closure of the 2004-2006 programming period				
OP	**Deadline for sending final payment application to the Commission**	**Date on which final payment application was sent to the Commission**		**Current developments regarding the application**
Joint regional OP	30. 9. 2010	29. 9. 2010		The Commission's request for certain information to be added to the final report was delivered on 8 March 2011.
OP RDMA	31. 3. 2010	31. 3. 2010		Final report regarding EAGGF approved; no comments regarding the calculation of the final application; so far no comments regarding the winding-up with regard to EAGGF; second response to the comments on the final report for FIFG sent and second response to the comments on winding-up with regard to FIFG sent; so far no comments on the calculation of the final application.
OP Industry and Enterprise	30. 9. 2010	29. 9. 2010		Delivery of the Commission's request for certain information to be added to the final report is expected.
OP Infrastructure	30. 9. 2010	30. 9. 2010		The Commission's request for certain information to be added to the final report was delivered on 21 February 2011; deadline for response is 21 April 2011.
OOP Human Resources Development	30. 9. 2010	29. 9. 2010		The Commission's request for certain information to be added to the final report delivered unofficially (by e-mail).
SPD 2	30. 9. 2010	29. 9. 2010		The Commission's request for certain information to be added to the final report was delivered on 16 February 2011; deadline for response is 16 April 2011.
SPD 3	30. 9. 2010	29. 9. 2010		The Commission's request for certain information to be added to the final report delivered by e-mail.
EQUAL	30. 9. 2010	29. 9. 2010		The Commission's request for certain information to be added to the final report delivered unofficially (by e-mail).
Interreg Poland	31. 3. 2010	31. 3. 2010		Final payment of €1,725,147.35 received on 19 January 2011; Czech Republic's disagreement with the calculation of the final balance sent to the Commission on 9 March 2011.
Interreg Saxony	30. 9. 2010	30. 11. 2009*	27. 9. 2010	No information is known about the sending of the final balance or approval of the final report.
Interreg Bavaria	31. 3. 2010	29. 10. 2009*	24. 3. 2010	Final report approved on 31 January 2011; final payment to be made after conclusion of ECA audit.
Interreg Slovakia	31. 3. 2010	7. 8. 2009*	30. 3. 2010	The Commission's requests for information to be added to the final report delivered on 10 May 2010 and 1 July 2010; information provided on 11 May 2010 and 6 July 2010 respectively; further developments unknown.
Interreg Austria	31. 3. 2010	29. 10. 2009*	17. 3. 2010	Final payment credited to sub-Paying Authority's (Ministry of Finance of the Czech Republic) account on 14 February 2011.

Source: Information of the MoF of 3. 3. 2011 and 17. 3. 2011.

*Date on which final payment application was sent to the Paying Authority in the partner country

Appendix 4

Overview of European Commission audit and verification missions in 2009 and 2010					
Year	**Commission audit mission**	**Date**	**OP**	**Auditee**	**Audit subject**
2009	DG REGIO, DG EMPL – mise pro ověření zjištěných skutečností	31. 3. – 2. 4. 2009	all OPs	MA, AA	Assessment of compliance under No. 71
					Commission requests for additional information
					MSC2007 monitoring system
					Administrative capacity
2010	DG REGIO	12. 4. – 16. 4. 2010	*ROP Central Bohemia, OP Environment*	AA, entrusted audit body	Methodology of systems audit and operations audit
	DG REGIO	31. 5. – 4. 6. 2010	*OP Enterprise and Innovations*	AA, entrusted audit body	Audit of operations in selected samples
	DG EMPL	31. 5. – 4. 6. 2010	*OP Human Resources and Employment*	AA, entrusted audit body	Audit of selected samples
	DG REGIO	14. 6. – 18. 6. 2010	*OP Transport*	AA, entrusted audit body	Audits of operations
	DG EMPL	21. 6. – 25. 6. 2010	*OP Human Resources and Employment*	AA, entrusted audit body	Audits of system and operations
	DG JUSTICE	12. 7. – 16. 7. 2010	*General Programme “Solidarity and Management of Migration Flows”*	Responsible authority, CA, AA	Audits of system and operations
	DG REGIO	12. 7. – 16. 7. 2010	*ROP Southeast, OP Prague Competitiveness*	AA, entrusted audit body	Audit of systems under ROP and OP Prague Competitiveness
	DG REGIO	6. 9. – 10. 9. 2010	*ROP Central Moravia*	AA, entrusted audit body	Audits of operations
	DG REGIO	4. 10. – 8. 10. 2010	*OP Enterprise and Innovation*	entrusted audit body, IB	Audits of systems, selected processes

Source: Information of the MoF, Audit Authority, of 2. 2. 2011.

Appendix 5

Community programmes in the 2007-2013 financial perspective	
Heading name	**Heading name**
Heading 1a – Competitiveness for growth and employment	7th Framework Programme for Research, Technological Development and Demonstration
	7th Framework Programme of the European Atomic Energy Community (Euratom) for Nuclear Research and Training Activities
	Integrated Action Programme in Lifelong Learning
	CIP (Competitiveness and Innovation Framework Programme)
	TEN (provision of Community financial assistance in the field of trans-European transport and energy networks)
	Marco Polo II
	Galileo
	Community programme for employment and social solidarity – PROGRESS
	European Institute of Innovation and Technology
	Customs
	Fiscalis
	Hercule II
	Community Statistical Programme
	Programme for Modernisation of European Enterprise and Trade Statistics (MEETS)
	Erasmus Mundus
	Pericles
	European Globalisation Adjustment Fund
	Decommissioning Assistance Programme
	Safer Internet Programme
	ISA (Interoperability Solutions for European Public Administrations)
	Community Programme to Support Financial Services, Financial Reporting and Auditing
Heading 2 – Preservation and management of natural resources	LIFE+
Heading 3a – Freedom, security and justice	Solidarity and Management of Migration Flows
	Security and Protection of Liberties
	Fundamental Rights and Justice
Heading 3b - Citizenship	Youth in Action
	Culture 2007-2013
	MEDIA 2007
	Europe for Citizens
	Civil Protection Financial Instrument
	Programme of Community Action in the Field of Health
	Programme of Community Action in the Field of Consumer Policy
	Solidarity Fund
Heading 4 – The EU as a global player	Pre-accession instrument (IPA)

Source: www.mfcr.cz and EU legislation establishing the relevant programmes.

Appendix 6

Overview of PHARE and Transition Facility programmes – state as of 31 December 2010 (in €)					
Programme code	Programme name	Programme allocation	Finances transferred to beneficiaries	Share of drawdown (%)	Programme status
CZ 98.06-12	PHARE National Programme 1998	22,450,000.00	18,666,826.56	83.15	incomplete
CZ 98.04	CBC PHARE 1998 - Germany	7,000,000.00	6,695,498.80	95.65	completed
CZ 98.05	CBC PHARE 1998 - Austria	2,900,000.00	2,812,863.45	97.00	completed
Total for programmes in 1998		**32,350,000.00**	**28,175,188.81**	**87.09**	
CZ 99.01-05	PHARE National Programme 1999	16,000,000.00	13,811,146.81	86.32	incomplete
CZ 99.08	Large Scale Infrastr. Facility – part IV	2,400,000.00	1,098,300.63	45.76	incomplete
CZ 99.09	CBC PHARE 1999 - Poland	3,000,000.00	2,931,171.21	97.71	incomplete
CZ 99.10	Large Scale Infrastr. Facility - part V	14,200,000.00	13,849,964.00	97.53	completed
CZ 99.12	CBC PHARE 1999 - Austria	10,600,000.00	10,317,463.44	97.33	incomplete
CZ 99.13	CBC PHARE 1999 - Slovakia	2,000,000.00	1,727,601.49	86.38	completed
CZ 99.14	CBC PHARE 1999 - Germany	29,400,000.00	28,607,487.08	97.30	completed
CZ 99.15	Consensus III	2,000,000.00	1,778,344.94	88.92	completed
CZ 99.16	Preparation of projects	2,000,000.00	1,815,487.29	90.77	completed
Total for programmes in 1999		**81,600,000.00**	**75,936,966.89**	**93.06**	
CZ 00.02-10	PHARE National Programme 2000	59,000,000.00	49,822,035.82	84.44	incomplete
CZ 00.11	Access	1,670,000.00	1,558,462.03	93.32	incomplete
CZ 00.12	CBC PHARE 2000 - Germany	10,000,000.00	9,629,240.91	96.29	completed
CZ 00.13	CBC PHARE 2000 - Poland	5,000,000.00	4,865,887.86	97.32	completed
CZ 00.14	CBC PHARE 2000 - Austria	4,000,000.00	3,906,482.69	97.66	completed
CZ 00.16	Supplementary investment programme	8,100,000.00	8,089,043.85	99.86	completed
Total for programmes in 2000		**87,770,000.00**	**77,871,153.16**	**88.72**	
CZ 01.01-10	PHARE National Programme 2001	65,400,000.00	52,589,028.97	80.41	incomplete
CZ 01.11	CBC PHARE 2001 - Austria	4,000,000.00	3,972,844.06	99.32	completed
CZ 01.12	CBC PHARE 2001 - Germany	10,000,000.00	9,854,542.09	98.55	completed
CZ 01.13	CBC PHARE 2001 - Poland	5,000,000.00	4,936,944.97	98.74	completed
CZ 01.14	Horizontal Programme for Community Support in the Field of Nuclear Safety	2,190,000.00	1,911,266.73	87.27	incomplete
Total for programmes in 2001		**86,590,000.00**	**73,264,626.82**	**84.61**	
CZ 02.01-09	PHARE National Programme 2002 – part I	78,493,285.00	62,978,669.88	80.23	incomplete
CZ 02.10	PHARE National Programme 2002 – part II	6,300,000.00	5,183,976.65	82.29	incomplete
CZ 02.11	CBC PHARE 2002 - Austria	4,000,000.00	3,944,208.16	98.61	completed
CZ 02.12	CBC PHARE 2002 - Germany	10,000,000.00	6,775,834.99	67.76	incomplete
CZ 02.13	CBC PHARE 2002 - Poland	5,000,000.00	4,939,018.10	98.78	incomplete
Total for programmes in 2002		**103,793,285.00**	**83,821,707.78**	**80.76**	

Overview of PHARE and Transition Facility programmes – state as of 31 December 2010 (in €)					
Programme code	**Programme name**	**Programme allocation**	**Finances transferred to beneficiaries**	**Share of drawdown (%)**	**Programme status**
CZ03.01-08	PHARE National Programme 2003 – part I	38,500,000.00	35,514,113.85	92.24	incomplete
CZ03.08.02-08.09	PHARE National Programme 2003 – part II	56,680,000.00	49,054,662.81	86.55	incomplete
CZ03.77	CBC PHARE 2003 - Poland	5,000,000.00	4,980,294.96	99.61	incomplete
CZ03.79	CBC PHARE 2003 - Austria	4,000,000.00	3,603,834.91	90.10	incomplete
CZ03.95	CBC PHARE 2003 - Germany	10,000,000.00	9,130,276.44	91.30	incomplete
CZ03.12	Horizontal Programme for Community Support in the Field of Nuclear Safety for 2003	1,830,000.00	1,768,577.02	96.64	completed
Total for programmes in 2003		**116,010,000.00**	**104,051,759.99**	**89.69**	
	Horizontal Programme Preparing Candidate Countries for Extended Decentralisation (EDIS)	300,000.00	295,817.00	98.61	completed
	Horizontal Programme for Community Support in the Field of Nuclear Safety for 2002 (NUS 2002)	4,060,000.00	3,717,219.70	91.56	incomplete
	Nuclear Safety	1,100,000.00	936,334.18	85.12	completed
	Replacement and Repair of Equipment Damaged by Floods in 2002 in the Nuclear Research Institute	455,000.00	454,636.00	99.92	completed
Total for horizontal programmes		**5,915,000.00**	**5,404,006.88**	**91.36**	
Total for programmes PHARE and CBC 98-03		**514,028,285.00**	**448,525,410.33**	**87.26**	
	Transition Facility 2004	17,100,000.00	12,122,941.29	70.89	incomplete
	Transition Facility 2005	11,800,000.00	9,716,915.56	82.35	incomplete
	Transition Facility 2006	7,160,000.00	6,149,948.43	85.89	incomplete
Total for programmes Transition Facility		**36,060,000.00**	**27,989,805.28**	**77.62**	

Source: Information of the MoF – Department 55 – National Fund of 17. 3. 2011.