

FINANCING AGREEMENT¹

The European Commission, hereinafter referred to as "**THE COMMISSION**", acting for and on behalf of the European Community, hereinafter referred to as "**THE COMMUNITY**"

on the one part, and

The Government of the Republic of Bulgaria, hereinafter referred to as "**THE RECIPIENT**"

on the other part,

HAVE AGREED AS FOLLOWS:

The measure referred to in Article 1 below shall be executed and financed out of the budget resources of THE COMMUNITY in accordance with the provisions set out in this Agreement. The technical, legal, and administrative framework within which the measure referred to in Article 1 below shall be implemented is set out in the General Conditions annexed to the Framework Agreement between THE COMMISSION and THE RECIPIENT, and supplemented by the terms of this Agreement and the Special Provisions annexed hereto.

ARTICLE 1 - NATURE AND SUBJECT

As part of its aid programme, THE COMMUNITY shall contribute, by way of grant, towards the financing of the following MEASURE:

Programme number: **BG 2005/017-684**

Title: **Phare Floods Assistance Programme for the Republic of Bulgaria (Phare National Programme part III) in 2005**

Duration: **Until 30 November 2007**

ARTICLE 2 - COMMITMENT OF THE COMMUNITY

The financial contribution of THE COMMUNITY is fixed at a maximum of **12,3 M€** hereinafter referred to as "**THE EC GRANT**".

¹ The Financing Agreement structure is as follows : 1. the cover pages with the references to the country concerned, amount and authority to sign, 2. Framework Agreement incl. Annex A and Annex B; Annex C – Special Conditions (the text of the adopted financing proposal starting from **Description and Objectives** onwards; and Annex D 'Visibility/Publicity).

ARTICLE 3 - DURATION AND EXPIRY

For the present MEASURE, THE EC GRANT is hereby available for contracting until **30 November 2007** subject to the provisions of this Agreement. All contracts must be signed by this date. Any balance of funds of the EC GRANT, which have not been contracted by this date shall be cancelled.

The deadline for execution of contracts of THE EC GRANT is **30 November 2008**. THE COMMISSION may however, in exceptional circumstances, agree to an appropriate extension of the contracting period or of the contract execution period, should this be requested in due time and properly justified by THE RECIPIENT. Disbursements of funds may continue for up to 12 months after the deadline for the execution of contracts to meet liabilities properly incurred through the execution of the contracts entered into under this programme. This Financing Agreement shall expire once those disbursements have been completed. All the funds which have not been disbursed by that time shall then be returned to the Commission.

ARTICLE 4 - ADDRESSES

Correspondence relating to the execution of THE MEASURE, stating THE MEASURE'S number and title, shall be addressed to the following:

for the COMMUNITY:

Delegation of the European Commission

9 Moskovska Str
PO Box 668
BG-1000 Sofia
Bulgaria

Tel: (+359 2) 933 5252

Fax: (+359 2) 933 5233

for THE RECIPIENT:

Mr Plamen Oresharski

Minister of Finance
102 Rakovski St
BG-1040 Sofia
Bulgaria

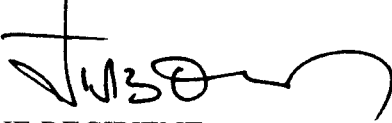
ARTICLE 5 - NUMBER OF ORIGINALS


This Agreement is drawn up in duplicate in the English language.

ARTICLE 6 - ENTRY INTO FORCE

This Agreement shall enter into force on the date on which it has been signed by both parties. No expenditure incurred before this date is eligible for the EC GRANT.

The Annexes shall be deemed an integral part of this Agreement.

Done at ... Sofia
Date 27.02.2006

for THE RECIPIENT
Plamen Oresharski
Minister of Finance

Done at ... Sofia
Date 27.02.2006

for THE COMMUNITY
Dimitris Kourkoulas
Head of EC Delegation

Encl.

1. Framework Agreement (incl. Annexes A & B)
2. Special Provisions (Annex C)
3. Visibility/Publicity (Annex D)

ANNEX C TO THE FINANCING AGREEMENT

Phare Floods Assistance Programme for the Republic of Bulgaria in 2005

(National programme part III)

1. OBJECTIVES AND DESCRIPTION

The Phare National Programme 2005 has been deployed according to the 6 overarching priorities that have been set for the MAP 2004-2006. For the part III it concentrates on two sectoral objectives:

- Objective 10 / Administrative reform and capacity;
- Objective 11 / ESC.

It has to be noted that this programme has the objective to ensure that Structural Funds can be implemented on accession in accordance with EU policy and procedures, with maximum impact on economic and social cohesion and to contribute to the economic development of regions affected by flooding, by mitigating the consequences of the floods and improving the living conditions of their inhabitants including by a better preparation of crisis management at central and local levels.

The programme is to contribute more widely to improvements in the living conditions of inhabitants of the areas affected by the floods of June, July and August 2005.

Summary descriptions¹ of the individual projects grouped under the sectoral objectives are as follows:

Objective 10: Administrative reform and capacity

<i>BG2005/017-684.02: Support to sustainable crisis management at central and local level</i>	
<i>Duration / Phase</i>	<i>2005</i>
<i>Twinning</i>	<i>N/A</i>
<i>Phare budget</i>	<i>€ 3.15 M</i>
<i>Implementing Agency</i>	<i>CFCU</i>

The aim of this project is to reinforce and increase the sustainability of the Bulgarian capacity to manage and react to crises, and natural disasters such as flooding, earth quakes and forest fires in particular. The project should result in the development of the relevant methodologies and standards, the relevant institutional structures and support mechanisms being fully operational, including the speedy mobilisation of financial means to address catastrophes, the establishment of a flood forecast and other natural calamities and early warning system, and relevant staff being fully trained and prepared to address crises. The project provides for an envelope enabling the purchase of directly-relevant equipment.

¹ Descriptions are indicative; some details may be changed

Objective 11: Economic and Social Cohesion

<i>BG2005/017-684.01: Post-flood rehabilitation and relief scheme</i>	
<i>Duration / Phase</i>	<i>2005</i>
<i>Twining</i>	<i>No</i>
<i>Phare budget</i>	<i>€ 9.15 M</i>
<i>Implementing Agency</i>	<i>Ministry of Regional Development and Public Works</i>

The aim of this project is to reconstruct local transport and environmental infrastructure as well as local educational and health care-related establishments damaged by flooding in the Spring-Summer of 2005, thereby contributing to the economic recovery and development of the regions worst affected by the flooding. More widely, it will contribute to the avoidance of an interruption in the process of preparation for accession notably regarding regional policy. The relevant procedures are identified in the project fiche insofar as they are not indicated in this project description. These procedures will include necessary derogations so as to ensure the quick implementation required. For example it has to be noted that subcontracting by beneficiaries of the grants shall be subject to Bulgarian public procurement law and not the PRAG. Relevant documentation, however, will have to be kept by the beneficiaries for 5 years after the expiry of the individual grants. The project and contract documentation can be in the Bulgarian language. The invitation to submit proposals, selection and approving the Evaluation Report may take place before the signature of the Financing Agreement. Grant Contracts, however, will only be signed after the signature of the Financing Agreement. The grant scheme will be publicised as widely as possible. The size for individual grants will be from 50.000 EUR to 300.000 EUR (Phare contribution). And the call for proposals will run, exceptionally, for 30 days.

The project also includes a small budget for technical assistance to assist the Implementing Agency to manage the programme, and for an audit of the project. This will be procured according to standard PRAG procedures.

Lessons Learned

This specific programme, in particular the specific derogations enabling the speedy mobilisation of the grant scheme, is mainly based on the experience related to the floods that occurred in 2002 in Czech Republic and financed by Phare projects CZ 01.10.04: "Flood Reparation Programme" and CZ 2002/000-282.02.03: "Rehabilitation of Flooded Areas - Support to Assisting CSOs". Lessons from the "Flood Mission" of July 2005, performed by Member State experts have also been taken into account in the design of this programme.

Overall programme conditionalities

Before the Financing Agreement between the Commission and the Government of Bulgaria is signed, the National Aid Coordinator will satisfy the Commission that adequate steps have been taken to staff and resource adequately the National Fund, CFCU, Ministry of Regional Development and Public Works, other Implementing Agencies and project management units involved in implementing this programme.

Before the Financing Agreement between the Commission and the Government of Bulgaria is signed, the National Aid Coordinator will confirm the availability of the national co-financing indicated in each project fiche, and the modalities for combining Phare and national co-financing when projects are contracted.

Any project involving the supply of equipment and works requires national co-financing as shown in the relevant project fiche. In addition, all operational and running costs and the maintenance of the equipment will be provided by the final beneficiaries.

If the total cost of equipment or works is less than the amount envisaged in the fiche, the amount of Phare support will be reduced to maintain unchanged the relative proportions of Phare support and national co-financing shown in the fiche. If the total cost is greater than the amount envisaged in the fiche, the extra support required will be provided by additional national co-financing.

Before the Financing Agreement between the Commission and the Government of Bulgaria is signed, the National Aid Coordinator will satisfy the Commission that draft terms of reference and technical specifications have been prepared, as appropriate, to allow each project to be launched immediately.

For projects involving more than one Bulgarian Ministry or agency, the National Aid Co-ordinator will ensure that effective mechanisms for co-operation and co-ordination between such Ministries or agencies are in place. The National Aid Co-ordinator will undertake thorough reviews of progress on implementation of the projects listed at least every three months from the time the Financing Agreement is signed until the final date for contracting.

If these reviews indicate that by the first quarter of the final year for contracting (2007 unless otherwise specified) there is a high risk of a project or component of a project not being contracted, the Commission reserves the right to take remedial action including, if necessary, reallocating funds to other purposes or cancelling projects or components thereof.

Further project-specific conditionalities are described in the relevant project fiches.

2. BUDGET

2.1. Budget Table for 2005

No. and OBJECTIVE	Phare support			Co-financing		TOTAL
	IB	INV	Total Phare (in €M)	Other sources (**)	National public fund (*)	
10 - Administrative reform and capacity	2.10	1.05	3.15	0	0.35	3.50
11 - ESC	0.15	9.0	9.15	0	3.0	12.15
TOTAL	2.25	10.05	12.30	0	3.35	15.65

(The distribution of figures between the budget lines is indicative within the limits of Art. 5 MoU NF)

(*) Contribution from national, regional, local, municipal authorities, FIs loans to public entities, funds from public enterprises.

(**) Private funds, FIs loans to private entities.

2.2. Principle of Co-Financing

In accordance with the Phare Guidelines, all investment projects supported by Phare must receive co-financing from national public funds.

The Community contribution may amount to up to 75% of the total eligible public expenditure. Taxes are not an element eligible for co-financing.

Co-financing for Institution Building projects is provided by the Beneficiary Country bearing certain infrastructure and operational implementation costs, through financing the human and other resources required for effective and efficient absorption of Phare assistance.

3. IMPLEMENTING AGENCIES

Implementing Agencies will be responsible for sub-programmes as follows:

The Ministry of Regional Development and Public Works will be the Implementing Agency for all programmes and sub-programmes of project **2005/017-684.01**: "Flood rehabilitation and relief scheme".

The Central Finance and Contracts Unit (CFCU), Ministry of Finance will be the Implementing Agency for all programmes and sub-programmes of project **2005/017-684.02**: "Support to the sustainable crisis management system at central and local level".

4. IMPLEMENTATION ARRANGEMENTS

4.1. Method of Implementation

Implementation of the programme will follow Art. 53 (1) b (second alternative) of the Financial Regulation². The Beneficiary Country will continue to ensure that the conditions laid down in Art. 164 (1) (a) - (e) of the Financial Regulation are respected at all times.

Until the accreditation of Implementing Agencies foreseen by Art. 12 (2) of Regulation 1266/1999³, project selection, tendering and contracting by the Beneficiary Country will be subject to ex-ante approval by the Commission.

4.2. General rules for Procurement

Procurement shall follow the provisions of Part 2, Title IV of the Financial Regulation and Chapter 3 of Part 2, Title III of its Implementing Rules⁴, as well as the Commission Decision SEC (2003) 387/2⁵.

The Contracting Authorities shall also use the procedural guidelines and standard templates and models facilitating the application of the above rules provided for in the "Practical Guide to contract procedures financed from the general EC budget in the context of external actions" ("Practical Guide") as published on the EuropeAid website⁶ at the date of the initiation of the procurement or grant award procedure.

In line with Art. 164 of the Financial Regulation, the Commission may decide to allow the Contracting Authorities entrusted with decentralised management responsibilities to execute procurement in accordance with national legislation and guidelines transposing the European Union Public Procurement Directives.

4.3. Grant Schemes

For grant schemes the precise implementation arrangements will be specified in the relevant project fiches in line with the following principles:

The procedures and formats to be used in the implementation of the schemes and award of the grants will follow the procurement rules for External Actions. In particular, due care will be given to the selection process of the projects. Grants will

² Council Regulation (EC, Euratom) 1605/2002 of 25 June 2002; OJ L 248; 16.9.2002; p. 1

³ Council Regulation (EC) 1266/1999 of 21 June 1999; OJ L 161; 26.6.1999; p. 68

⁴ Commission Regulation (EC; Euratom) 2342/2002 of 23 December 2002; OJ L 357; 31.12.2002; p.1 as last amended by Commission Regulation (EC, Euratom) n°1261/2005 of 20 July 2005; OJ L 201; 02.08.2005; p. 3

⁵ Commission Decision SEC (2003) 387/2 on Rules and procedures for service, supply and works contracts financed from the general budget of the European Communities in the context of co-operation with third countries, adopted on March 25, 2003

⁶ current address: http://europa.eu.int/comm/europeaid/tender/gestion/index_en.htm

be awarded in conformity with the provisions of chapter 6 of the Practical Guide, and following the principles of Phare decentralised management. Prior to EDIS accreditation, the ex-ante approval of the Commission Delegation in Bulgaria will be required.

The competent PAO for the programme under which the grant scheme is financed has to retain his/her contractual and financial responsibility for the implementation of the schemes. In particular, the PAO has to formally approve the call for proposals, application forms, evaluation criteria, as well as the selection process and results. The PAO also has to sign the grant agreements with the beneficiaries and to ensure adequate monitoring and financial control under his/her authority and responsibility. With this reservation, the management can be decentralised from the PAO to the appropriate bodies at sectoral or regional level.

Specific derogations are included in each project fiche of this programme for the implementation of selected projects through provision of works, supplies and services, which are sub-contracted by the final beneficiaries of the individual grants.

The financial commitments in Phare terms will be effected at the date of signature of the grant agreements by the competent PAO. The projects should be fully implemented before the expiry date for contract execution of the corresponding Financing Agreement.

4.4. Implementation Principles for Twinning Projects

N/A.

5. MANAGEMENT OF ASSISTANCE

5.1. Project Management

5.1.1. Responsibilities

The National Aid Co-ordinator (NAC) will have overall responsibility for programming and monitoring of Phare programmes.

The National Authorising Officer (NAO) and the NAC shall be jointly responsible for the co-ordination between Phare, ISPA and SAPARD, as well as the Structural and Cohesion Funds.

The NAO and the Project Authorising Officer (PAO) will ensure that the programmes are implemented in line with the procedures laid down in the instructions of the Commission. They will also ensure that all contracts required to implement the Financing Agreement are awarded using the procedures and standard documents for External Actions in force at the time of implementation, and that EU state aid rules are respected.

5.1.2. *Project Size*

In accordance with the Phare Guidelines and given the specific objectives of this programme, the minimum project size rule (€ 2 million) does not apply. The main reason is that this programme aims at covering urgent needs following the floods of summer 2005 in Bulgaria.

5.1.3. *Deadline for contracting and execution of contracts, programming deadline*

(1) All contracts must be concluded by no later than November 30, 2007. This deadline, however, may be extended by the Head of the EC Delegation, case by case, on a duly justified basis.

(2) All contracts must be executed by no later than November 30, 2008.

In no case can the contracting period for projects implemented under this programme exceed three years after the date of the global commitment (Art. 166 (2) FR). Budgetary commitments which have not given rise to payments during three years counted from the date of the legal commitment will be de-committed (Art. 77 (3) FR).

(3) Under DIS, a complete tender dossier must be submitted to the Delegation for approval by no later than 6 months after the signature of the Financing Agreement. In case of non-compliance, the Beneficiary Country will inform the JMC, which may recommend reallocation or cancellation of funds in accordance with Art. 5 of the MoU on the National Fund.

5.1.4. *Environmental Impact Assessment and Nature Conservation*

The procedures for environmental impact assessment as set down in the EIA-directive⁷ are fully applicable for all investment projects under Phare. For some investments financed by this "Phare Flood assistance programme", specific derogations maybe requested and submitted to an ex-ante approval by the EC Delegation. If the EIA-directive has not yet been fully transposed, the procedures should be similar to the ones established in the above-mentioned directive. If a project would fall within the scope of annex 1 or annex 2 of the EIA-directive, the carrying out of the EIA-procedure must be documented⁸.

If a project is likely to affect sites of nature conservation importance, an appropriate assessment according to Art. 6 of the Habitats-directive must be documented⁹.

All investments shall be carried out in compliance with the relevant Community environmental legislation. The Project Fiches will contain specific clauses on

⁷ DIR 85/337/EEC; OJ L 175/40; 5.7.1985, as amended

⁸ in Annex EIA to the corresponding investment project fiche.

⁹ in Annex Nature Conservation to the corresponding investment project fiche

compliance with the relevant EU-legislation in the field of the environment according to the type of activity carried out under each investment project.

5.2. Financial Management

5.2.1. Principles and Responsibilities

The National Fund in the Ministry of Finance, headed by the NAO, will supervise the financial management of the programme, and will be responsible for reporting to the European Commission. The NAO shall have the overall responsibility for financial management of the Phare funds, and the full accountability for the Phare funds of a programme until the closure of that programme.

The NAO shall ensure that the Phare rules, regulations and procedures pertaining to reporting and financial management are respected, and that a reporting and project information system is functioning.

The Commission will make payments to the NF in accordance with the Memorandum of Understanding signed between the Commission and the Republic of Bulgaria in December 1998.

Payments will be made following requests from the NAO onto a separate bank account, denominated in €, which will be opened and managed by the National Fund in the central bank or in a Government guaranteed bank. In principle, all bank accounts will be interest bearing.

According to Articles 3 & 4 of the implementing rules of the Financial Regulation accrued interest is the property of the Beneficiary Country. The NAO must however ensure that the accrued interest is actually registered in its entirety as revenue in the national budget. Furthermore the NAO will ensure a regular reporting of the interest via Perseus.

5.2.2. Payments to the National Fund

A first payment¹⁰ of up to 20% of the funds to be managed locally¹¹, will be sent to the NF following signature of the Financing Agreement and the Implementing Agreements between the NF and the Implementing Agencies (IAs)/Central Finance and Contracts Unit (CFCU). Furthermore, the NAO must submit to the Commission the designation of the PAOs and a description of the system put in place, highlighting the flow of information between the NF and the IA/CFCU and the manner in which the payment function between them will be carried out.

Two further payments¹² of up to 30% of the funds to be managed locally¹³ will be made. The second payment will be triggered when 5 % of the total budget in force¹⁴

¹⁰ representing pre-financing as defined in Art. 105 (1) of the Implementing Rules to the Financial Regulation

¹¹ excluding the amount foreseen for Community Programmes

¹² representing interim payments or the renewal of pre-financing as defined in Art. 105 (1) of the Implementing Rules to the Financial Regulation

has been disbursed by the IAs and the CFCU. The third payment may be requested when 35% of the total budget in force¹⁵ has been disbursed.

A final fourth payment will be made when 70 % of the total budget in force¹⁶ has been disbursed and all contracts have been signed.

Exceptionally the NAO may request more than the percentage agreed where it can be demonstrated by a cash-flow projection that the cash-flow requirements in the subsequent period will exceed such percentage. In cases where the aggregate of the funds deposited in the NF, CFCU and IAs accounts exceeds 15% of the total budget in force for the programme the Commission may exceptionally authorise a payment, if the NAO provides duly substantiated evidence that contractual obligations cannot be met with the funds available.

5.2.3. Payments from the National Fund to the Implementing Agency

The National Fund will make payments to IAs, including the CFCU, in accordance with Implementing Agreements signed between the NF and the IAs/CFCUs. Bank accounts for sub-programmes shall be opened in the name of the relevant Implementing Agency/CFCU in charge of financial management of the sub-programme in line with Art. 13 of the MoU on the National Fund.

As long as implementation follows DIS, each individual Implementing Agreement must be endorsed in advance by the European Commission. In cases where the NF is itself the paying agent for the CFCU/IA there will be no payments from the NF to the CFCU. The CFCU and the IAs must each be headed by a Programme Authorising Officer (PAO) appointed by the NAO after consultation with the NAC. The PAO will be responsible for all operations carried out by the relevant CFCU/IA.

5.2.4. Payments to the National Fund for Participation in Community Programmes and Agencies

N.A.

5.2.5. Payments in Case of Contractual Retention Clauses

For those contracts with contractual retention clauses (e.g. funds retained for a warranty period), the Implementing Agency assumes full responsibility for managing the funds until final payment is due, as well as for ensuring that the said funds will only be used to make payments related to the retention clauses.

¹³ excluding the amount for Community Programmes

¹⁴ excluding the amount for Community Programmes

¹⁵ excluding the amount for Community Programmes

¹⁶ excluding the amount for Community Programmes

The IA further assumes full responsibility towards the contractors for fulfilling the obligations related to the retention clauses. Funds not paid out to the contractors after final payments have been settled shall be reimbursed to the Commission.

5.2.6. Closure of Expenditure and Clearance of Accounts

No later than sixteen months after the end of execution of contracts, the NF will submit a final declaration of expenditure covering both PHARE support and co-financing and an attestation regarding the regularity, accuracy and veracity of the accounts transmitted. The final certified expenditure should at this point equal the original value of the contracts minus any deductions and savings agreed with contractors in the course of implementation. This should also equal payments made plus any sums outstanding on account of contractual retention.

If the payments received from the Commission exceed the final certified expenditure, the NF shall return the excess to the Commission at the time of submitting the final declaration. If there are any outstanding payments (with the exception of contractual retention funds), the NF should provide an explanation and a forecast when payment will be finalised. The NF shall report on progress on contractual retention funds and outstanding payments on a quarterly basis. If they are not paid to the contractor, they shall be returned to the Commission.

After evaluation of the final declaration, the Commission will state its view on any expenditure to be excluded from Community funding, where it finds that expenditure has not been executed in compliance with Community rules.

The results of the Commission's checks and its conclusions to exclude expenditure from financing will be notified in writing to the NF, which shall be given one month to transmit its reply in writing.

If no agreement is reached within one month of receipt of the NF's written reply, the Commission shall decide and establish the amounts to be excluded, having regard in particular to the degree of non-compliance found, the nature and gravity of the infringement as well as the financial loss suffered by the Community.

Following the decision about amounts to be excluded, all ineligible expenditure will be recovered without prejudice to the treatment of irregularities and subsequent financial corrections stipulated below.

The funds will be recovered either by direct reimbursement from the NF or by compensation in accordance with Community rules.

6. MONITORING AND EVALUATION

Project implementation will be monitored through the Joint Monitoring Committee (JMC). It includes the NAO, the NAC and the Commission services. The JMC will meet at least once a year to review all Phare funded programmes in order to assess their progress towards meeting the objectives set out in the Financing Agreements and the Accession Partnership. The JMC may recommend a change of priorities and/or reallocation of Phare funds. Furthermore, the JMC will review the progress of

all pre-accession EU-funded assistance programmes once a year (Phare, ISPA, SAPARD).

For the Phare programme, the JMC will be assisted by Sectoral Monitoring Sub-Committees (SMSC), which will include the NAC, the PAO of each Implementing Agency (and the CFCU where applicable) and the Commission Services. The SMSC will review in detail the progress of each programme, including its components and contracts, assembled by the JMC into suitable monitoring sectors. Each sector will be supervised by one SMSC on the basis of regular monitoring reports produced by the Implementing Agency, and interim evaluations undertaken by independent evaluators. The SMSC will put forward recommendations on aspects of management and design, ensuring that these are effected. The SMSC will report to the JMC, to which it will submit overall detailed opinions on all Phare financed programmes in its sector.

The Commission services shall ensure that this programme will be subject to interim (either centralised or decentralised) and/or ex post evaluations.

7. AUDIT, FINANCIAL CONTROL, ANTI-FRAUD MEASURES, PREVENTIVE AND CORRECTIVE ACTIONS

7.1. Supervision and Financial Control by the Commission and the European Court of Auditors

All Financing Agreements as well as all resulting contracts are subject to supervision and financial control by the Commission (including the European Anti-Fraud Office) and audits by the European Court of Auditors. As long as EDIS is not yet applicable to the Implementing Agencies in the Beneficiary Country, this includes measures such as ex-ante verification of tendering and contracting carried out by the Delegation in the Beneficiary Country.

In order to ensure the efficient protection of the financial interests of the Community, the Commission (including the European Anti-Fraud Office) may conduct on-the-spot checks and inspections in accordance with the procedures foreseen in Council Regulation (EC, Euratom) 2185/96¹⁷.

The controls and audits described above are applicable to all contractors and subcontractors who have received Community funds.

Without prejudice to the responsibilities of the Commission and the European Court of Auditors¹⁸, the accounts and operations of the National Fund and, where applicable, the CFCU and all relevant Implementing Agencies may be checked at the Commission's discretion by the Commission itself or by an outside auditor contracted by the Commission.

¹⁷ Council Regulation (EC, Euratom) 2185/96 of 11. November 1996, OJ L 292; 15.11.1996; p. 2

¹⁸ as referred to in the General Conditions relating to the Financing Memorandum" attached to the Framework Agreement

7.2. Obligations of the Beneficiary Country

7.2.1. *Audit and Financial Control*

In order to ensure sound financial management of the Phare funds, the Beneficiary Country must have a system for management and control of assistance in accordance with generally accepted principles and standards in place. This system shall fulfil the requirements set out in Art. 164 of the Financial Regulation, and in particular provide adequate assurance of the correctness, regularity and eligibility of claims on Community assistance.

The Beneficiary Country's management and control systems shall provide a sufficient audit trail, as defined in Art. 7 (2) of Commission Regulation 438/2001¹⁹.

The competent national financial control authority shall carry out appropriate financial controls of all actors involved in the implementation of the programme.

Each year an audit plan and a summary of the findings and main recommendations of the audits carried out and an outline of the follow-up given to past audit recommendations shall be sent to the Commission. Audit reports shall be at the disposal of the Commission.

7.2.2. *Preventive Measures*

The Beneficiary Country shall take any appropriate measure to prevent and counter active and passive corruption²⁰ practises at any stage of the procurement procedure or grant award procedure, as well as during the implementation of corresponding contracts.

The authorities of the beneficiary country, including the personnel responsible for the implementation of the programme, shall also undertake to take whatever precautions are necessary to avoid any risk of conflict of interest, and shall inform the Commission immediately of any such conflict of interest or any situation likely to give rise to any such conflict.

¹⁹ Commission Regulation (EC, Euratom) 438/2001 of 2 March 2001, OJ L 63; 3.3.2001, p.21

²⁰ Active corruption is defined as the deliberate action of whosoever promises or gives, directly or through an intermediary, an advantage of any kind whatsoever to an official for himself or for a third party for him to act or to refrain from acting in accordance with his duty or in the exercise of his functions in breach of his official duties in a way which damages or is likely to damage the European Communities' financial interests.

Passive corruption is defined as the deliberate action of an official, who, directly or through an intermediary, requests or receives advantages of any kind whatsoever, for himself or a third party, or accepts a promise of such advantage, to act or to refrain from acting in accordance with his duty or in the exercise of his functions in breach of his official duties in a way which damages or is likely to damage the European Communities' financial interests.

7.2.3. *Anti-Fraud Measures and Corrective Actions*

Beneficiary Countries shall, in the first instance, bear the responsibility to ensure investigation and satisfactory treatment of suspected or actual cases of fraud and irregularities following national or Community controls.

The national authorities shall ensure the functioning of a control and reporting mechanism equivalent to the one foreseen in Commission Regulation 1681/94²¹.

In particular, all suspected or actual cases of fraud²² and irregularity²³ as well as all measures related thereto taken by the national authority must be reported to the Commission services without delay. Should there be no suspected or actual cases of fraud or irregularity to report, the Beneficiary Country shall inform the Commission of this fact within two months following the end of each quarter.

In case of irregularity or fraud, the Beneficiary Country shall make the necessary financial corrections required in connection with the individual irregularity. The corrections made by the Beneficiary Country shall consist in cancelling all or part of the Community contribution. The Community funds released in this way may be re-used by the NF for the purpose of the programme, in compliance with Art. 5 of the MoU on the National Fund.

7.3. **Recovery of Funds in Case of Irregularity or Fraud**

Any proven irregularity²⁴ or fraud²⁵ discovered at any time during the implementation of the programme or as the result of an audit will lead to the recovery of funds by the Commission.

²¹ Commission Regulation (EC) 1681/94 of 11. July 1994; 12.7.94; p. 43

²² Fraud shall mean any intentional act or omission relating to: the use or presentation of false, incorrect or incomplete statements or documents, which has as its effect the misappropriation or wrongful retention of funds from the general budget of the European Communities or budgets managed by, or on behalf of, the European Communities; non disclosure of information in violation of a specific obligation with the same effect; the misapplication of such funds for purposes other than those for which they are originally granted.

²³ Irregularity shall mean any infringement of a provision of national or Community law, this Financing Memorandum or ensuing contracts, resulting from an act or omission by an economic operator, which has, or would have, the effect of prejudicing the general budget of the Communities or budgets managed by them, by an unjustified item of expenditure. The term "Community law" in this context shall be defined as the entirety of Community rules applicable between the Parties of the Financing Memorandum (e.g. the Europe Agreements, Framework Agreements, the MoU on the Establishment of the National Fund etc.)

²⁴ see definition above

²⁵ see definition above

If, after completing the necessary verifications, the Commission concludes that:

- (a) the Beneficiary Country has not complied with the obligations to prevent, detect, and correct irregularities or
- (b) the implementation of a project appears not to justify either part or the whole of the assistance allocated or
- (c) there are serious failings in the management or control systems which could lead to irregularities,

the Commission may suspend further financing of the programme in question, and, stating its reasons, request that the Beneficiary Country submit comments and, where appropriate, carry out any corrections within a specified period of time.

If no agreement is reached by the end of the period set by the Commission and if the required corrections have not been made, the Commission may – taking into account any comments made by the Beneficiary Country – decide within three months to:

- (a) reduce or cancel any payment for the programme in question, or
- (b) make the financial corrections required by cancelling all or part of the assistance granted to the programme concerned.

The Commission shall, when deciding on the amount of a correction, take into account the principle of proportionality, the type of irregularity and the extent and financial implications of the shortcomings found in the management and control system of the Beneficiary Country.

In the absence of a decision to do either (a) or (b), further financing of the programme shall immediately resume.

The National Authorising Officer will ensure the reimbursement of any unused funds or any sum wrongly paid within sixty calendar days of the date of the notification. If the NAO does not repay the amount due to the Community, the Beneficiary Country shall refund this amount to the Commission.

Interest on account of late payment shall be charged on sums not repaid by applying the rules specified in the Financial Regulation.

8. VISIBILITY AND PUBLICITY

The PAO in charge will be responsible for ensuring that the necessary measures are taken to ensure appropriate publicity for all activities financed from the programme. This will be done in close liaison with the Commission. Further details are set down in the Annex on Visibility and Publicity.

9. SPECIAL CONDITIONS

In the event that agreed commitments are not met for reasons which are within the control of the Government of the Republic of Bulgaria, the Commission may review the programme with a view, at the Commission's discretion, to cancelling all or part of it and/or to reallocate unused funds for other purposes consistent with the objectives of the Phare programme.