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**COMMISSION REPORT TO THE EUROPEAN PARLIAMENT AND TO THE  
COUNCIL**

**Protection of the Communities' financial interests — Fight against fraud — Annual  
Report 2008**

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## EXECUTIVE SUMMARY

The EU budget is not an anonymous source of funding. It is the shared effort and commitment of EU Member States and citizens to make their vision become reality, from supporting economic and social solidarity to promoting research, technological development and training, and to supporting sustainable development worldwide. Accordingly, the Treaty calls on the Commission and Member States to coordinate their action to protect the EU budget and to counter fraud and other illegal activities affecting it. Indeed, Member States should be as rigorous in protecting the EU budget as they are in controlling expenditure from national budgets.

Member States are well-placed to fulfil that role. National authorities are in fact in charge of the daily management and control of the largest part of the annual EU budget, approximately 80%. The Commission has an overall oversight, standard setting and compliance verification role. Major reform efforts in recent years have enhanced clarity about the respective roles of the authorities involved, and through greater vigilance at all levels, the sound financial management of EU funds is gradually improving across the board.

This annual Report on the Protection of the Communities' financial interests as called for by the Treaty is presented by the Commission in close co-operation with the Member States. It provides detailed statistics on irregularities reported and suspected cases of fraud as well as information on the quality and speed of exchange on irregularities affecting the EU budget.

The statistics presented must be read and used with great care: a reported irregularity is in most cases not a fraud (which is a deliberate act). A reported suspicion of fraud is not necessarily a fraud confirmed by a court judgment. All irregularities covered in this report are effectively being dealt with by Member States and/or Commission. Finally, the greater the control effort is, the likely it is that irregularities will be detected and reported. As such, an increase in the number of irregularities can be a first indication that rigorous controls are being implemented.

### **Statistics on fraud and other irregularities**

Overall figures for 2008 show that the **number of irregularities** increased for structural funds and cohesion fund, for pre-accession funds and direct expenditure sector and decreased for agriculture and own resources. The overall number of irregularities for expenditure has increased from 6 047 in 2007 to 6 595 in 2008.

At the same time, the **estimated financial impact of irregularities** decreased from €1 024 million in 2007 to €783.2 million in 2008. It decreased in all sectors, except for direct expenditure sector and pre-accession funds. For this last area, both the number of new cases and the amounts affected are the highest so far reported. The increase may be the result of enhanced controls at the end of the project cycle, of the growing number of reporting countries, and of a wide variety of pre-accession assistance programmes being indicated i.e. the first cases on Transition Facility, CARDS, and more cases for the Turkish Instrument for pre-accession. For the traditional own resources area, the number of irregularities was down from 6 097 in

2007 to 5 344 in 2008, and so was the financial impact from €401 million in 2007 to €351 million in 2008.

The total estimated financial impact of **cases of suspected fraud** has decreased for both expenditure and traditional own resources areas. It should be made clear that what is involved here is reported suspicions of fraud and not cases confirmed by the courts. The real financial impact, after recovery and financial correction, can be known only at the end of the legal and administrative proceedings.

### **Major developments in the area of the protection of financial interests-fight against fraud**

The debate around the reform of the European Anti-fraud Office (OLAF) was re-launched; the proposal for amending Regulation (EC) No 1073/1999<sup>1</sup> concerning investigations by OLAF was taken up actively in the European Parliament. This reform should further reinforce the Office's independence, while providing strong procedural guarantees and ensuring proper oversight of its operations.

The Community has continued to promote **international cooperation** with third countries and international organisations in order to combat fraud and other illegal activities. In December 2008, the Commission has presented a proposal for a Council regulation on the signing on behalf of the Community of an anti-fraud cooperation agreement with the Principality of Liechtenstein. The Community has become a full state party to the United Nations Convention against Corruption (UNCAC). OLAF is actively improving, in close cooperation with the Commission services concerned, the cooperation in fraud prevention and investigation with its operational partners, in particular with African and Middle East countries.

At **EU level**, the Commission and the Member States are implementing the decision to ensure transparency regarding the beneficiaries of EU funds. Though this measure is mainly intended to enhance democratic accountability and informed policy debates, it also helps dissuading fraud.

**Member States'** contributions to this report show that they have taken various institutional and legislative measures to protect the Communities' financial interests such as: establishing new bodies to combat fraud; adopting or amending their national legislations relating to the management of EU funds to ensure better transparency of administrative procedures and better financial control; adopting new legislation to combat VAT fraud.

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<sup>1</sup> OJ L 136, 31.05.1999.

## INTRODUCTION

This report consists of five parts:

The **first part** gives a **summary of the statistics on irregularities** reported by the Member States in those areas where Member States implement the budget (agricultural policy, Structural Actions and pre-accession funds, i.e. around 80% of the budget) and for the collection of the Community's own resources. It also gives an estimate of irregularities in the field of expenditure managed directly by the Commission and an overview of the operational activities of the European Anti-Fraud Office (OLAF).

The second part sets out the **main legislative measures taken by the Community and the Member States in 2008 to protect the Communities' financial interests**.

The report also lists the **administrative measures adopted by the Commission in the areas of transparency and fraud prevention**.

Part 4 deals with **cooperation with the Member States** and gives an overview of the **powers and organisation of the national authorities in the fight against fraud and designated for cooperation with OLAF**. It also analyses the **reporting discipline of irregularities**.

The **final part of the report**, for which the same kinds of reservation apply as for part 1, deals with recoveries made in 2008 in all budget areas.

The report is accompanied by two Commission working papers<sup>2</sup>.

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<sup>2</sup> For references, see cover page of the report.

## **1. RESULTS OF THE FIGHT AGAINST FRAUD: STATISTICS ON FRAUD AND OTHER IRREGULARITIES**

### **1.1. Statistics on fraud and other irregularities reported by the Member States and Commission departments in 2008**

In the fields where Member States implement the budget and for the collection of the Community's own resources, Community legislation requires the Member States to report suspicions of fraud and other detected irregularities affecting the Communities' financial interests.

Distinguishing between fraud and other irregularities is important. An irregularity is any infringement of a Community provision by an economic operator which has, or would have, the effect of prejudicing the Communities' financial interests.<sup>3</sup> Fraud is an irregularity committed intentionally which constitutes a criminal offence.<sup>4</sup> The Member States identify whichever irregularities constitute suspected fraud. The real financial impact of fraud can be measured only at the end of legal proceedings.

The Commission working paper *Statistical evaluation of irregularities*<sup>5</sup> presents an in-depth analysis of the information reported by the Member States and includes statistics on fraud and other irregularities detected by Commission departments in the areas of the budget under centralised direct management.

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<sup>3</sup> Article 1(2) of Council Regulation (EC, Euratom) No 2988/95 of 18 December 1995 on the protection of the European Communities' financial interests (OJ L 312, 23.12.1995).

<sup>4</sup> Article 1(1)(a) of the Convention of 26 July 1995 on the protection of the financial interests of the European Communities (OJ C 316, 27.11.1995).

<sup>5</sup> For reference, see cover page of the report.

Table 1: Number of irregularities and amounts — 2008

Area	Number of irregularities reported		Total estimated financial impact of irregularities, including suspected fraud (€ million)		Estimated financial impact of suspected fraud only (€million)	
	2007 <sup>6</sup>	2008	2007 <sup>7</sup>	2008	2007	2008
<b>Agriculture (EAGF and EAFRD)</b>	1 548	1 133	155	102.3	44.8 (~0.1 % of allocations)	4 (0.01 % of allocations)
<b>Structural Funds and Cohesion Fund</b>	3 756	4 007	804	585.2	141 (~0.31 % of allocations)	57 (~0.11 % of allocations)
<b>Pre-accession funds</b>	332	523	32	61	5 (~0.38 % of allocations)	13 (~0.9 % of allocations)
<b>Direct expenditure</b>	411	932	33	34.7	18.1 (~0.17 % of allocations)	3.2 (~0.03 % of allocations)
<b>Total expenditure</b>	6 047	6 595	1 024	783.2	208.9 (~0.22 % of the expenditure in the four areas)	77.2 (~ 0.07 % of the expenditure in the four areas)
<b>Own resources<sup>8</sup></b>	6 097	5 344	401	351	130.78 (~0.81 % of the total amount of own resources <sup>9</sup> )	75 (~0.46 % of the total amount of own resources)

<sup>6</sup> The figures have been updated for certain sectors since the 2007 report.

<sup>7</sup> Idem.

<sup>8</sup> Customs duties and agricultural levies.

<sup>9</sup> This percentage is based on an estimate of traditional own resources in the 2008 general budget, and not on accounts.

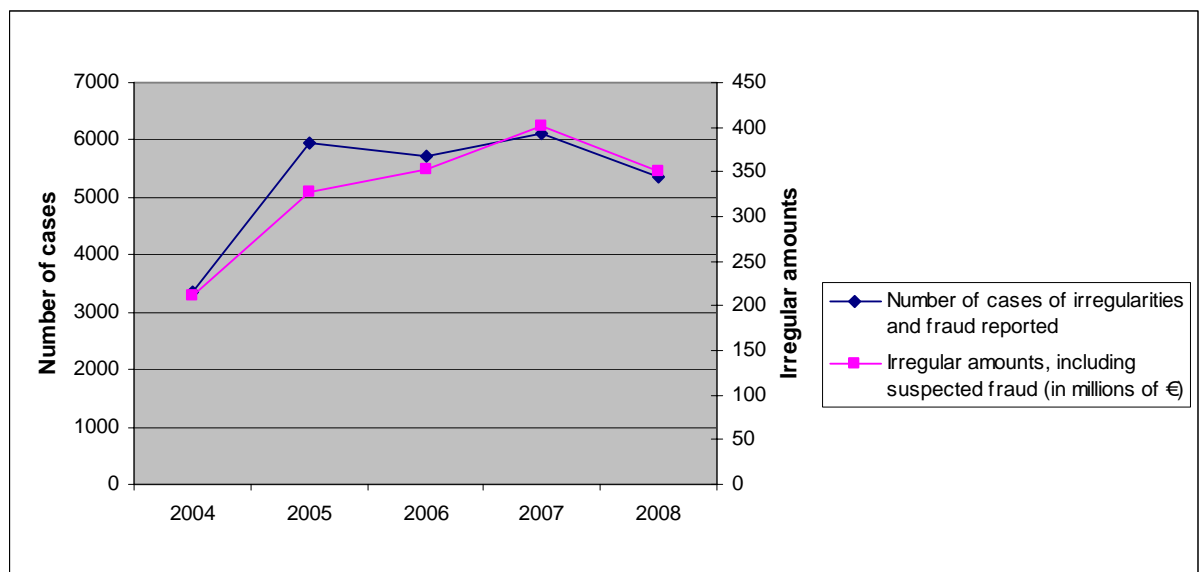


### 1.1.1. Traditional own resources

The number of cases of irregularities reported in 2008 was 12.5% down on 2007 (5344 cases in 2008, compared with 6097 in 2007), while the estimated amount is 12.5% lower (from €401 million in 2007 to €351 million in 2008). Suspected fraud accounted for approximately 20% of cases of irregularities reported, with an estimated financial impact of €75 million, equivalent to approximately 0.46% of total own resources in 2008 (compared with €130.78 million, or around 0.81%, in 2007). It should again be made clear that what is involved here is reported suspicions of fraud and not cases confirmed by the courts. The real financial impact can only be established at the end of the proceedings.

The goods most affected were, as in previous years, TVs and monitors. The most frequent irregularities were false declarations (misdescription, incorrect value, origin and preferential arrangements) and formal shortcomings (failure to fulfil obligations or commitments). The second product was tobacco. The Commission continues to pay particular attention to these sectors. Clothing increased in importance, as did machines, plastics and meat, whereas (parts of) cars and motors remained relatively stable. Vegetables (especially garlic) declined in importance.

Graph 1: Number of irregularities reported and estimated financial impact — traditional own resources — 2004-08



### 1.1.2. Agricultural expenditure (EAGF<sup>10</sup> and EAFRD<sup>11</sup>)

The number of irregularities reported was down 27% (1133 cases, compared with 1548 in 2007). The amount involved (€102.3 million, or approximately 0.21% of total expenditure excluding advance payments for the agricultural sector) was down 34%. Suspected fraud accounted for around 7% of cases of irregularities reported, with an estimated financial impact of €4 million, or 0.01% of total appropriations, in 2008 (compared with €4.8 million, or around 0.1% of total appropriations, in 2007). It should again be made clear that what is involved here is reported suspicions of

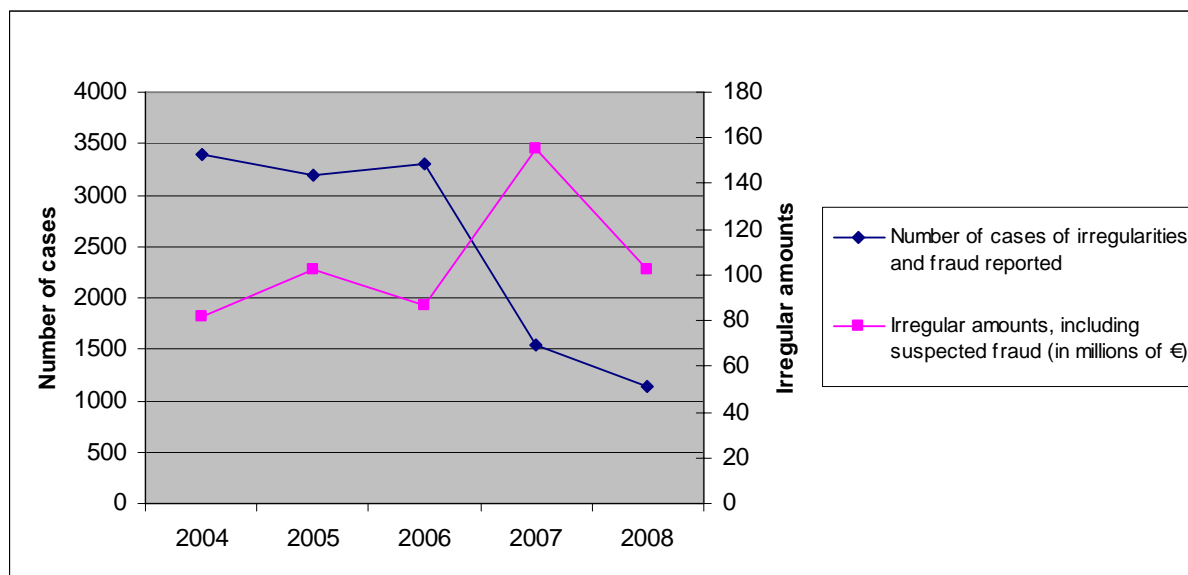
<sup>10</sup> European Agricultural Guarantee Fund.

<sup>11</sup> European Agricultural Fund for Rural Development.

fraud and not cases confirmed by the courts. The real financial impact can only be established at the end of the proceedings.

The highest amounts related to fruit and vegetables, rural development (2000-2006 programming period) and the wine sector. These sectors together account for more than 70% of the total amount affected by irregularities.

*Graph 2: Number of irregularities reported and estimated financial impact — agricultural expenditure — 2004-08*



### 1.1.3. Structural measures

The number of irregularities reported concerning the Structural Funds and the Cohesion Fund was up 6.7% (4007 cases, compared with 3756 in 2007). Their estimated financial impact (€85.2 million, or around 1.25% of commitment appropriations) was down 27%. Suspected fraud accounted for approximately 7.4% of cases of irregularities reported, with a financial impact estimated at €7 million, or around 0.11% of total commitment appropriations (compared with €41 million, or 0.31%, in 2007). It should again be made clear that what is involved here is reported suspicions of fraud and not cases confirmed by the courts. The real financial impact can only be established at the end of the proceedings.

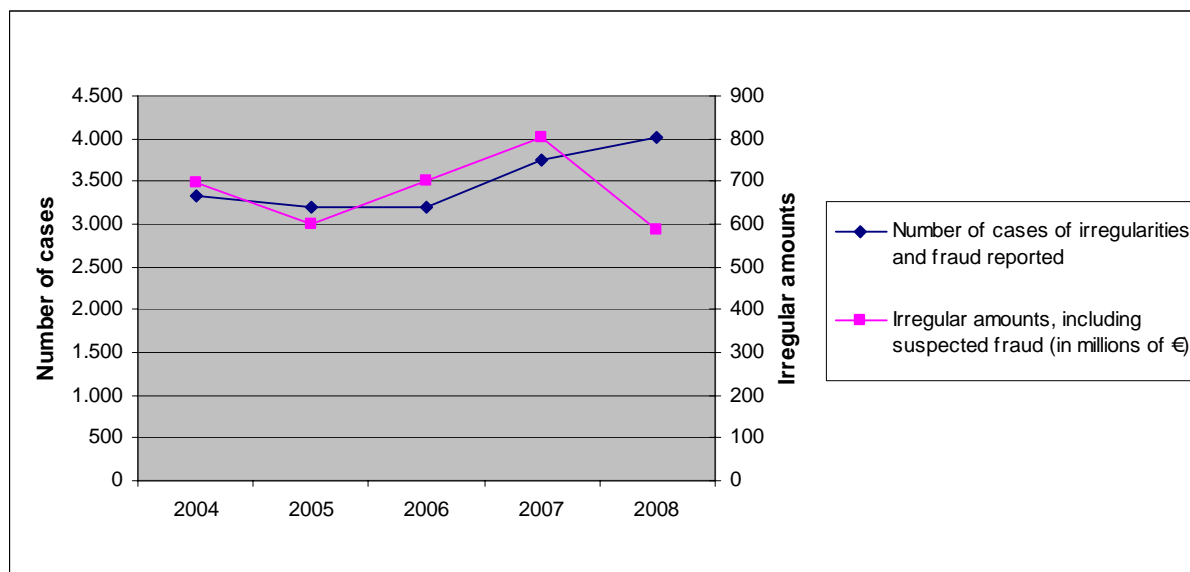
As in previous years, the ERDF<sup>12</sup> and the ESF<sup>13</sup> accounted for most irregularities (around 88%). The number of irregularities reported for the guidance section of the EAGGF and for the FIFG<sup>14</sup> was down by 17%; the number of irregularities affecting the ESF also decreased, by 4%. The number of irregularities reported for the ERDF was up by 18.7% and for the Cohesion Fund by 63%.

<sup>12</sup> European Regional Development Fund.

<sup>13</sup> European Social Fund.

<sup>14</sup> Financial Instrument for Fisheries Guidance.

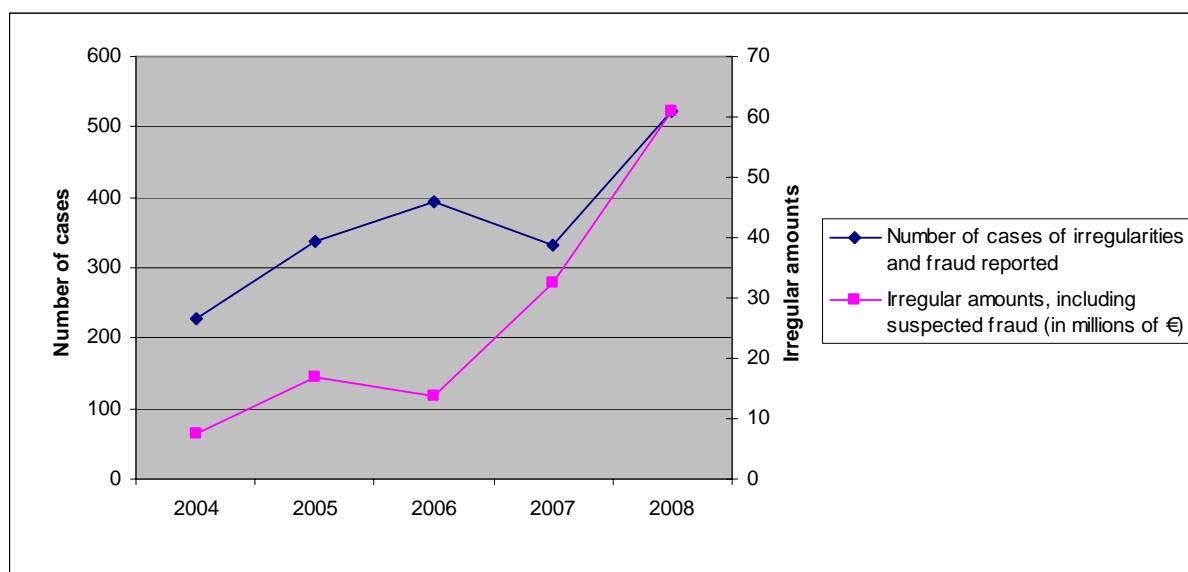
Graph 3: Number of irregularities reported and estimated financial impact — structural measures — 2004-08



#### 1.1.4. Pre-accession funds

The number of irregularities reported concerning PHARE, SAPARD and ISPA funds – and including as of 2008 CARDS, Transition Facility, and the Pre-accession assistance for Turkey – increased by 58 % (523 cases compared with 332 in 2007). The presumed financial impact increased from €32 million in 2007 to €61 million in 2008 (approximately 5.4% of the total committed amount). Suspected fraud accounted for approximately 21.7% of the irregular amounts reported in 2008, with a financial impact estimated at €13 million, or around 0.94% of the total annual budget. It should again be made clear that what is involved here is reported suspicions of fraud and not cases confirmed by the courts. The real financial impact can only be established at the end of the proceedings.

Graph 4: Number of irregularities reported and estimated financial impact — pre-accession funds — 2004-08



In July 2008, the Commission issued a Report on the management of EU funds in Bulgaria<sup>15</sup>. Following allegations of irregularities, suspicions of fraud and possible conflicts of interest in the award of contracts, the Commission (OLAF) initiated investigations into the management of EU funds by the Bulgarian authorities. The Commission decided on a temporary interruption of pre-accession funds and on freezing payments under various other financial instruments until the necessary remedial action to ensure sound financial management of EU funds had been properly implemented by the Bulgarian authorities. The Commission has provided concrete guidance on how to improve the implementation structures and procedures for agencies managing EU funds in Bulgaria, and OLAF has established close cooperation with the Bulgarian prosecution services. In July 2008, following audit missions under the SAPARD programme in Romania, which revealed significant deficiencies in management and control systems, the Commission decided to interrupt reimbursements of SAPARD expenditure. Only when the Commission concludes, on the strength of reports by the competent national authorities and confirmed by independent audit bodies, that the remedial action plan formulated by the Romanian authorities has been properly implemented will it consider reimbursing the expenditure concerned.

#### 1.1.5. Statistics on expenditure directly managed by the Commission

This year's analysis of irregularities in this area was based on data held in the Commission's accounting system ABAC, covering more detailed information on recoveries. However, as the relevant function was added only in 2008, it has been necessary to limit the scope of the analysis for 2008 to expenditure managed by the Commission on a centralised direct basis (see point 7.1. of the working paper *Statistical evaluation of irregularities*). The data presented should therefore be treated with particular caution and not as empirical evidence of the level of fraud and irregularity.

<sup>15</sup> COM(2008) 496 final.

The number of recovery orders relating to cases of irregularities and suspected fraud in this area came to 932, with a presumed financial impact of €4.7 million, €3.2 million of which was accounted for by 19 reported cases of suspected fraud. Irregularities in the sector of external action accounted for €6.8 million and in the area of internal policies for €27.9 million. The estimated financial impact of possible fraud cases amounts to 0.03 % of the total annual value of commitments directly managed by the Commission.

## 1.2. Statistics on OLAF's activities

Once a preliminary evaluation has been made of information received, it is up to OLAF to open one of four types of cases: an internal investigation, an external investigation, a coordination case or a criminal assistance case. The number of cases opened each year is stable (204 in 2008, as against 210 in 2007 and 195 in 2006). Since 2004, the number of investigations opened by OLAF on its own initiative (internal and external investigations) has equalled then exceeded the number opened by OLAF to provide assistance and coordination to national authorities (coordination cases and criminal assistance cases). Since 2005, OLAF's own-initiative investigations have accounted for around 75 % of all cases opened.

The number of active cases has increased (425 at the end of 2008, compared with 408 at the end of 2007), owing in large measure to efforts by OLAF to deal with the backlog of the oldest cases.

*Table 2: Cases ongoing as at 31 December 2008 by sector, and their financial impact*

Sector	Cases in active investigation 31 December 2008	Financial impact from investigation (€million)
Agriculture	68	125
Cigarettes	18	5
Customs	47	852
Direct expenditure	40	54
EU institutions and bodies	107	27
External Aid	102	129
Structural funds	43	171
<b>Total</b>	<b>425</b>	<b>1361.7</b>

For more details and a comparison with previous years, see the OLAF report.<sup>16</sup>

<sup>16</sup> [http://ec.europa.eu/comm/anti\\_fraud/reports/index\\_en.html](http://ec.europa.eu/comm/anti_fraud/reports/index_en.html).

## 2. MAIN LEGISLATIVE MEASURES TAKEN BY THE EUROPEAN UNION IN 2008 TO PROTECT ITS FINANCIAL INTERESTS

### 2.1. Cross-cutting legislative developments

In 2008, there were significant developments both in the institutional framework, as the debate on the reform of the European Anti-Fraud Office acquired fresh impetus, and in international cooperation by the Community with third countries and international organisations in the fight against fraud and corruption. Important legislative measures were also taken to ensure better protection of the euro.

#### 2.1.1. *Institutional developments — the reform of the European Anti-Fraud Office (OLAF)*

OLAF was set up in 1999 to protect the financial interests of the European Communities and the reputation of the European institutions.

In 2008, the Commission's 2006 proposal<sup>17</sup> for amending Regulation (EC) No 1073/1999 of the European Parliament and of the Council of 25 May 1999 concerning investigations by OLAF was taken up actively in the European Parliament. The legal initiative for better governance and improved effectiveness of OLAF's activities passed first reading by the European Parliament in November 2008, with a number of amendments. The parliamentary amendments<sup>18</sup> building on the Commission proposal and seeking an improved legal framework for the Office and for investigations and their follow-up (including cooperation with Member States' competent authorities), and better protection of the fundamental rights of persons concerned by investigations received the overall support of the Commission, with some reservations owing to institutional and legal limits of the current set-up of OLAF. Better protection of fundamental rights includes the possibility for a person concerned by an investigation to introduce a complaint to an independent Review Advisor regarding the alleged violation of that person's procedural rights.

The reform debate will continue in 2009. Further simplification and consolidation of the entire anti-fraud legislation is also under consideration.

#### 2.1.2. *The international dimension of the protection of the Communities' financial interests — cooperation with third countries and international organisations*

The Community promotes cooperation with third countries and international organisations through international agreements and administrative arrangements, in order to protect its financial interests and to combat fraud and all other illegal activity.

##### *Bilateral anti-fraud agreements*

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<sup>17</sup> COM (2006)244 final.

<sup>18</sup> EP Resolution No P6-TA-PROV(2008)0553.

In December 2008, the Commission presented a proposal<sup>19</sup> for a Council decision on the signing, on behalf of the Community, of a cooperation agreement between the European Community and its Member States and the Principality of Liechtenstein to combat fraud and any other illegal activity to the detriment of their financial interests. Negotiations have been led by the Commission on the strength of a mandate granted in 2006. The proposal also covers evasion of direct taxation, which is not a criminal offence in Liechtenstein. The parties to the agreement would be obliged to provide each other with assistance in cases of fraudulent conduct contrary to the legislation on direct taxes, which includes submitting incomplete tax returns. In the light of the European Council conclusions of 10 February 2009 and the G20 Summit Statement of April 2009<sup>20</sup> negotiations for the agreement have been pursued in accordance with the latest developments on the protection of public finances, banking secrecy and tax cooperation.

The negotiations for an agreement with Liechtenstein were preceded by the anti-fraud cooperation agreement between the European Community and the Swiss Confederation<sup>21</sup>. It contains provisions relating to administrative assistance and to mutual legal assistance in criminal matters for the protection of financial interests; it covers indirect tax (VAT and excise duties) and customs offences, corruption and money laundering. Pending ratification by all Member States, the agreement can be applied provisionally by means of a declaration by the contracting parties (a contracting party can apply the agreement at any time with any other contracting party having made the same declaration). In December 2008, a number of Member States<sup>22</sup> and Switzerland made such a declaration and the agreement will be applicable between them as from 8 April 2009.

#### *Multilateral anticorruption agreements*

The European Community ratified the United Nations Convention against Corruption (UNCAC)<sup>23</sup>. Within its area of competence, the European Community is therefore a full state party to the Convention and is the only regional economic integration organisation which has this status.

The UNCAC addresses primarily prevention measures in the public and private sectors, such as the establishment of anticorruption bodies, and transparency and accountability in matters of public finance. International cooperation is another important aspect. Parties are also required to take measures which will support the tracing, freezing, seizure and confiscation of the proceeds of corruption. Effective asset recovery is a fundamental principle of the Convention and sends a message to corrupt officials that there will be no place to hide their illicit assets.

#### *Non-legislative acts: Administrative arrangements*

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<sup>19</sup> COM (2008)839 final.

<sup>20</sup> See point 15, paragraph 7 of the G20 Summit Statement.

<sup>21</sup> OJ L 46, 17.2.2009.

<sup>22</sup> BG, FI, FR, DE, PL, RO, SE, and UK. For Germany the agreement is applicable from 9 April 2009, for Finland from 15 April and for the UK from 20 April 2009.

<sup>23</sup> Council Decision No 2008/801/EC on the conclusion, on behalf of the European Community, of the United Nations Convention against corruption, OJ L 287 of 29.10.2008.

In the field of external aid OLAF continued, in close cooperation with the Commission services concerned, to foster the exchange of operational expertise between anti-fraud investigators and services managing and supervising aid funds in Africa. Fund managers and investigators are establishing close contacts and, where possible, administrative cooperation arrangements<sup>24</sup> are concluded with services of countries recipients of EU funds with a view to improving management and control of public funds and optimising the effectiveness of external aid.

### 2.1.3. *Ratification process for Protection of the Financial Interests (PFI) instruments*

The second Protocol to the Convention on the Protection of the European Communities' Financial Interests<sup>25</sup> entered into force on 19 May 2009, following its ratification by Italy on 18 February 2009. The Convention and its protocols<sup>26</sup> were ratified in 2008 by Poland. In February 2008, the Commission published a second report<sup>27</sup> on the implementation by the Member States<sup>28</sup> of the above-mentioned legal instruments. Slovenia amended its Criminal Code by including an article on incriminating fraud against the European Communities, which had previously not been specifically defined as a criminal offence in Slovenian law.

### 2.1.4. *Protection of the euro against counterfeiting*

Four Commission proposals<sup>29</sup> were adopted in December 2008 by the Council of the European Union to strengthen the protection of the euro against counterfeiting. The new legislation introduces the obligation for financial institutions to ensure that notes and coins are checked for authenticity before putting them back into circulation. At the same time, to minimise the risk of confusion between medals/tokens and genuine euro coins, there has been further clarification of which designs may not be reproduced on medals and tokens.

At operational level, the Commission continued, in cooperation with the Member States, the European Central Bank and Europol, to manage the Pericles programme for training and technical assistance to combat counterfeiting. Eleven actions were launched under the 2008 budget, and over 90 % of the €1 million budget for 2008

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<sup>24</sup> Such arrangements have been already been concluded with Argentina, Djibouti, Morocco, the Republic of Congo, Senegal and FIGE (Forum des Inspections Générales d'Etats d'Afrique) and, in 2008, with authorities in South Africa.

<sup>25</sup> OJ C316 of 27.11.1995.

<sup>26</sup> First protocol of 27 September 1996 (OJ C 313, 23.10.1996). Protocol of 29 November 1996 on the interpretation, by way of preliminary rulings, by the CJEC of the Convention (OJ C 151, 20.5.1997). Second Protocol of 19 June 1997 (OJ C 221, 19.7.1997).

<sup>27</sup> COM(2008) 77 final.

<sup>28</sup> The PFI instruments have not been ratified by the Czech Republic, Hungary and Malta, along with Estonia for the ECJ Protocol.

<sup>29</sup> Regulation (EC) No 44/2009 of 18 December 2008 amending Regulation (EC) No 1338/2001 laying down measures necessary for the protection of the euro against counterfeiting (OJ L 17, 22.1.2009, p.1); Regulation (EC) No 45/2009 of 18 December 2008 amending Regulation (EC) No 1339/2001 extending the effects of Regulation (EC) No 1338/2001 laying down measures necessary for the protection of the euro against counterfeiting to those Member States which have not adopted the euro as their single currency (OJ L 17, 22.1.2009, p.4); Regulation (EC) No 46/2009 of 18 December 2008 amending Regulation (EC) No 2182/2004 concerning medals and tokens similar to euro coins (OJ L 17, 22.1.2009, p.5); Regulation (EC) No 47/2009 of 18 December 2008 amending Regulation (EC) No 2183/2004 extending to the non-participating Member States the application of Regulation (EC) No 2182/2004 concerning medals and tokens similar to euro coins (OJ L 17, 22.1.2009, p.7).



was committed. Most of the projects subsidised were related to training and staff exchange activities, involving participants from most Member States and a number of third countries. The objective was to raise awareness of banknote and coin counterfeiting, to provide technical training for participants and to share best practices.

The total number of counterfeit euro coins removed from circulation in 2008 was 195 900, down from 211 100 the year before (-7%). This success is the result of joint efforts by the European Commission and the Member States' authorities to remove counterfeit coins from circulation and underlines the need for all Member States to apply appropriate methods to this end.

## **2.2. Progress in the customs area**

### *2.2.1. Mutual assistance under the first pillar*

Significant progress has been made in the mutual assistance sector with the adoption of Regulation (EC) 766/2008<sup>30</sup> on 9 July 2008. This legislation amends Council Regulation (EC) 515/97<sup>31</sup> on mutual assistance in customs and agricultural matters. The new provisions extend the current exchange of information on suspected frauds to the systematic communication of pre-defined commercial information and establish a Customs Files Identification Database (FIDE), covering investigation files and helping Member States to coordinate their controls better, detect suspicious movements of goods and means of transport, and collect information in a 'European Data Directory'. The database was fully operational on 15 September 2008.

The Modernised Customs Code (MCC)<sup>32</sup> entered into force in June 2008, introducing a thorough reform of Community customs rules and procedures, and making them simpler and electronic. The MCC will become operational once its implementing provisions are ready and applicable, and no later than June 2013.

### *2.2.2. Efforts to combat the smuggling and counterfeiting of cigarettes*

The illicit trade in contraband and counterfeit cigarettes causes significant losses to the EU and national budgets every year.

To prevent and to reduce the consequences, in 2008 the Commission, which has previously concluded two agreements with tobacco manufacturers Philip Morris International and Japan Tobacco International<sup>33</sup>, took an active part in two Intergovernmental Negotiating Body (INB) sessions to negotiate a draft Protocol to the WHO Framework Convention on Tobacco Control, dealing with efforts to combat the illicit trade in tobacco products. Negotiations are ongoing with a view to agreeing on a standard creating universal obligations on tracking and tracing, and

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<sup>30</sup> OJ L 218, 13.8.2008.

<sup>31</sup> OJ L 82, 22.3.1997.

<sup>32</sup> Regulation (EC) No 450/2008 of the European Parliament and of the Council of 23 April 2008 laying down the Community Customs Code (Modernised Customs Code), OJ L 145, 4.6.2008.

<sup>33</sup> The two agreements provide for the payment by the tobacco producers of USD 1250 million (PMI) and USD 400 million (JTI) which may be used for combating the smuggling and counterfeiting of cigarettes. By the end of 2008, PMI had paid USD 650 million (approx. €503.8 million) and JTI USD 100 million (approx. €77.5 million).

designing a specific framework for cooperation between customs and judicial authorities.

### **3. MAIN ADMINISTRATIVE MEASURES TAKEN BY THE COMMISSION IN THE AREA OF TRANSPARENCY AND FRAUD PREVENTION**

#### **3.1. Transparency measures**

As part of the European Transparency Initiative<sup>34</sup>, the Commission obtained the support of the Council and of the European Parliament in favour of full disclosure of the beneficiaries of EU fund.

The greater share of EU funds (almost 80%) are handled by the national administrations, and as such, the responsibility to publish the names of beneficiaries rests with them. This obligation covers the Common Agricultural Policy, the Structural Actions, including the Cohesion Fund, and the European Refugee Fund.

The European Commission also manages grants and procurement contracts, amounting to some 20% of the EU budget in areas such as research policy, education and training, transport and energy networks. Under Article 30.3 of the revised Financial Regulation of 2006<sup>35</sup>, it is obliged to publish the names of the beneficiaries. To comply with this legal requirement the Commission, in 2008, set up the new central Financial Transparency System to facilitate access to consolidated information which had hitherto been published on the web pages of each Commission department. Its current version covers approximately €10 billion of aid, and the system will be extended to cover the Commission's own administrative expenditure. A specific search engine gives access to data on the beneficiaries of external aid.

Commission Regulation No 1302/2008<sup>36</sup> on the central exclusion database was adopted on 17 December 2008. It establishes a central database ('the exclusion database') as referred to in Article 95 of the Financial Regulation, which contains the details of candidates and tenderers who are in an exclusion situation described by Articles 93 and 94 of the Financial Regulation (for example, bankrupt or guilty of grave professional misconduct). The information is accessible to all entities managing EU funds.

The revised Commission Decision No 2008/969/EC, Euratom<sup>37</sup> on the Early Warning System (EWS) for the internal use of the Commission and the executive agencies was adopted on 16 December 2008. It establishes the EWS for the general budget of the European Union and any other fund managed by the Communities. The EWS is an internal information tool to help the Commission identify legal entities presenting financial or other risks, thus enabling the Commission to take any precautionary measures needed.

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<sup>34</sup> COM(2007)127; [http://ec.europa.eu/commission\\_barroso/kallas/work/eu\\_transparency/index\\_en.htm](http://ec.europa.eu/commission_barroso/kallas/work/eu_transparency/index_en.htm).

<sup>35</sup> Council Regulation (EC, Euratom) No 1995/2006 of 13 December 2006 amending Regulation No 1605/2002 on the Financial Regulation applicable to the general budget of the European Communities (OJ L 390/2006 of 31.12.2006).

<sup>36</sup> OJ L 344, 20.12.2008.

<sup>37</sup> OJ L 344, 20.12.2008.

### **3.2. Further efforts to strengthen the management and control systems and progress towards a positive Statement of Assurance (DAS)**

The Commission Action Plan towards an Integrated Internal Control Framework<sup>38</sup> was adopted in January 2006 in line with the Barroso Commission's strategic objective to obtain a positive Statement of Assurance (DAS) from the European Court of Auditors. It reflected the recommendations made by the Court of Auditors in its Opinion 2/2004<sup>39</sup> and provided for sixteen concrete actions. The Action Plan has been fully implemented, and its impact on the ground is beginning to materialise.

As part of the Action Plan, in December 2008, the Commission presented a Communication on the tolerable risk of error<sup>40</sup>. While a zero-tolerance policy on fraud would remain, adopting a tolerable risk approach means defining the levels to which it is reasonable to expect the Commission and its implementing partners, including the Member States, to reduce errors while using control resources effectively. This is a decision that needs to be taken by the legislative authority, and the Communication seeks to re-launch the discussion with the European Parliament and the Council on the issue. The Communication defines the tolerable risk concept and provides illustrative examples in two key-spending areas - the ERDF and the EAFRD – and makes a first estimation of the tolerable risk for these expenditure areas. At present, the Court of Auditors uses a 2% materiality level applied to all policy areas for assessing the legality and regularity of underlying transactions. The Commission's analysis suggests that the 2% materiality level currently used by the Court of Auditors for the annual DAS may not be an appropriate measure of a cost-effective control strategy for some policies. This means that the tolerable risk of error would need to be analysed and decided separately for each policy area.

The Court of Auditors' reports for 2006 and 2007 have shown that the error rate for structural actions remains high. Following mainly the Court of Auditors' recommendations in its 2006 Annual report and in its Opinion No 6/2007<sup>41</sup>, which highlighted the weaknesses in the shared management of the Structural Funds in the Member States, the Commission launched an Action Plan<sup>42</sup> on 19 February 2008 to strengthen the Commission's supervisory role in the shared management of structural actions and thus address the high level of errors in reimbursements for structural actions and weaknesses in the Member States' management and control systems.

The Commission's focus is on boosting the effectiveness of controls undertaken by the Member States and of Commission audits, to ensure that by the time the 2000-2006 programmes and projects are closed, the residual risk of error is as low as possible. For 2007-2013, the preventive actions will ensure that the Member States' systems function effectively from the beginning of programme implementation, or failing this, that any deficiencies are detected as early as possible. In February 2009, the Commission presented to the European Parliament, the Council and the European Court of Auditors a report<sup>43</sup> on the action plan for 2008.

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<sup>38</sup> COM(2006)9 final.  
<sup>39</sup> OJ C 107, 30.4.2004, p.4.  
<sup>40</sup> COM(2008)866 final.  
<sup>41</sup> OJ C 216, 14.9.2007.  
<sup>42</sup> COM(2008)97.  
<sup>43</sup> COM(2009)42.

Concerning Commission direct expenditure, the Internal Audit Service of the Commission (IAS) conducted audits in the area of procurement, including IT services and grant schemes. IAS reports noted certain improvements in the Commission's internal control systems. Details are available in the annual report to the discharge authority on the internal audits carried out in 2008.

### **3.3. Joint fraud prevention strategy under the structural measures**

The Commission established a joint fraud prevention strategy (JFPS) for the ERDF, the ESF and the Cohesion Fund, following an audit recommendation by IAS. The document sets out fraud prevention actions to achieve the objectives, both in the field of risk assessment and of fraud awareness. The Commission has already implemented some of these actions, including a seminar in Brussels for managing and paying authorities and a meeting of the Homologues Group (national and community auditors) in Cardiff in October 2008.

### **3.4. The Hercule II programme**

The purpose of the Hercule II programme is to promote activities to protect the Communities' financial interests. For the 2007-2013 exercise, its budget has been increased by €6 million a year in order to finance the purchase of equipment and training activities to combat the smuggling of cigarettes. This increase is also the result of the extra monies<sup>44</sup> made available under the anti-contraband agreements with tobacco producers PMI and JTI (see 2.2.2).

In 2008, 10 research actions in the legal field, 9 training projects and 25 technical assistance projects were supported, and the allocated budget of €13.8 million was entirely committed.

## **4. COOPERATION WITH THE MEMBER STATES IN THE FIGHT AGAINST FRAUD AND IRREGULARITIES**

This chapter – based on the replies of Member States to a questionnaire<sup>45</sup> - gives an overview of the legislative and institutional developments in the Member States in 2008 and of the national anti-fraud structures designated for cooperation with OLAF in relation to on-the-spot checks. It also deals with certain aspects of the reporting of irregularities by the Member States.

### **4.1. Institutional and legislative initiatives taken by certain Member States in 2008 to protect EU financial interests**

Belgium set up a body, organised on collegiate lines, to combat fraud, including tax fraud. The United Kingdom established the National Fraud Strategic Authority (NFSA), a non-statutory body whose key priorities include stronger deterrence of fraudsters through a tough, multi-agency law enforcement and regulatory response, and building greater public confidence in the response to fraud.

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<sup>44</sup> 9.7% of the funds paid by PMI and JTI have been allocated to the European Community.

<sup>45</sup> See all answers in the Commission working paper "Implementation of the Article 280 of the Treaty by the Member States in 2008".

Several Member States<sup>46</sup> have adopted or amended their national legislation relating to management of EU funds and public procurement procedures, to provide more transparency in administrative procedures and better financial control. For 2008 Sweden will, for the first time, supply national certification on the management of EU funds, ensuring that the internal control framework is in place and securing satisfactory internal control of EU funds managed in partnership with the Commission.

Malta adopted a National Anti Fraud and Corruption Strategy, aiming to create a normative, institutional and operational framework. The Czech Republic adopted a National Strategy for the protection of the EU's financial interests and an accompanying action plan.

Some Member States<sup>47</sup> adopted legislation and rules to combat VAT fraud and improve the coordination of operations by the relevant national authorities in this field.

Greece adopted a law on the prevention and suppression of money laundering and terrorist financing and other provisions. Similarly, Cyprus replaced all its previous laws from 1996-2004 by the newly adopted Fight against Money Laundering Act.

In the field of irregularities and recovery, a few Member States<sup>48</sup> adopted new measures for identifying and notifying irregularities, and enhanced procedures and mechanisms for recovering overpayments.

Latvia amended its Criminal Law on establishing liability for the dissemination of intentionally false data or information on the state of the Latvian financial system.

Member States have reported several other legislative or administrative developments<sup>49</sup> taken in the course of 2008. These were adopted on the Member States' own initiative and not simply to transpose Community legislation.

#### **4.2. National authorities designated to cooperate with OLAF in the fight against fraud**

Article 4 of EC Regulation **2185/96**<sup>50</sup> requires OLAF to prepare and conduct on-the-spot checks in close cooperation with the competent authorities of the Member State concerned. Therefore, prior identification of the competent national authority is essential.

For the Common Agricultural Policy and the Structural Funds, where shared management arrangements (between the Commission and the Member States) are in place, having clearly designated competent authorities has made it easier to run on-the-spot checks. For direct expenditure, however, the lack of clarity in the

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<sup>46</sup> BG, LV, LT, LU, HU, PT, SK, SE.

<sup>47</sup> ES, HU, RO, IT.

<sup>48</sup> BG, EE, IT, PL, SK, UK.

<sup>49</sup> See the Commission working paper "Implementation of the Article 280 of the Treaty by the Member States in 2008".

<sup>50</sup> OJ L 292/15.11.1996.

designation of competent authorities and lines of demarcation in Member States gives rise to difficulties in applying Regulation No 2185/96.

In its Resolution of 19 February 2008 on the protection of the Communities' financial interests<sup>51</sup>, the European Parliament also called for more information on the national competent authorities. The resultant information will also serve to improve the implementation of Regulation 2185/96 and to identify legislative gaps with a view to possible consolidation of the antifraud legislation<sup>52</sup>.

#### 4.2.1. *Central coordinating authority*

Most Member States<sup>53</sup> reported having a central coordinating authority responsible for operational support to OLAF and that OLAF can contact when conducting on-the-spot checks. In some Member States<sup>54</sup>, the central coordinating authority is the AFCOS (Anti-Fraud Coordination Service), while in others<sup>55</sup> another national authority has been designated. Some Member States<sup>56</sup> indicated that one or more coordinating authorities may be contacted depending on the type of financial resources (e.g. funds, customs or tax).

In addition, Member States<sup>57</sup> pointed out that the powers and duties of these coordinating authorities mostly involve communicating irregularities to the Commission and putting OLAF into contact with the competent national investigative authority. In some of the Member States<sup>58</sup>, the designated authority also has various investigative powers (e.g. interviewing economic operators, accessing documents and premises, searching and seizing, accessing information about ongoing criminal or administrative investigations, tracing people, telephones and mail) that can be used to support OLAF investigations and on-the-spot checks.

Finally, the Netherlands, Portugal and Slovenia indicated that the designated authority operates on the basis of annual programming. Italy, the Netherlands, Portugal and the United Kingdom stated that the authority is obliged to draw up a report on the objectives of its monitoring activity.

#### 4.2.2. *National authorities with responsibilities extended to the field of direct expenditure*

It is also important to clarify whether Member States have a single authority in the area of direct expenditure that OLAF can contact for on-the-spot checks.

Several Member States<sup>59</sup> (without an AFCOS) reported that they have a single authority that can be contacted. In most cases, it is law enforcement rather than an administrative authority, with an established legal basis.

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<sup>51</sup> P6\_TA-PROV(2008)0052.

<sup>52</sup> See point 2.1.1.

<sup>53</sup> BE, BG, CZ, DK, DE, EE, IT, CY, LV, LT, HU, MT, NL, PL, PT, RO, SI, SK, SE, UK.

<sup>54</sup> BG, CZ, DK, EE, CY, LV, HU, MT, PL, RO, SI, SK, SE.

<sup>55</sup> BE, DE, IT, LT, NL, PT, UK.

<sup>56</sup> BE, IE, IT, NL, AT, UK.

<sup>57</sup> DK, HU, IT, LT, NL, PT, SI, UK.

<sup>58</sup> DK, LT, MT, PT, RO, SI, UK.

<sup>59</sup> BE, DK, EE, IT, LT, LU, PT, SI, SK.

Besides communicating irregularities to the Commission and putting OLAF into contact with other competent investigative authorities, the designated authority in some Member States<sup>60</sup> has various investigative powers of the sort mentioned above which can be used to support OLAF investigations and on-the-spot checks in the field of direct expenditure.

### 4.3. Reporting of irregularities

Under Community legislation<sup>61</sup> Member States are required to notify the Commission of suspected fraud and any other irregularities which are the subject of a primary administrative or judicial finding. Regarding expenditure, this notification concerns agriculture, the structural actions and the pre-accession funds, and, as regards revenue, the Own Resources sector. Member States must inform the Commission of all irregularities involving an amount of over €10 000<sup>62</sup>.

The Commission's analysis and statistical assessment of irregularities depends on the accuracy, completeness, quality, and timeliness of Member States' notifications. In these areas, the national authorities still vary, though improvements have been made thanks to harmonisation of their reporting approaches.

This chapter analyses Member State practices in irregularity reporting, looking at three aspects: the timely reporting of irregularities, the estimation of their financial impact, and the classification of irregularities. Member States were asked to provide information for agriculture, the structural funds and the pre-accession funds. These areas are therefore indicated where relevant in the text below.

#### 4.3.1. *Timely reporting of irregularities in the agricultural and the structural actions sectors*

According to the 2007 Report on the protection of financial interests — Fight against fraud, timely reporting has been improving in recent years, although the time gap between the moment when the irregularity is discovered and the moment when it is reported remains significant.

Community legislation requires Member States to report all irregularities not later than two months after the end of the quarter in which an irregularity has been subject of a primary administrative or judicial finding and/or new information about a reported irregularity becomes known. The gap between the discovery and reporting of an irregularity should not be more than five months.

In 2007, in the agriculture sector, only 33 % of irregularities were reported within the deadline, while in 2008 the figure was 84 %. The average time between discovery and reporting of an irregularity was 1.2 years in 2007. In 2008, due to the introduction of a new electronic module, the time gap was not monitored.

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<sup>60</sup> DK, LT, PT, RO, SI.

<sup>61</sup> Commission Regulation (EC) 1848/2006 of 14.12.2006 (OJ L355, 15.12.2006); Commission Regulation (EC) No 2035/2005 of 12.12.2005 (OJ L328 of 15.12.2005), amending Regulation No 1681/94 of 11.07.1994 (OJ L178 of 12.7.1994); Commission Regulation (EC) No 2168/2005 of 23.12.2005 (OJ L345 of 28.12.2005) amending Regulation No 1831/94 of 26.07.1994 (OJ L 191, 27.7.1994); Commission Regulation (EC) 1828/2006 of 8.12.2006.

<sup>62</sup> For SAPARD €4000, for ISPA there is no threshold.

In 2007, for structural actions, 75 % of irregularities were reported on time, while in 2008 the figure was 86 %. In 2007, the gap between detection and reporting was 0.9 years, and in 2008 1.1 years.

For both agriculture and the Structural Actions sectors, Member States gave a large number of reasons for late reporting.

The complexity of national administrative procedures was mentioned by several Member States<sup>63</sup>, along with late reporting of irregularities by intermediate bodies. Sometimes reporting is hindered by the structure of the reporting/managing authority itself<sup>64</sup>, involving a considerable number of administrative layers. In other cases, irregularities are not reported until the administrative authority has ascertained that the circumstances in question represent an irregularity and recovery procedures are already under way or an administrative decision has been taken<sup>65</sup>. The Czech Republic, Hungary and the United Kingdom (Scotland) indicated that appeal and review proceedings may sometimes cause delays in the reporting procedure, while two other Member States<sup>66</sup> noted that the differing interpretations given by national authorities to the terms 'irregularity' and 'preliminary notification' may also result in late reporting.

Inadequate IT support<sup>67</sup> or insufficient training or staffing<sup>68</sup> were other reasons given. Delays may also result from not using the AFIS system<sup>69</sup>.

To improve their reporting timeliness, most Member States have taken measures to tighten national administrative procedures<sup>70</sup>, including the adoption of internal rules or guidelines. Other measures aim to improve the work flow with intermediate bodies<sup>71</sup> (reminders, ad-hoc meetings, exchange of information between different bodies, and direct contact with entities that notify irregularities late). Many Member States organise regular training for staff<sup>72</sup>.

In 2008, the United Kingdom (Scotland) completed an eight-month independent review of the appeals process. Hungary produced guidelines for reporting that are in line with the AFIS system. Italy drew up initial administrative or judicial documents laying down the reporting obligation. Poland produced a list of documents that may be considered primary administrative findings.

#### 4.3.2. *Estimating the financial impact of irregularities*

Sectoral regulations governing irregularity reporting to the Commission require Member States to evaluate and report the financial impact of irregularities too.

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<sup>63</sup> BE (Brussels capital region for the Structural Funds and Walloon region for agriculture), CZ, DK (agriculture), DE (agriculture), EE, EL (agriculture), ES, HU, NL, AT, PL (Structural Funds), SK, SE, UK (Northern Ireland).

<sup>64</sup> IE, IT, ES (Structural Funds).

<sup>65</sup> MT, FI.

<sup>66</sup> EE, PL.

<sup>67</sup> PL.

<sup>68</sup> HU.

<sup>69</sup> FR.

<sup>70</sup> DK, EL, ES, HU, MT, PT, SE.

<sup>71</sup> BE, BG, CZ, FR, MT, NL, AT, SK, UK.

<sup>72</sup> EE, IE, IT, LT, HU, PL, SE.



This is in many cases difficult to evaluate because so many factors need to be taken into account. These can include incomplete information when the evaluation is undertaken, or the absence of a pre-defined set of criteria to help the evaluator establish the financial impact of an irregularity.

For both the agricultural and Structural Actions sectors, a large number of Member States<sup>73</sup> have adopted guidelines for evaluating the individual financial impact of an irregularity. Of the Member States receiving support from the pre-accession funds, seven<sup>74</sup> have such guidelines. The main criterion used is the irregular amount having an impact on Community budget which is to be paid or which was unduly paid<sup>75</sup>. Another criterion is the eligibility of expenditure claimed<sup>76</sup>. Supplementary criteria relating to the irregularity itself are also employed: the scale and seriousness of the irregularity, the existence of intentional/deliberate behaviour, the category/nature of the irregularity, previous occurrence of the irregularity. Other criteria<sup>77</sup> — especially in the Structural Actions sector — may be the legal provision infringed, the type of project and expenditure, the practice employed in committing the irregularity, the penalties applicable in the event of failure to meet the requirements laid down in legal acts, or the impact that the irregularity might have on other projects funded for the same beneficiary<sup>78</sup>.

Where several individual irregularities with a financial impact under the reporting threshold relate to the same beneficiary running one or more projects under the same programme/measure, a large number of Member States communicate this fact to OLAF<sup>79</sup>. Member States also make use of information on irregularities for risk analysis purposes<sup>80</sup>. In cases where an irregularity with a financial impact was initially estimated above the reporting threshold, but is subsequently recalculated below the threshold, Member States have indicated that an update will be sent to the Commission on any such reduction.

#### 4.3.3. *Classification of irregularities*

Member States are required to classify irregularities in specific categories — irregularity<sup>81</sup>, suspected fraud<sup>82</sup> and fraud<sup>83</sup>.

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<sup>73</sup> 20 Member States for agricultural funds: BG, CZ, DK, DE, EE, IE, ES, FR, IT, CY, LV, LT, LU, HU, MT, AT (excluding export refunds), PL, PT, RO, UK; 19 for the Structural Funds: BE (BERBC03, Walloon region, ESF Agency, French Community; ESF VL Flemish Community), BG, CZ, DK, DE, EE, IE, ES, FR, CY, LV, HU, MT, NL, AT, PT, RO, SK, UK.

<sup>74</sup> BG, EE, CY, LV, MT, RO, SK.

<sup>75</sup> BG, CZ, DK, EE, IE, ES, CY, LV, LT, LU, HU, MT, PT, SK and UK.

<sup>76</sup> BE (French Community), FR, AT, PL.

<sup>77</sup> MT, UK (Northern Ireland), EE.

<sup>78</sup> UK (JIU).

<sup>79</sup> BE (except Walloon region), BG, CZ, FR (for agriculture only), IT, LV, LT, HU, MT, PL, PT (only for agriculture), RO, SI (only for agriculture), UK (except Scotland).

<sup>80</sup> For agriculture: all except DK; for the Structural Funds: all except EL, LT, LU, NL, FI.

<sup>81</sup> In conformity with European Council Regulation 2988/95 of 18 December 1995, an ‘irregularity’ means any infringement of a provision of Community law 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.

<sup>82</sup> Given that the reporting of irregularities is done at an early stage, the sectoral regulations provide that Member States must include, among the communicated irregularities, not only cases of established fraud but also cases of suspected fraud. According to EC Regulation Nos 1848/2006 for the agriculture

According to the 2007 Report on the protection of the Communities' financial interests, in the agricultural sector, Member States classified only 68% of the irregularities reported, while the figure was 67% for the Structural Actions and 57% for the pre-accession funds.

While the majority of Member States find it relatively easy to distinguish between irregularity and established fraud, some find it harder to identify cases of suspected fraud, because of difficulties in determining fraudulent or intentional behaviour<sup>84</sup>. Difficulties in classifying irregularities arise from insufficient information or evidence being available to the authorities at an early stage in the procedure<sup>85</sup> or from the limited practical experience or lack of expertise of the staff handling the irregularity<sup>86</sup>. Classification is also hindered by lengthy administrative and judicial procedures<sup>87</sup>, as an irregularity initially classified in a given category may subsequently need to be reclassified.

For agriculture, Member States<sup>88</sup> stated that they would classify an irregularity as a case of suspected fraud where this was indicated by the findings of the national management and control system (e.g. internal and external audits, internal control procedures, on-the-spot checks). In the same sector, only two Member States would classify an irregularity as a case of suspected fraud if the case had been brought before a court. For the Structural Funds, most<sup>89</sup> Member States use the first criterion and only four the second criterion. The first criterion is largely used for the pre-accession funds as well.

## **5. RECOVERY**

### **5.1. Own Resources**

The Member States have to recover established amounts, including those they register in the shared database OWNRES. The amount to be recovered following irregularities detected in 2008 is approximately €351 million.

An established amount may not be recovered completely, despite Member States' efforts. Amounts established may change because of additional information or judicial procedures, or the debt may be deemed irrecoverable because of the debtor's financial problems.

At present, the recovery rate for irregularities occurring in 2008 is 37.5% (approximately €32 million). This is an average starting position, although lower

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sector, and 2035/2005 and 2168/2005 for the structural and cohesion funds, 'suspected fraud' means an irregularity giving rise to administrative and/or judicial proceedings at national level in order to establish the presence of intentional behaviour.

<sup>83</sup> According to the Convention on the protection of the European Communities' financial interests, fraud is an irregularity committed intentionally, and is determined to be a criminal act only by the outcome of judicial proceedings.

<sup>84</sup> BE, ES, HU, LV, LT, PT.

<sup>85</sup> CY, MT.

<sup>86</sup> EE, HU, RO, FI, SE.

<sup>87</sup> RO, SI.

<sup>88</sup> BE, BG, CZ, DK, EE, FR, IT, LT, LU, PL, RO, SI, UK.

<sup>89</sup> BE, BG, CZ, DK, EE, IE, IT, CY, LV, LT, LU (ERDF), NL, PL, PT, RO, SI, SK, FI, SE, UK.

than last year's of 40%. Over the last decade the recovery rate has varied between 40% and 55%.

When non-recovery of an established debt is not attributable to a Member State, the Member State may request that the irrecoverable amount be written off. In 2008 the Commission refused Member States' write-off requests in 32 cases totalling some €17.4 million because it deemed that non-recovery was attributable to the Member States.

Moreover, certain Member States were held financially responsible for a total of more than €43 million because they did not establish customs debts where they should have done so.

## 5.2. Agriculture

Article 32 of Council Regulation (EC) No 1290/2005 provides for an automatic clearance mechanism for unsuccessful recoveries of unduly paid amounts. If a Member State fails to recover an unduly paid amount from the beneficiary within four years of the primary administrative or judicial finding (or, in the case of proceedings before national courts, within eight years), 50% of the non-recovered amount is charged to the budget of the Member State concerned as part of the annual financial clearance of the EAGF and EAFRD accounts. Even after the application of this mechanism, Member States are obliged to pursue their recovery procedures and to credit 50% of the amounts effectively recovered to the Community budget. If they fail to do so with the necessary diligence, the Commission may decide to charge the entire outstanding amounts to the Member State concerned.

As of financial year 2008, where undue payments are the result of administrative errors committed by the national authorities, the entire amount involved is deducted from the annual accounts of the paying agencies concerned, and thus excluded from Community financing.

For EAGF, this mechanism was applied for the second time by the financial clearance decision for the financial year 2007,<sup>90</sup> which cleared all pending non-recovered cases dating from 2003 or 1999 (cases which were four or eight years old respectively) by charging €31.4 million to the Member States. For those paying agencies for which the 2007 accounts were disjoined from the financial clearance decision, a further €0.05 million was charged by a subsequent decision<sup>91</sup>, and a further €6.2 million still remains to be charged.

Regarding the financial year 2008, Member States recovered €108 million, 32.2 was declared irrecoverable and the outstanding amount still to be recovered from the beneficiaries at the end of the financial year was €1 246 million for EAGF. The financial consequences of non-recovery for cases dating from 2004 or 2000 were determined according to the '50-50 rule' mentioned above by charging €31.4 million to the Member States in the financial clearance decision for the financial year 2008 adopted by the Commission on 29 April 2009<sup>92</sup>. A further €0.8 million will be

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<sup>90</sup> Decision 2008/396/EC (OJ L 139, 29.5.2008).

<sup>91</sup> Decision 2009/87/EC (OJ L 31, 3.2.2009).

<sup>92</sup> Decision 2009/367/EC, (OJ L 111, 5.5.2009).

charged by subsequent decisions. Due to this '50-50' clearance mechanism that was applied in the last years by charging some of the non-recovered amounts to the Member States the outstanding amount towards the EU budget was reduced to around €900 million.

Regarding EAFRD and the Transitional rural development instrument the clearance mechanism set out above did not apply yet. For these funds, the amount outstanding at the end of the financial year 2008 was €7.9 million. €17.2 million was recovered and €0.2 million was declared irrecoverable during financial year 2008.

### 5.3. Structural Funds

For the Structural Funds, recovery from the beneficiaries of amounts unduly paid owing to irregularity or fraud is also a matter for the Member States. These amounts can be recovered at Commission level by reducing or cancelling the financial contribution.

The programmes co-financed by the Structural Funds are multiannual and based on interim payments. Recovery of amounts unduly paid may take place before or after conclusion of the programme. For the 1994-99 programming period, the deadline for requesting final payment from the Commission was 31 March 2003. In that period, the Community co-financed around 1000 programmes worth some €159 billion in total.<sup>93</sup> The Commission's authorising and managing departments, assisted by OLAF, are responsible for administrative and financial follow-up once these programmes have been concluded.

For the *1994-99 programming period*, the Member States communicated 11035 cases of irregularities (62 in 2008) with a financial impact estimated at €1.51 billion<sup>94</sup> for the Community contribution (€10.95 million for 2008).

Of these cases, 5944 have been closed definitively at Commission level and an amount of €97 million was taken into account during final payment or decommitted after closure or reimbursed to the Community budget. Member States indicated that administrative and judicial procedures had been finalised at national level in a further 861 cases, with a financial impact of €9 million for the same period. The Commission has started reconciliation procedures with a view to closing these cases.

In 2008, the Commission adopted three decisions on how to treat 24 cases of irregularities for which the Member States concerned asked the Commission to bear the financial consequences of the irrecoverable amounts. One decision concerning 20 cases financed by FIG in the sum of €3 851 988 and two decisions concerning the ESF in the sum of €120 359 were charged to the Community budget.

For the *2000-06 programming period*, the Member States have so far communicated 15574 cases of irregularities (3791 in 2008) with a financial impact of some €2.30 billion for the Community contribution (€16.3 million for 2008).

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<sup>93</sup> These are multiannual programmes. This figure does not include projects directly financed under the Structural Funds and Cohesion Fund.

<sup>94</sup> Situation according to the data in the ECR database as at 15 April 2008.

The Member States have informed the Commission that administrative and/or judicial procedures have been finalised at national level for 7389 of these cases and that some €704 million has been recovered.

At the end of 2008, the total amount of *financial corrections* concerning the 1994-99 and 2000-06 programming periods was €1995 million (€114 million in 2008) and €3313 million (€1173 million in 2008) respectively. These are the result of audits by the Commission and the European Court of Auditors, OLAF investigations and the closure procedure for the two programming periods. They consist of expenditure affected by irregularities which, for this reason, must be excluded from co-financing by the EU budget. On top of that, the Member States also effect corrections following their own audits or Commission's and European Court of Auditors' audits. These are not registered in the Commission's accounting system, but the information is reported by the Member States to the Commission once a year.

#### **5.4. Direct expenditure**

In the areas where funds are managed directly by the institutions, amounts unduly paid are recovered directly by them, without the intervention of the Member States. The Financial Regulation and its implementing rules set out the different stages in the recovery procedure:

- estimation and establishment of the entitlement by the authorising officer (who must ensure that the claim is certain, of a fixed amount and due),
- establishment of a recovery order (instruction from the authorising officer to the accounting officer to proceed with recovery) followed by a debit note to the debtor, and
- recovery by the accounting officer, who will, if possible, effect the recovery by offsetting if the debtor has a claim on the Communities that is certain, of a fixed amount and due.

If, after reminders and letters of formal notice have been sent out, the debtor has not paid the debt and the accounting officer has not been able to recover the amount due by offsetting or calling in a bank guarantee provided by the debtor, the authorising officer determines, without delay, what method of enforced recovery should be applied to the debt.

There are two mutually exclusive ways of obtaining an enforcement order:

- a decision constituting an enforcement order within the meaning of Article 256 of the EC Treaty (formalises the establishment of the entitlement in a decision which constitutes an enforcement order);
- an order before the national or Community courts. This also includes a civil action within criminal proceedings in jurisdictions where this is possible.

In cases where recovery orders concerning irregularities and cases of fraud were launched during 2008, full or partial recovery has already been announced in 679 reported cases. The Commission has recovered €22 million. In 670 cases the full

irregular amount has been recovered. An amount of €13 million still remains to be recovered, concerning 262 cases.

### **5.5. Recovery following an OLAF case**

Where the final report of an OLAF case concludes that certain sums have probably been paid to a beneficiary against the rules or that sums that should have been collected have not been, the relevant authorities (generally the authorities in the Member States or third countries concerned) must recover the amounts in question. OLAF follows the course of these recovery proceedings.

In 2008, OLAF formally closed the financial follow-up for more than €146.8 million. €128 million was recovered in the field of the Structural Funds.

In 2008, OLAF also reviewed the financial follow-up procedures relating to OLAF cases. This resulted in new case handling and acceptance criteria involving *de minimis* thresholds to be applied from 1 January 2009. The introduction of these thresholds will enable OLAF's limited financial follow-up resources to be focused more sharply on the more significant cases of fraud or irregularity involving sizeable amounts of money. For more details see the OLAF report<sup>95</sup>.

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<sup>95</sup> [http://ec.europa.eu/comm/anti\\_fraud/reports/index\\_en.html](http://ec.europa.eu/comm/anti_fraud/reports/index_en.html).