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

**Protection of the European Union's financial interests-Fight against fraud-Annual  
Report 2009**

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## INTRODUCTION

The protection of the EU's financial interests and the fight against fraud are areas in which responsibility is shared between the European Union and the Member States. Each year the Commission, in cooperation with the Member States, produces a report presenting statistics and the new measures they have taken to meet their obligations in this field, in accordance with Article 325 (5) TFEU. The report is sent to the European Parliament and the Council and is published<sup>1</sup>. This year's report also analyses two special topics that the Commission and the Member States have agreed to present in the 2009 report and to which Member States have contributed via a questionnaire<sup>2</sup>. These topics are 'Cooperation between the Commission and the Member States concerning on-the-spot checks' and 'Measures taken by the Member States for the recovery of irregular amounts'. Both topics are of particular relevance for the EU institutions<sup>3</sup> as well as to the national competent authorities.

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, cohesion policy and pre-accession funds, i.e. around 80% of the budget) and for the collection of the EU's traditional 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 statistics must be read and used with great care: a reported irregularity is not in most cases a possible fraud (which is a deliberate act). A reported suspicion of fraud is not necessarily a fraud confirmed by a court judgment. All the irregularities presented are being dealt with and are subject to different forms of follow-up, as described in parts 1 and 5.

The **second part** focuses on the **international dimension** of the protection of the EU's financial interests and presents the state of ratification of the protection of financial interests (PFI) instruments.

In **part 3** the report deals with administrative measures taken by the Commission to fight fraud and irregularities in the customs area.

**Part 4** gives an overview of the results of the questionnaire regarding **cooperation between the Commission (OLAF) and the Member States concerning on-the-spot checks**<sup>4</sup>.

The **final part of the report** deals with **recoveries** made in 2009 in all budget areas and presents the measures that Member States take for securing the recovery of irregular amounts.

The report is accompanied by two Commission working papers<sup>5</sup>.

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<sup>1</sup> Previous years' reports: [http://ec.europa.eu/anti\\_fraud/reports/anti-fraud\\_en.html](http://ec.europa.eu/anti_fraud/reports/anti-fraud_en.html).

<sup>2</sup> The complete results of the questionnaire are presented in the document 'Implementation of Article 325 TFEU in 2009 by the Member States' (Accompanying document 1 to this report).

<sup>3</sup> See also the Resolution of the European Parliament of 24 April 2009 on the protection of the Communities' financial interests and the fight against fraud — Annual report 2007 (2008/2242(INI)).

<sup>4</sup> See Accompanying document 1 'Implementation of Article 325 TFEU in 2009 by the Member States'.

## **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 2009**

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

Distinguishing between fraud and other irregularities is important. An irregularity is any infringement of an EU provision by an economic operator which has, or would have, the effect of prejudicing the EU's financial interests<sup>6</sup>. Fraud is an irregularity committed intentionally which constitutes a criminal offence<sup>7</sup>. The Member States must 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>8</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>5</sup> For references, see cover page of the report.

<sup>6</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>7</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>8</sup> Second Accompanying document to this report.

Table 1: Number of irregularities and amounts — 2009

Area	Number of irregularities reported		Total estimated financial impact of irregularities, including suspected fraud (€ million)		Estimated financial impact of suspected fraud only (€ million)	
	2008 <sup>9</sup>	2009	2008 <sup>10</sup>	2009	2008	2009
<b>Agriculture</b>	1 133	1 621	102.3 (0.24 % of allocations)	125 ( 0.24 % of allocations)	4 (0.01 % of allocations)	13.3 (0.03% of allocations)
<b>Cohesion Policy</b>	4 007	4 931	585.2 (~0.11 % of allocations)	1 223 (2.53% of allocations)	57 (~0.11 % of allocations)	109 (~0.23 % of allocations)
<b>Pre-accession funds</b>	523	706	61(~0.9 % of allocations)	117 (~ % 0.78 of allocations)	13 (~0.9 ~% of allocations)	57 (0.38~% of allocations)
<b>Direct expenditure</b>	932	705	34.7 (~0.17 % of allocations)	27.5 (~0.17 % of allocations)	3.2 (~0.02 % of allocations)	1.5 (~ 0.01 % of allocations)
<b>Total expenditure</b>	6 595	7 963	783.2(~ 0.07 % of the expenditure in the four areas)	1 492.5 (1.13% of the total expenditure in the four areas)	77.2 (~ 0.07 % of the expenditure in the four areas)	180.8 (0.13 % of the expenditure in the four areas)
<b>Own resources<sup>11</sup></b>	6 075	4 648	375 (~0.46 % of the total amount of own resources) <sup>12</sup>	343 (~0. 23 % of the total amount of own resources)	75 (~0.46 % of the total amount of own resources)	99 (~0.68 % of the total amount of own resources)

## 1.2. Revenues

### 1.2.1. Traditional own resources (TOR)

The number of cases of irregularities reported in 2009 was 23 % lower than in 2008 (4 648 cases in 2009, compared with 6 075 in 2008), while the estimated amount is also 8.5 % lower (from €375 million in 2008 to €343 million in 2009). The number of communications from the *ten new Member States* showed continued growth since their accession in 2004 until 2007. In 2008 the growth stopped and 2009 shows 2 % less communicated cases compared with 2008 although the amount of TOR increased by 20 % from 2008 to 2009.

Suspected fraud accounted for approximately 19 % of cases of irregularities reported, with an estimated financial impact of approximately €99 million.

<sup>9</sup> The figures have been updated for certain sectors since the 2008 report.

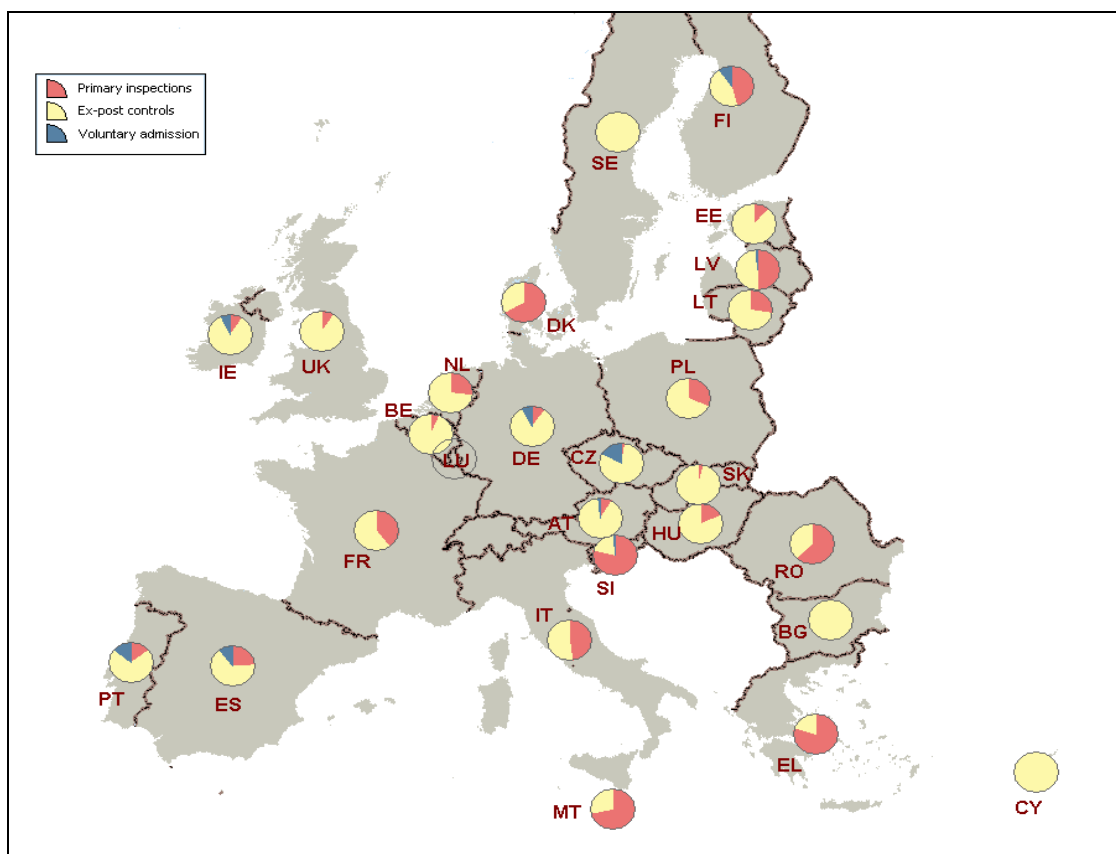
<sup>10</sup> Idem.

<sup>11</sup> Customs duties and agricultural levies.

<sup>12</sup> This percentage is based on an estimate of traditional own resources in the 2009 general budget, and not on accounts.

The methods of detection of irregularities vary between Member States; however, in 2009 the vast majority of cases (75 %) were detected by means of either primary national inspections or post-clearance control audits. A large group of Member States<sup>13</sup> mostly use ‘ex-post controls’ to detect irregularities. Primary inspections are used in particular in Denmark, Slovenia, Romania, Malta and Greece.

Chart 1 illustrates by which methods OWNRES<sup>14</sup> cases — in amounts — have been discovered by the Member States in 2009. For reasons of presentation the following methods are included in the term ‘ex-post controls’: audit of the accounts, Commission inspections, inspections by anti-fraud services, inspection visits, national post-clearance audits and tax audits.



**Chart 1: Detection of irregularities in 2009 — methods**

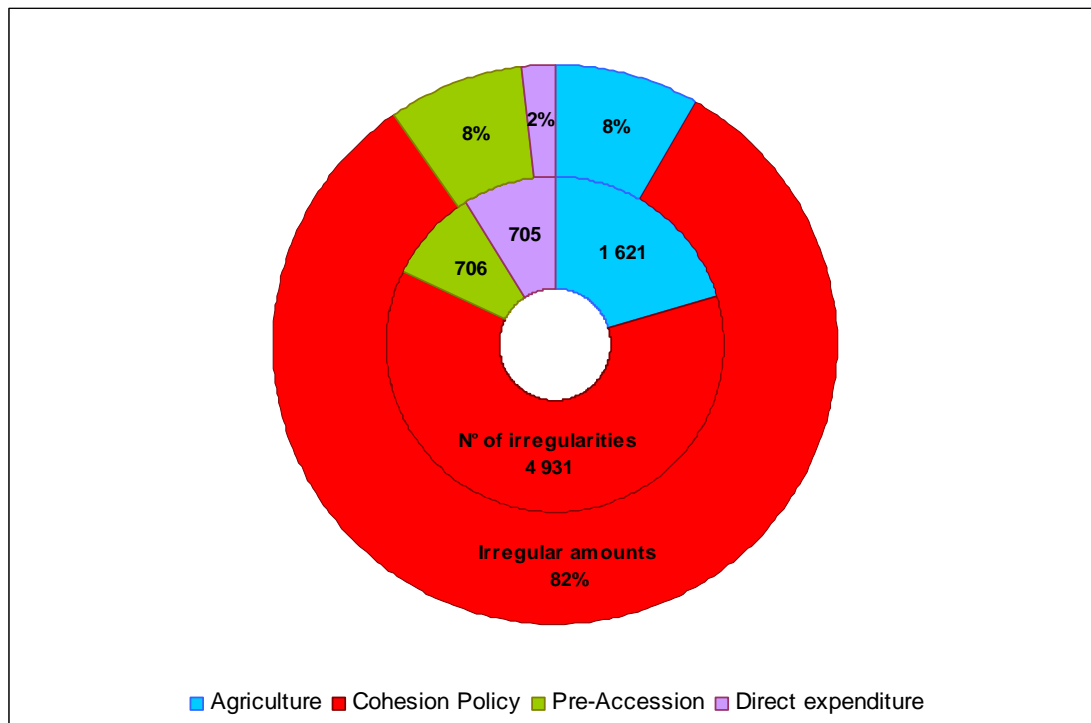
The goods involved in irregularities and frauds demanding Member States’ attention are very diverse. TVs and monitors, clothing and of course tobacco keep their relevance in 2009 and like in previous years are the most important goods involved in registered cases of irregularity or fraud. The origin of the goods concerned is likewise varied, although some countries remain continuously at the top of the rankings (China, the United States, Japan).

<sup>13</sup> BG, CY, AT, SE, HU, SK, BE, EE, LT, DE, ES, PT, FR, IE, UK.

<sup>14</sup> OWNRES is an abbreviation for own resources; the OWNRES database is a key tool for obtaining data for global analysis of fraud and irregularities affecting traditional own resources.

### 1.3. Expenditure — overall analysis

The report analyses four main headings on the expenditure side of the EU budget: Agriculture, Cohesion policy, Pre-accession assistance and Direct expenditure, covering different policies ranging from research and development to humanitarian aid.



**Chart 2: Proportion of the above-mentioned four budget areas in terms of reported irregularities and suspicions of fraud (inner circle) and the related financial amounts (outer circle) in 2009.**

The Cohesion Policy and Pre-Accession Assistance present a share of the irregularities that exceeds by far their share of resources on the overall budget, showing that they remain sectors where the management and control systems need further improvements.

In general, for what concerns the reporting of irregularities for the expenditure part of the EU budget, 2009 should be regarded as a transition year due to the introduction of the internet based reporting system (IMS- Irregularity Management System) which may have caused problems in relation to the reporting, registration and migration of irregularities into the new system. However, the new reporting system has improved the overall conditions for irregularity reporting. It is therefore welcomed by the majority of the Member States which have already used it for the 2009 reporting year. All Member States should fully implement the IMS and be ready to use the system for the 2010 reporting exercise.

#### 1.3.1. Agricultural expenditure

In 2009, Member States reported 1 621 new cases with a total amount affected of about €125 million. An increase of 43 % of reported cases is registered in comparison to 2008, as well as an increase of 23 % in the irregular amounts reported. A reason for this increase is the entry into operation of IMS, which allowed far more users to process communications, thus having



a direct impact on the number of cases reported. Spain reported the highest number of cases (404) and Italy reported the highest amounts affected (€54 million).

Compliance by Member States has improved with the introduction of the new internet-based reporting system, although some attention still needs to be paid to issues such as timely reporting, personal data and measures affected.

Therefore, the Commission calls upon Member States to further improve compliance with special reference to the latter issues, by using the newly introduced internet reporting system.

For expenditure from the financial years 2006-09, Member States have reported so far 2086 cases of irregularities, with a total affected amount of €97 million. The highest number of cases was reported by Spain (377) and the highest amounts affected by irregularities were reported by Italy (€14 million). The highest expenditure was made by France (20%), while the number of irregularity cases (127) and the corresponding amounts affected by irregularities (€9 million, representing 0.09% of expenditure) communicated by France remain rather low compared to the expenditure. For the same financial years, Member States have communicated 288 cases of suspected fraud, with a total amount affected of €12 million.

Sectors with a rather high irregularity rate are 'sugar', 'pig meat, eggs and poultry', 'cereals', 'rural development' and 'fruits and vegetables'. These figures should be considered as a half-time result, as cases of irregularities concerning the 2006-2009 expenditure will continue to be reported in the coming years.

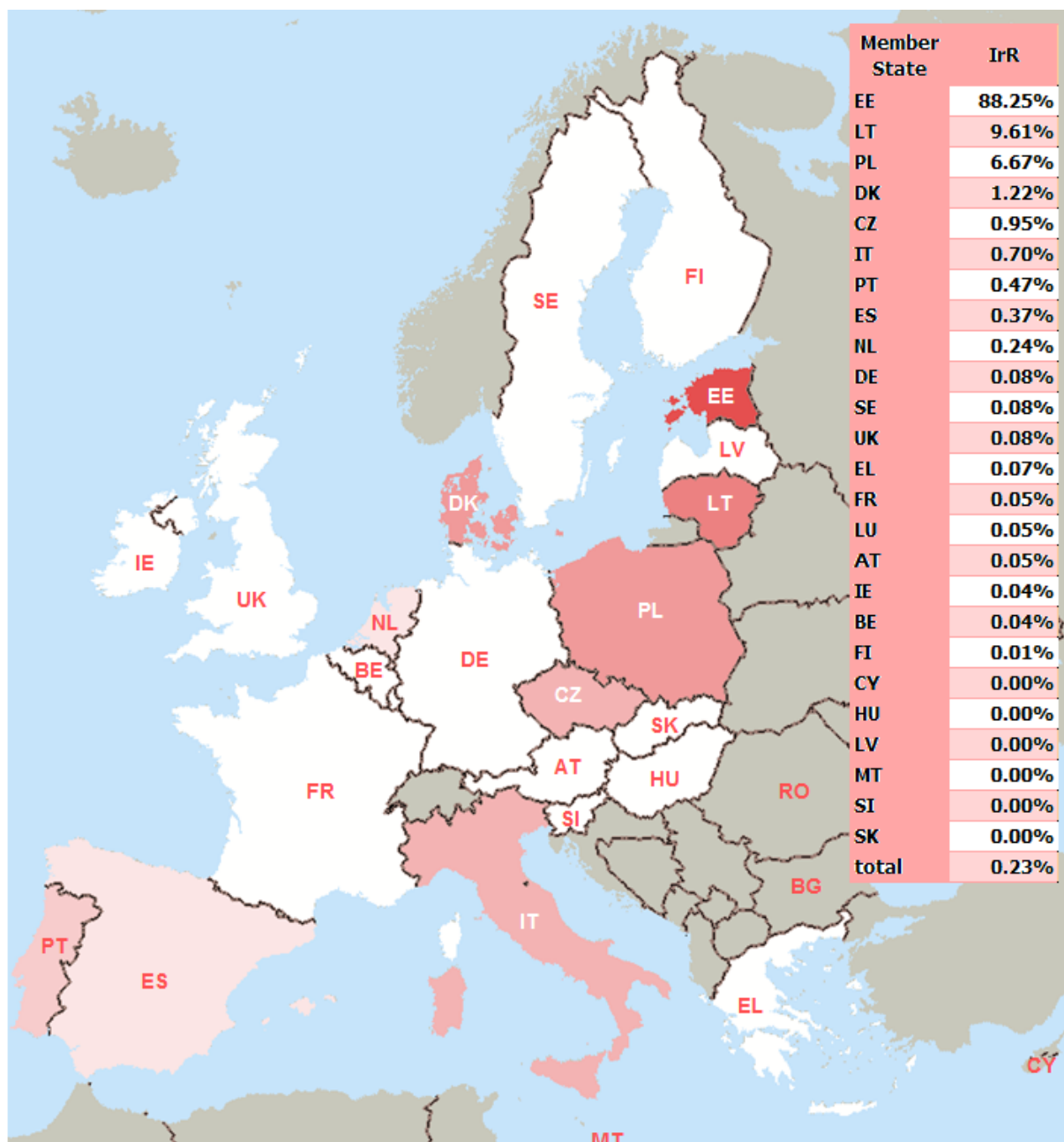
Definitive figures can only be determined for years that can be considered as 'finalised'. The financial year 2004 is the latest financial year to be considered as finalised. Audit plans have been executed, recovery procedures have been started and irregularities have been reported.

The total expenditure for 2004 was about €43 billion. Member States reported in total 2216 cases with a total amount affected of about €99 million. This implies an irregularity rate of 0.23%.

Chart 3 provides an overview of the irregularity rates per Member State<sup>15</sup> in 2004. The irregularity rate varies considerably between the Member States. This may be an indication of the effectiveness of the control systems in place and it is a question that will necessitate further monitoring. Member States classified 37 cases as suspected fraud, of which 23 cases (62%) were reported by Italy.

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<sup>15</sup> CY and MT are not indicated on the map, the reason being that they had no expenditure for this sector in 2004.



**Chart 3: Irregularity rate per Member State-EU-25, in 2004**

### 1.3.2. Cohesion Policy

In 2009, 4931 irregularities were reported, involving an overall amount of €1.22 billion. Reported irregularities and related financial amounts have been increasing in relation to 2008. The increase has been significant in terms of both number of reported irregularities (+23%) and irregular amounts (+109%). A number of factors could explain these increases: reported irregularities concern three different programming periods (1994-99, 2000-06 and 2007-13); Romania and Bulgaria have both reported irregularities; the closure of the 2000-06 programming period is approaching and there is an increase in checks and audits linked to this event.

In particular, the last argument seems the most pertinent, considering also that a similar situation has been encountered (and with even higher differences in relation to the previous year) for the closure of the 1994-99 programming period.

However, given the multi-annual nature of the programmes run under the cohesion policy, the analysis by programming period provides more interesting indications than an analysis based on yearly budgets.

Throughout the 2000-06 programming period, which is approaching its closure (2010), the overall irregularity rate is almost 1.6%, while the fraud rate is about 0.25%. These rates exclusively represent the estimated impact on the payments from the Commission to the Member States of, respectively, irregularities (including suspected and established fraud) and suspected fraud (alone). In both cases, therefore, these rates fail to indicate what the real dimension of irregularities and fraud is. These rates represent the results of the checks and audits by national competent authorities and no extrapolation is allowed unless the size of the audited and checked sample is known.

The highest irregularity rates concern the European Regional Development Fund (ERDF)<sup>16</sup> and Objective 2 programmes (aimed at revitalising areas facing structural difficulties). For the ERDF the most plausible explanation is that this fund finances projects of a higher value and therefore irregularities tend also to involve a greater amount. For the Objective 2 programmes, the very high irregularity rates of the UK and the Netherlands, which mainly benefit from this type of programmes, may have influenced the overall rate.

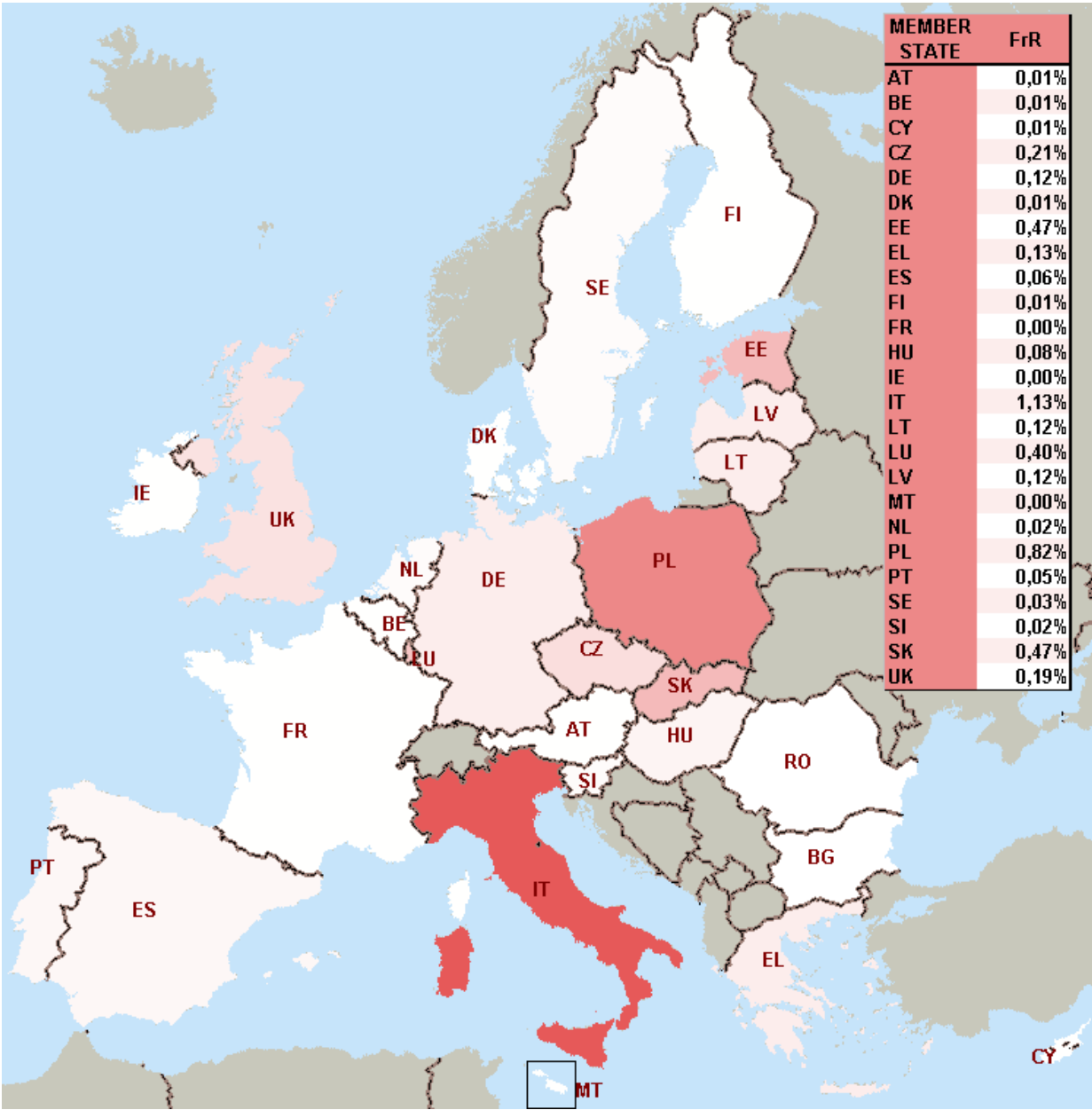
In terms of suspected fraud rate, the ERDF remains the most affected fund (0.29%). Objective 1 programmes (supporting developments in less prosperous regions) present the highest rate (0.30%), followed by Objective 3 programmes (which support the adaptation and modernisation of education, training and employment policies and systems in non-Objective 1 regions) with 0.17%<sup>17</sup>.

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<sup>16</sup> The ERDF finances direct aid to investments in companies (in particular SMEs) to create sustainable jobs; infrastructure projects linked notably to research and innovation, telecommunications, the environment, energy and transport; financial instruments (capital risk funds, local development funds, etc.) to support regional and local development and to foster cooperation between towns and regions; technical assistance measures.

<sup>17</sup> Given the fact that regions benefiting from the Objective 1 programmes are the less prosperous regions and those benefiting from Objective 3 programmes are the richest, *need* and *greed* seem the principal drivers behind fraud.

Italy, Poland, Estonia and Slovakia present the highest suspected fraud rates among Member States as shown in Chart 4:



**Chart 4: Fraud rate per Member State (EU-25) for the 2000-06 programming period**

However, higher suspected fraud rates may not necessarily mean that more fraudulent activity affecting the EU’s financial interests is taking place in certain Member States. It is rather an indication that the anti-fraud systems in place are performing well (capable of detecting fraud and willing to report it), which always produces higher results. The Commission will further monitor these results and analyse the relationship between the anti-fraud systems in place and the suspected fraud rates reported.

Among the Member States with very low suspected fraud rates Spain and France stand out (especially in relation to their size and to the financial support received). In particular, those results could indicate either a lower fraud detection capability or the fact that a proportion of any detected fraud remains unreported.

Finally, data related to the Cohesion Fund remain too fragmented to provide a reliable picture. The Commission is working on the full deployment of IMS also for the Cohesion Fund and this is expected to improve the situation in the coming years. Member States<sup>18</sup> which have not yet introduced the new reporting system are invited to deploy all the necessary efforts for its implementation.

In order to simplify the irregularity reporting process, on 1 September 2009 Commission Regulation (EC) No. 1828/2006<sup>19</sup> was amended<sup>20</sup>. The main objectives of the amendments introduced were to clarify the existing provisions based on the experience gained by the Commission and the Member States with regard to the application of Regulation (EC) No. 1681/94 concerning irregularities and the recovery of sums wrongly paid in connection with the financing of the structural policies and the organisation of an information system in this field<sup>21</sup>, by making the reporting easier while ensuring that important data for risk analysis are not lost, and to align reporting provisions concerning structural funds to a large extent with the provisions applicable to the agricultural sector.

### 1.3.3. *Pre-accession funds*

In 2009, 706 newly detected irregular cases with an affected amount of €117 million were reported by the national authorities in 14 reporting countries. An increase of 35 % in the number of cases is recorded. It demonstrates that detections in the area of pre-accession assistance are not phasing out but rather shifting towards a smaller group of countries, i.e. EU-2 and candidate countries. Bulgarian and Romanian irregularities together make up 81 % of cases and 93 % of irregular amounts reported in 2009. Yet, the rising tendency is only applicable to Bulgaria, with an increase of 134 % in cases. Consequently, the trends are highly influenced by their reporting patterns and thus the focus of analysis is narrowed down.

The EU amounts affected keep rising and thus accumulate with reference to the whole programming period, while allocations remain fixed and payments are gradually declining. As a consequence irregularity and suspected fraud rates show a rising trend.

Five Member States (Bulgaria, Hungary, Poland, Romania, Slovakia) and Turkey reported suspected fraud cases in 2009. The number of cases of suspected fraud was 262, with a financial impact of €57 million.

The highest number of suspected fraud cases was reported by Bulgaria. Suspected fraud cases detected for the SAPARD<sup>22</sup> fund clearly dominate the picture. They make up 67 % of all the cases from this country. In fact, Bulgarian SAPARD cases account for 92 % of all SAPARD suspected fraud in 2009 reported to OLAF. Bulgarian authorities were requested by the Commission to enhance control systems and carry out additional checks and this is reflected in the rising figures of detected and reported suspected fraud cases. The drastically rising share of suspected fraud is expected to decline following the finalisation of judicial procedures and communication of updated reports in the coming years.

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<sup>18</sup> Spain and France did not use the IMS in 2009 and Sweden and Ireland have still to fully implement it.

<sup>19</sup> OJ L 371, 27.12.2006.

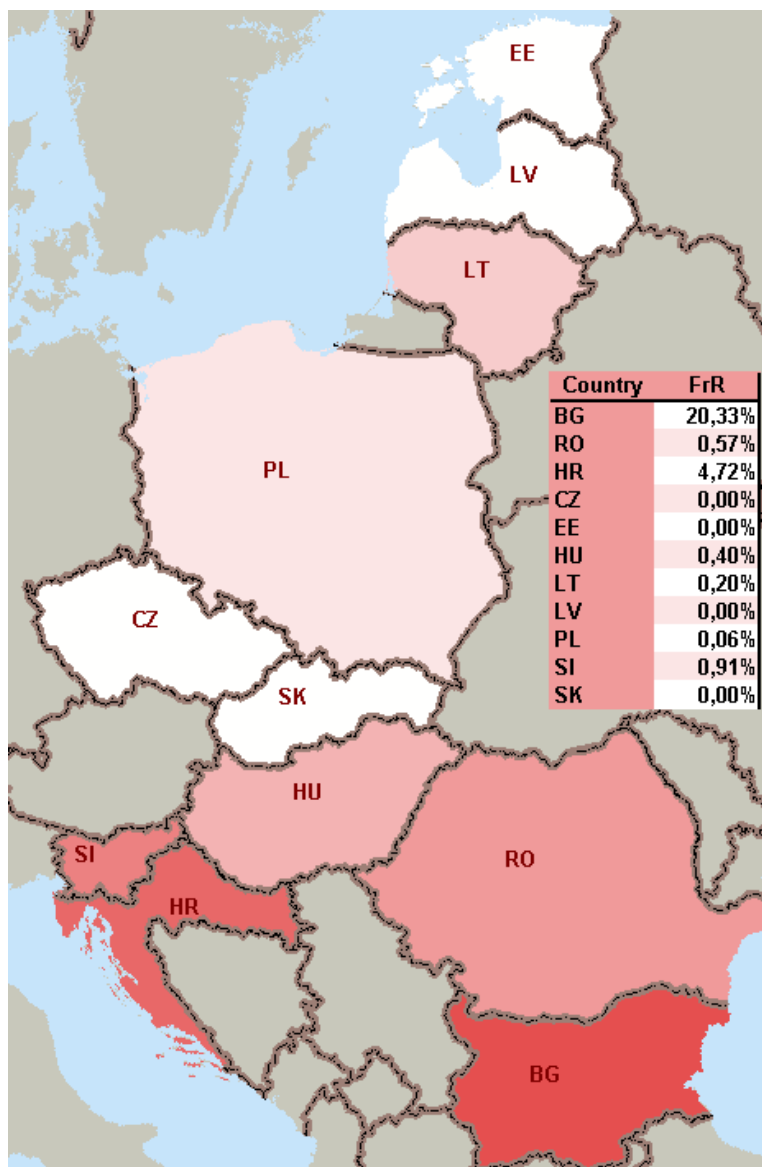
<sup>20</sup> OJ L 250, 23.9.2009.

<sup>21</sup> OJ L 172, 7.7.1994.

<sup>22</sup> This programme has supported agricultural and rural development in candidate countries.

The total suspected fraud rate for the whole programming period of SAPARD is at the level of 2.8%. The Bulgarian fraud rate for SAPARD is 20%, while the Czech Republic, Estonia, Latvia and Slovakia have a zero fraud rate which puts, for instance, in question the reliability of the reported information or the fraud detection capability in the SAPARD sector.

Chart 5 shows the fraud rate for SAPARD by country.



**Chart 5: suspected fraud rate for SAPARD programme per Member State and per Candidate Country in 2009.**

Controls seem to be well spread. Control of documents and audit are the most frequently applied methods of detecting irregularities in 2009. The majority of suspected fraud cases in Bulgaria were detected by audit. The exceptional situation in Bulgaria points to some weaknesses in the national anti-fraud system.

The Member States and Candidate countries are invited to report irregularities via the new Pre-accession Assistance Module of IMS as soon as this module becomes operational<sup>23</sup>.

#### 1.3.4. *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, which is a transverse, transactional information system allowing all budgetary and accounting operations to be executed and monitored by the Commission. One of the functionalities of the ABAC system is the 'recovery context', which gathers detailed information on recovery orders issued by the Commission departments and registered in ABAC. The recovery context is a relatively new functionality within the system. The collection of data from the Commission departments only started recently and the current data available in ABAC refer to recovery orders issued since 2008. The data presented should therefore be treated with particular caution and not as empirical evidence of the level of fraud and irregularity.

The number of recovery orders relating to cases of irregularities and suspected fraud in this area came to 705, with a presumed financial impact of €27.5 million, €1.5 million of which was accounted for by 15 reported cases of suspected fraud. Irregularities in the sector of external action accounted for €4.4 million and in the area of internal policies for €23.1 million.

#### 1.4. **Statistics on OLAF's activities**

Once a preliminary evaluation has been made of information received, OLAF may open any of five types of cases: an internal investigation, an external investigation, a coordination case, a criminal assistance case or a mutual assistance case. The number of cases opened each year is stable (220 in 2009, 204 in 2008 and 201 in 2007). 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 (455 at the end of 2009, compared with 425 at the end of 2008). The table below provides a snapshot of the situation at the end of 2009. The slight increase in the number of active investigations as compared to 2008 is partially due to the introduction of a *de minimis* policy, whereby OLAF is focussing its operational resources on more complex fraud cases which by their nature require longer periods of investigation.

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<sup>23</sup> Once the module becomes fully operational it will manifest a number of advantages like improved compliance, less technical nature mistakes, possibility for reporting authorities at different levels to access information on all the (open) irregularities already reported.

Table 2: Cases ongoing as at 31 December 2009 by sector, and their financial impact

Sector	Cases under active investigation 31 December 2009	Financial impact from investigation (€ million)
Agriculture	79	106.48
Cigarettes	32	65.31
Customs	36	245.23
Direct expenditure	47	65,41
EU institutions and bodies	133	25.07
External Aid	86	153.31
Structural funds	43	658.19
Trade	1	0.29
<b>Total</b>	<b>457</b>	<b>1319.29</b>

For more details and a comparison with previous years, see the OLAF report.<sup>24</sup>

<sup>24</sup> [http://ec.europa.eu/comm/anti\\_fraud/reports/index\\_en.html](http://ec.europa.eu/comm/anti_fraud/reports/index_en.html).



## **2. THE INTERNATIONAL DIMENSION OF THE PROTECTION OF THE EUROPEAN UNION'S FINANCIAL INTERESTS**

The protection of financial interests and the fight against fraud and corruption are tasks for the European Union that go beyond its borders and need therefore to be reflected in the international agreements that the Union is concluding with third countries or in the multilateral conventions to which it becomes a party.

To effectively combat fraud, corruption, smuggling of cigarettes and other illegal activities detrimental to its financial interests, the EU on its behalf and on behalf of the Member States is negotiating anti-fraud agreements with third countries and takes part in multilateral agreements or conventions.

### **2.1. Anti-corruption multilateral agreements**

The European Commission on behalf of the European Union negotiated the conditions for the implementation of the United Nations Convention against Corruption (UNCAC) at the 3rd Conference of the States Parties. Alongside Member States, the European Union is a 'state party' to the Convention within its area of competence (prevention measures in the public and private sectors, such as the establishment of anti-corruption bodies, and transparency and accountability in matters of public finance, effective asset recovery and international cooperation). Parties are required — inter alia — to take measures which will support the tracing, freezing, seizure and confiscation of the proceeds of corruption. The Conference also adopted the terms of reference of the review mechanism for the Convention. It will require the European Union to assess its compliance with the standards of the UNCAC and prepare itself for the review in the coming years.

The Commission also takes part in the activities of the European anti-corruption network, which was created by the Council in 2008<sup>25</sup>. It was formally established in November 2009 at a meeting of the European Partners against Corruption (EPAC) in Slovenia, where the rules of procedure were adopted and the management bodies set up. The Commission (OLAF) is a formal member of EPAC.

### **2.2. Negotiation of bilateral anti-fraud agreements**

In the context of the reinforced commitment of the EU and the G-20 to establish a high level of international cooperation with the financial centres and tax havens in third countries which match the OECD standards on tax cooperation, and following the Ecofin Council meeting of February 2009, the Commission amended its proposal, adopted on 10 December 2008, for a Council Decision on the signing and on the conclusion of a cooperation agreement between the European Community and its Member States, of the one part, and the Principality of Liechtenstein, of the other part, to combat fraud and any other illegal activity to the detriment of their financial interests.

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<sup>25</sup> Council Decision 2008/852/JHA of 24 October 2008 on a contact-point network against corruption (OJ L 301, 12.11.2008).

The amended proposals<sup>26</sup> were adopted in November 2009 and take on board the recent standards for provisions on exchange of information in the field of taxation and the changes imposed by the entry into force of the Lisbon Treaty.

This agreement would bring considerable added value in so far as its scope covers not only tax evasion, tax fraud and any other illegal activities affecting the financial interests of the parties, but also the exchange of information on tax matters, in line with the OECD standard, thereby preventing banking secrecy being relied on as an exception that would prevent information exchange. The agreement contains provisions on administrative assistance, in particular on assistance on request (requests for information, for surveillance and for investigations) and on special forms of cooperation and recovery. However, it also allows for mutual legal assistance in all matters of tax offences.

This agreement is of the utmost importance as it should also serve as a model for anti-fraud agreements with other third countries (Andorra, Monaco, San Marino and the Swiss Confederation), along the lines of the recommendation adopted by the Commission in June 2009. The agreement should therefore be signed without delay and the Council should give its approval.

### **2.3. Negotiation of anti-fraud provisions to be included in Association Agreements (AAs) and Partnership and Cooperation Agreements (PCAs)**

In line with its enhanced European Neighbourhood Policy (ENP), the European Commission is currently conducting negotiations for a new, comprehensive agreement with Ukraine, a priority partner country within the ENP. Relations between the EU and Ukraine have since 1998 been based on the Partnership and Cooperation Agreement (PCA), which provides a comprehensive framework for cooperation between the two parties.

At the Paris Summit between the EU and Ukraine in September 2008, an agreement was reached to start negotiations on an EU and Ukraine Association Agreement (AA), which is to be the successor agreement to the PCA. The AA should renew the EU-Ukraine common institutional framework, facilitating the deepening of relations in all areas, including the protection of the EU's financial interests and the fight against fraud and corruption affecting EU funds.

The provisions in the financial cooperation chapter negotiated with the Ukrainian counterparts represent the most comprehensive and broadest set of anti-fraud and control provisions in relation to the Commission's competences in this area. The chapter consists of a wide range of stipulations regarding the exchange of information and further cooperation at operational level, the prevention of irregularities, fraud and corruption, the communication of irregularities, on-the-spot checks, administrative measures and penalties, etc.

The Commission, through OLAF, is currently leading several PCA and AA negotiation processes<sup>27</sup> with respect to financial cooperation and protection of the EU's and its partner countries' financial interests. The financial cooperation chapter within the EU-Ukraine Association Agreement could be used as a solid basis for future negotiations.

<sup>26</sup> COM(2009) 644 final, 23.11.2009 and COM(2009) 648 final, 2.12.2009.

<sup>27</sup> Armenia, Azerbaijan, Brunei, China, Georgia, Iraq, Libya, Malaysia, Moldova, Mongolia, Philippines, Russia, Ukraine and Vietnam.

## 2.4. Fight against international illicit tobacco traffic

Illicit trade in tobacco products is a criminal activity with a number of particularly harmful aspects. The Commission, through OLAF, not only assists and supports law enforcement authorities throughout the EU with their operational cases, but also coordinates major tax and criminal investigations with the Member States and third countries. OLAF organises and coordinates Europe-wide and world-wide customs operations to target specific problems, such as Operation Diabolo in 2007 (aimed at intercepting counterfeit products from China which are smuggled in shipping containers to the EU); Operation Mudan in 2008 (to address the growing problem of smuggling of cigarettes by post), and Diabolo II (which had the same objective as the first Operation Diabolo) in September 2009.

In 2009, the Commission continued to play a leading role in the negotiations on a protocol to eliminate illicit trade in tobacco products. This protocol is based on the WHO Framework Convention on Tobacco Control, an international treaty with currently 168 parties. The Commission (represented by OLAF and DG SANCO) has worked closely, and effectively, with the Member States and the Council, in the context of the Working Party on Customs Union (Legislation and Policy) to coordinate the position of the EU for these intergovernmental negotiations. Central to this coordinated position is the provision of Article 7 (Tracking and tracing). The Commission views this particular provision as being the core of the Protocol and an essential instrument in the fight against the illicit trade.

The Commission invites Member States to continue joint efforts to make these negotiations a success.

## 2.5. Ratification process for protection of financial interests (PFI) instruments

The second Protocol to the Convention on the Protection of the European Communities' Financial Interests<sup>28</sup>, which contains in particular provisions on liability of legal persons, confiscation and money laundering, entered into force on 19 May 2009, after the Member States concerned notified their ratification<sup>29</sup>.

Hungary ratified the Convention and its protocols<sup>30</sup> on 18 January 2010, with a single declaration with regard to the protocol on the interpretation of the Convention by the European Court of Justice (ECJ). Estonia has yet to ratify this latter protocol. The Czech Republic and Malta remain the only Member States that have not yet ratified either the Convention on the Protection of the European Communities' Financial Interests or its protocols. With regard to the follow-up of the second report on the implementation by the Member States of these instruments<sup>31</sup>, the Commission has engaged in further analysis on the conformity of national provisions, in particular as regards Austria, Belgium, France, Germany, Ireland, Italy and Luxembourg.

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<sup>28</sup> OJ C 316, 27.11.1995.

<sup>29</sup> See also Communication from the Commission on the entry into force on 19 May 2009 of the second PFI protocol, OJ C 219, 12.9.2009.

<sup>30</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) and Second Protocol of 19 June 1997 (OJ C 221, 19.7.1997).

<sup>31</sup> COM(2008) 77 final, 14.2.2008.

The Member States are invited to proceed with the ratification of these legal instruments without delay.

### **3. OTHER OPERATIONAL SUPPORT MEASURES TAKEN BY THE COMMISSION IN 2009: PROGRESS IN THE CUSTOMS AREA**

Further progress was achieved in 2009 in the customs area, with the deployment, in accordance with the new Regulation 766/2008<sup>32</sup>, of a new customs database and the joint customs operation Diabolo II.

#### **3.1. The joint customs operation Diabolo II**

This joint customs operation led to the seizure of more than 65 million counterfeit cigarettes and 369 000 other counterfeit items (shoes, toys, cameras, headphones, hats, caps, gloves, handbags, etc.) representing over 20 different trademarks. It also resulted in further international investigations into criminal activities. The operation, coordinated by the European Commission through the European Anti-Fraud Office (OLAF), was named 'Diabolo II' following the successful 2007 joint customs operation 'Diabolo I'.

The success of this joint operation highlights the importance of maintaining close cooperation among all partners to combat the global trade in counterfeit goods and to protect legitimate trade in genuine products. This operation is an excellent model for future operational cooperation, built on confidence and trust, involving all ASEM (Asia–Europe meeting)<sup>33</sup> partners.

ASEM, with its 45 European and Asian members, again proved an effective platform for cooperation among customs administrations. Diabolo II targeted the smuggling of counterfeit cigarettes and other counterfeit goods within the framework of ASEM. The operation took place in September/October 2009, coordinated by OLAF with the support of Europol and Interpol.

The operation's success is due to cooperation and effective work involving customs officials from 13 Asian countries and 27 EU Member States and constitutes an encouragement for the conduct of further common operations.

#### **3.2. Deployment of improved databases — Customs Files Identification Database (FIDE)**

The objective of FIDE (a new database used by the Member States' customs authorities) is to help prevent operations in breach of customs and agricultural legislation applicable to goods entering or leaving the customs territory of the EU and to facilitate and accelerate their detection and prosecution. A decision was adopted by the Council on 30 November 2009, replacing the CIS Convention and its FIDE protocol<sup>34</sup>.

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<sup>32</sup> OJ L 218, 13.8.2008.

<sup>33</sup> ASEM members: Brunei, Cambodia, China, India, Indonesia, Japan, Korea, Laos, Malaysia, Mongolia, Myanmar, Pakistan, Philippines, Singapore, Thailand, Vietnam, ASEAN secretariat, all EU Member States and the European Commission.

<sup>34</sup> Decision 2009/917/JHA, OJ L 323, 10.12.2009.

FIDE enables the national authorities responsible for carrying out customs investigations when opening a file on or investigating one or more persons or businesses to identify competent authorities of other Member States which are investigating or have investigated those persons or businesses in order to coordinate their investigations. FIDE acts as a registry of persons or companies subject to investigation without revealing details on the investigation.

Member States that are not yet using the FIDE database are invited to do so in order to better coordinate their investigations.

#### **4. RESULTS OF THE QUESTIONNAIRE REGARDING COOPERATION WITH THE MEMBER STATES CONCERNING ON-THE-SPOT CHECKS**

On-the-spot checks and inspections are one of the most powerful tools available to the Commission to conduct administrative investigations outside the EU institutions and bodies with a view to achieving the objective of combating fraud and other illegal activity undermining the EU's financial interests. An on-the-spot check is an inspection carried out on the premises of an economic operator. The power to conduct such checks was conferred on the Commission by Regulation 2185/1996<sup>35</sup>. The responsibility was then confirmed by the EU legislator with the establishment of OLAF, which exercises the powers conferred on the Commission under Regulation 2185/1996<sup>36</sup>.

The implementation of this Regulation is based on close two-way cooperation between OLAF and the competent national authorities<sup>37</sup>. The participation of Member States' investigative authorities is desirable because it facilitates and increases the effectiveness of checks and inspections, in particular in the event of opposition by economic operators, when binding measures of national law and possible emergency procedures may be applied. Cooperation is vital, starting with the pre-operational phase of the inspection, when the competent national authority has to be notified by OLAF of the object, purpose and legal basis of the check that OLAF intends to conduct. For that, OLAF needs to correctly identify the competent national authority and this has at times proved challenging, particularly in the field of direct expenditure.

To solve this problem Member States have communicated to OLAF — via a questionnaire — the complete contact details of national authorities for all expenditure fields, including direct expenditure<sup>38</sup>, thus enabling the OLAF investigators to identify and contact the competent authority in good time before the check. OLAF will remain in close contact with the Member States for the continuous updating of this information.

The designation of a national administrative and judicial authority with competences extended to the field of direct expenditure in all Member States is strongly recommended.

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<sup>35</sup> Regulation 2185/1996 concerning on-the-spot checks and inspections carried out by the Commission in order to protect the European Communities' financial interests against fraud and other irregularities (OJ L 292, 15.11.1996).

<sup>36</sup> Pursuant to Article 3(1) of Regulations 1073/1999 and 1074/1999 concerning investigations conducted by the European Anti-fraud Office (OLAF).

<sup>37</sup> See Article 4 of Regulation 2185/1996.

<sup>38</sup> Not all Member States have designated a central authority dealing with direct expenditure, but most of them have reported that they have an investigative service responsible for this field, with the exception of Germany, Spain and the UK.

Following the preparatory steps for the inspection, effective involvement of the national competent authorities on the ground and assistance to the OLAF investigators in the event of opposition by the economic operator are essential in order to ensure the success of the inspection. During the conduct of an on-the-spot check and in as much as EU law does not provide specific rules, OLAF inspectors are required to comply with the rules of procedure laid down by the law of the Member State concerned. It is therefore important for the Commission to better understand the national laws and practices and administrative procedures in conducting these checks and for this purpose Member States have provided information on these topics via a questionnaire. The complete answers provided by the Member States to the questionnaire are included in the staff working document<sup>39</sup> accompanying this report and represent useful background information regarding the national requirements and practices for the OLAF investigators when preparing on-the-spot checks in the Member States.

#### **4.1. National conditions for gaining access to information**

Under Article 7 of Regulation 2185/1996, Commission inspectors have access to all information and documentation on the operations concerned under the same conditions as national administrative inspectors. All Member States have reported that national legislation grants inspectors full access to information and documentation available on the operation concerned. In cases where the operator is the beneficiary of an EU grant, the obligation to provide access to documentation and information is inserted as an obligation in the grant contract<sup>40</sup> and thus constitutes an important precautionary measure. Particular conditions apply to enforcement measures such as searching or seizures, where a judicial warrant issued by a law-enforcement agency is necessary<sup>41</sup>. As a general rule, national inspectors also have access to information located elsewhere than on the economic operator's premises and they may check such premises; however, checks in private residences are not possible without a judicial warrant, in line with the European Convention on Human Rights (ECHR) and constitutional provisions<sup>42</sup> regarding fundamental rights and freedoms. Where applicable in certain Member States<sup>43</sup>, the main legal limitations in obtaining the information relevant to on-the-spot checks from documents, electronic resources or interviews mentioned were data protection requirements, banking secrecy rules and professional secrecy rules.

In order to safeguard the chain of custody and continuity of possession over the records selected during the on-the-spot checks, national inspectors may make copies of records (either on paper or electronic records), and items can be photographed and filmed. In many Member States, inspectors have the authority to seize and detain original documents pertaining to the scope of the control, in justified cases, where there is a risk that evidence may be hidden or destroyed or because it is necessary to retain the originals for further examination<sup>44</sup>.

In general, the presence of a lawyer during administrative on-the-spot checks is not provided for by national legislation. Therefore, national provisions do not allow the operator concerned by the check to delay access to information until he consults his lawyer. However, most

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<sup>39</sup> See Accompanying document 1 'Implementation of Article 325 TFEU in 2009 by the Member States'.

<sup>40</sup> LT, UK, AT.

<sup>41</sup> DE, LU.

<sup>42</sup> As especially highlighted by DE.

<sup>43</sup> BE, CZ, DE, EE, IE, EL, IT, CY, HU, PL, RO, SK, SE, UK.

<sup>44</sup> BE, IE, EL, FR, CY, HU, MT, AT, PT, RO, LU, SI, SK, FI, UK.

national legislations<sup>45</sup> recognise the lawyer-client privilege to be applicable to administrative checks, under conditions which vary from one Member State to another<sup>46</sup>. In all Member States national inspectors have access to information and documentation pertaining to the on-the-spot check and they may retain original documents or take copies of the originals. Certain limitations are imposed by the necessity of a warrant for searches and seizures.

Regarding the forensic examination of computers, OLAF has recently designed a leaflet for the information of economic operators. This document advises economic operators on their rights and details the procedure for the forensic examination of computers during OLAF's on-the-spot checks. The leaflet is of particular relevance in Member States which do not have specific legislative provisions with regard to this procedure.

As a general rule, whenever the economic operator subject to an on-the-spot check is the beneficiary of a EU grant, the grant contract should include the obligation of the economic operator to give access to information to OLAF inspectors in order to facilitate the check.

#### **4.2. National procedural requirements for on-the-spot checks and for drawing up administrative inspection reports**

Article 6(1) of Regulation 2185/1996 requires the Commission inspectors to comply, during on-the-spot checks, with the rules of procedure laid down by the law of the Member State concerned. Member States have indicated that these procedures are usually provided by manuals and instructions to the national inspectors. Among these procedural requirements, Member States have mentioned: non-notification of checks except where necessary, restrictions on access to private residences (see above), observance of the law on the use of languages<sup>47</sup>. Inspectors should produce a written authorisation or inspection order and special identification card<sup>48</sup>; the check should take place in the presence of the economic operator concerned<sup>49</sup> and during certain hours, depending on national legislation<sup>50</sup>. An inspection report must be drafted and, in certain cases, a final discussion with the liable party should take place before the report is drawn up<sup>51</sup>. Certain procedural requirements apply to the national administrative reports: in most Member States, national inspectors use a standard template and the content usually describes the irregularities noted, the legal provisions infringed and the results of the check. The report must be signed in all cases by the national inspectors conducting the check and in some cases by the economic operator. If the economic operator refuses to sign, this will be mentioned in the report. The report is usually approved by the hierarchical superior of the inspector in charge of the check. In general, Member States have indicated that there are no restrictions regarding the admissibility of administrative inspection reports in administrative or judicial proceedings. Exceptions included situations where irregularities have been committed while collecting the information contained in the report<sup>52</sup>

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<sup>45</sup> Exceptions: ES, LV, LT, PL.

<sup>46</sup> See document 'Implementation of Article 325 TFEU in 2009 by the Member States' (Accompanying document 1 to this report).

<sup>47</sup> As especially highlighted by BE.

<sup>48</sup> CY, IE.

<sup>49</sup> PL.

<sup>50</sup> PL, HU.

<sup>51</sup> SI.

<sup>52</sup> HU, BE, UK.

and where national law provides that evidence obtained during administrative procedures cannot be used in criminal proceedings<sup>53</sup>.

In order to be admissible in administrative or judicial proceedings, national administrative reports drafted following an on-the-spot check must likewise meet certain requirements, including signature by the national inspectors. It has been OLAF's experience that the signature of the report by the national inspector has on occasion been delayed or refused without giving specific reasons during joint inspections.

It is therefore essential that the national inspector participating in an OLAF on-the-spot check also signs the OLAF report without undue delay, thus avoiding the risk of it being non-admissible or having lower evidentiary value in administrative or judicial proceedings.

#### **4.3. Assistance of national authorities in the event of opposition by economic operators**

Assistance by the national authorities is important and it is not conditional on the national authority's participation in the check. The need for the support of national authorities becomes even more pressing in cases where the economic operator opposes the check by the Commission inspectors. The assistance and support of the national authorities is extremely important regardless of the type of EU expenditure concerned (direct expenditure or shared management of EU funds). The same kind of support, particularly for the safeguarding of evidence, must be made available when checks regarding direct expenditure are conducted, in order to ensure the same level of protection of EU funds for all expenditure areas.

In cases where the economic operator opposes the check, certain Member States<sup>54</sup> indicated that the Commission inspectors may enter the premises of the economic operator concerned even without his prior consent during an on-the-spot check. In cases where there is opposition by an economic operator hampering the check, Member States' competent authorities may assist Commission inspectors by issuing a judicial or administrative warrant<sup>55</sup>, or assist them if necessary — with reasonable force — to access the premises of the economic operator. In such cases of opposition by the economic operator, police or national inspectors may intervene and assist the Commission inspectors<sup>56</sup>. Other measures that Member States may take include suspending or terminating payments in the case of beneficiaries of EU grants or applying fines. In the event that the operator concerned refuses to grant access to information, the inspectors may seal the premises<sup>57</sup> and take and retain in their custody both books and other paper or electronic records, with a judicial or administrative warrant<sup>58</sup>. They may apply a formal interrogation procedure to the representatives of the economic operator<sup>59</sup>. Criminal sanctions such as fines or suspension of payments to the beneficiary of EU grants may be applied when the economic operator refuses to grant access to information.

Member States have adopted binding measures in their national law to ensure that OLAF investigators conducting on-the-spot checks can benefit from the assistance of the national

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<sup>53</sup> EE.

<sup>54</sup> BE, CZ, IT, CY, LT, MT.

<sup>55</sup> BE, BG, CZ, DE, FR, CY, LV, LU, PT, UK.

<sup>56</sup> DK, RO, PL, UK.

<sup>57</sup> BE, BG, CZ, IE, EL, ES, FR, IT, CY, LT, AT.

<sup>58</sup> BE, BG, CZ, DK, IE, EL, ES, FR, CY, LV, LT, LU, AT, SI, UK.

<sup>59</sup> CZ, IE, EL, FR, MT, ES, CY, LT, AT.



competent authorities in cases where the economic operator opposes the check. Some of these measures, such as issuing a judicial or administrative mandate, seizures of documents or interrogation procedures, give immediate results and should be favoured by national legislation.

The active participation of national authorities on the ground can contribute greatly to the success of the operation. Therefore, national inspectors should be actively involved in the inspection, rather than participating as simple observers, which some national authorities chose in some OLAF cases as declared status during on-the-spot checks. The same level of assistance to OLAF inspectors should be ensured for shared management as for direct expenditure.

#### **4.4. National precautionary measures to prevent loss or destruction of evidence**

Emergency measures such as sealing business premises and photographing or filming installations, circuits and other objects are allowed by most national legislations. Sometimes these measures can be taken only in the context of a judicial procedure<sup>60</sup>. Other precautionary measures include taking samples, with judicial authorisation, seizing documents or seeking police assistance when needed. These measures may be taken in situations where there is a threat of disappearance, concealment or modification of documents or where there are suspicions that a crime has been committed<sup>61</sup>. The reasons for taking such measures must be recorded. In most Member States there is a possibility of appeal against such measures.

#### **4.5. General conclusions**

Following this exercise it may be concluded that Member States have taken a number of measures to consolidate the implementation of Regulation 2185/1996; however, in practice, some improvements can still be made in that area, including in cooperation between OLAF and the national authorities, as outlined above.

The Commission will continue to monitor the implementation of these recommendations in future reports.

### **5. RECOVERY**

#### **5.1. Measures for securing the recovery of irregular amounts**

Member States were asked about their national provisions on the recovery of irregular amounts, with a focus on legal instruments and measures against financial loss or damage, and about the registration of irregularities and recovery of debts. In its Resolution of 24 April 2009 on the protection of the Communities' financial interests and the fight against fraud — Annual report 2007 (2008/2242(INI)) the European Parliament noted that recovery rates are still low, especially in sectors where Member States manage recoveries. The European Parliament considered that more appropriate and faster recovery procedures were needed and binding and precautionary elements should be included in future legislation concerning shared management so that irregular amounts can be recovered at the end of the recovery procedure. This way, the recovery of taxpayers' money could be more efficiently secured.

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<sup>60</sup> BE.

<sup>61</sup> DE, LV, AT, SK.

### 5.1.1. *National legislation on recovery of EU funds*

Member States' replies show that all Member States have provisions within their national legislation for securing the recovery of irregular amounts as regards the revenue and expenditure side of the EU budget in areas where no rules on recovery are laid down by EU legislation. The provisions relate to mechanisms of offsetting, precautionary enforcement, seizure and forced recovery.

Regarding expenditure, to secure the recovery of irregular payments included in contracts involving EU funds, most Member States<sup>62</sup> use legal instruments, such as different types of guarantees, promissory notes, security deposits, personal or joint sureties, offsetting, bank bonds, mortgages or insurances.

Two thirds of the Member States<sup>63</sup> are using legal instruments and measures, such as on-demand guarantees, offsetting and suspension of payments, in order to speed up the recovery of amounts irregularly paid.

The national legislation of most of the Member States<sup>64</sup> contains provisions on protective and precautionary measures that can be taken after the detection of suspected irregular amounts (revenue and expenditure). Such measures are: confiscation, administrative seizure, retention of goods subject to tax, financial penalties, suspension, refusal or adjustments of further payments, termination of the project financing and repayment of the funds paid, reduced funding.

Member States' national legislation provides the possibility (not specifically an obligation) for the national administration to stand as offended/injured party in criminal proceedings for frauds against the EU budget.

### 5.1.2. *Registration of irregularities and recovery of debts within the national administration*

Although individual errors cannot be categorically ruled out, according to the information received via the questionnaire, the Member States can in principle guarantee the completeness of the registration of irregularities.

In all Member States the recovery figures are audited on a national level after the recoveries are completed. Checks and audits are primarily made by various national authorities, such as internal audit services of the respective institutions (managing authority, certifying authority, intermediate bodies, implementing bodies), customs authorities and national audit office.

As regards EU revenues and expenditure, two thirds of the Member States<sup>65</sup> have at national level a legally regulated threshold under which there is no recovery order. This threshold varies from €3 to €100, sometimes not being uniform within the same country for all the funds used or areas concerned (agriculture, structural funds, and customs).

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<sup>62</sup> BE, BG, CZ, DK, DE, EE, IE, EL, ES, FR, IT, LV, HU, PL, PT, RO, SI, SK, FI, UK.

<sup>63</sup> BE, BG, CZ, EE, EL, ES, FR, IE, LV, LT, LU, HU, NL, AT, PL, PT, RO, SI, UK.

<sup>64</sup> BE, BG, CZ, DK, EE, IE, EL, ES, FR, IT, CY, LV, LT, HU, MT, AT, PL, PT, RO, SI, SK, UK.

<sup>65</sup> BE, DK, DE, EE, ES, FR, IT, CY, LV, LT, LU, MT, NL, AT, PL, PT, SI, SK, FI.

In some of the Member States<sup>66</sup> the recovery order is not enforceable.

Only a few Member States<sup>67</sup> would to a certain extent use the revenues forecast as a method for making a preliminary estimate of a potential irregularity amount to be recovered before the recovery actually starts. When doing so, the estimates would normally be provided within the monitoring and accounting systems used for the management of EU funds.

### 5.1.3. *Conclusions*

As regards the recovery of illegal amounts the legal instruments and measures against financial loss or damage and concerning the registration of irregularities and recovery of debts are as a matter of principle incorporated within the national legislative systems. This way the Member States show that security measures are in place, but certain improvements can still be made.

Member States' legislation should give priority to the enforceability of recovery orders, which has an important role in speeding up recovery procedures. To secure the recovery of irregular payments included in contracts involving EU funds, all Member States should provide for legal instruments, such as different types of guarantees, promissory notes, security deposits, personal or joint sureties, offsetting, bank bonds, mortgages or insurances, in the contracts.

To support speedy recovery procedures additional binding and precautionary elements should be considered for future EU legislation concerning shared management.

## 5.2. **Recovery of irregular amounts in 2009**

### 5.2.1. *Traditional 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 2009 is approximately €343 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 2009 is 44 % (approximately €152 million). This is an average starting position, although higher than last year's of 38 %. The recovery rate for all years (1989-2009) is 45.1 %.

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 2009 the Commission refused Member States' write-off requests in 61 cases totalling some €11.5 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 €9 million because they did not establish customs debts where they should have done so.

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<sup>66</sup> BG, DE, CY, MT, AT, PL, SI, SE.

<sup>67</sup> BE, CZ, AT, PT, SK.

### 5.2.2. *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 within the framework of the annual financial clearance of the EAGF and EAFRD accounts. Even after the application of this mechanism, Member States are required to pursue their recovery procedures and to credit 50% of the amounts effectively recovered to the EU 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.

Undue payments that are the result of administrative errors committed by the national authorities have to be deducted from the annual accounts of the paying agencies concerned and, thus, excluded from EU financing.

In the year 2009, the 50/50 mechanism was applied by the financial clearance decision for the financial year 2008<sup>68</sup> to all pending non-recovered cases dating from 2004 or 2000 (cases that were four or eight years old respectively). A total of €31.4 million was charged to the Member States in this way and €20.1 million was borne by the EU budget for reasons of irrecoverability. A further €0.8 million was charged to the Member States by a subsequent decision<sup>69</sup> that cleared the accounts for financial year 2008 of those paying agencies that were disjoined in April 2009.

During the financial year 2009 Member States recovered €167.3 million and the outstanding amount still to be recovered from the beneficiaries at the end of that financial year was €1 136.2 million.

The financial consequences of non-recovery for cases dating from 2005 or 2001 was determined in accordance with the 50/50 rule mentioned above by charging €22.8 million to the Member States concerned<sup>70</sup>. Moreover, €20.3 million was borne by the EU budget for cases reported irrecoverable during financial year 2009. For those paying agencies for which the 2009 accounts were disjoined from the financial clearance decision, a further €11.9 million will be charged by subsequent Commission decisions.

Due the application of the 50/50 mechanism since its introduction in 2006 the amount outstanding from the Member States towards the EU budget has been reduced to €830 million<sup>71</sup>.

During the years 2007-09 the Commission audited the correct application of the new clearance mechanism through 15 on-the-spot checks covering 14 paying agencies in 11 Member States.

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<sup>68</sup> Commission Decision 2009/367/EC (OJ L 111, 5.5.2009).

<sup>69</sup> Commission Decision 2010/56/EU (OJ L 32, 4.2.2010).

<sup>70</sup> Commission Decision 2010/258/EU (OJ L 112, 5.5.2010).

<sup>71</sup> The amount includes updated financial information provided by the Member States for the financial year 2009.

In general the Member States' authorities have adequate procedures in place to protect the financial interests of the European Union. Deficiencies found during these on-the-spot checks are being followed up in the context of conformity clearance procedures.

### 5.2.3. Cohesion policy

For the Structural Funds, recovery from the beneficiaries of amounts unduly paid owing to irregularity or suspected fraud is mainly a matter for the Member States. Member States must also deduct from a future payment claim any amount which was previously unduly claimed from the EU budget.

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 EU co-financed around 1000 programmes worth some €159 billion in total<sup>72</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 11 046 cases of irregularities (21 in 2009) with a financial impact estimated at €1.51 billion<sup>73</sup> for the EU contribution (€1.84 million for 2009).

Of these cases, 7 049 have been closed definitively at Commission level and an amount of €742 million was taken into account during final payment or decommitted after closure or reimbursed to the EU budget. Member States indicated that administrative and judicial procedures had been finalised at national level in a further 566 cases, with a financial impact of €52 million for the same period. The Commission has started reconciliation procedures with a view to closing these cases.

In 2009, the Commission adopted seven decisions on how to treat 241 cases of irregularities for which the Member States concerned asked the Commission to bear the financial consequences of the irrecoverable amounts. Three decisions concerning 217 ERDF notifications totalling €1 773 541 and four decisions concerning the ESF for a total of €1 307 85 were charged to the EU budget.

For the *2000-06 programming period*, the Member States have so far communicated 20 991 cases of irregularities (4 679 in 2009) with a financial impact of some €3.49 billion for the EU contribution (€1.12 billion for 2009).

The Member States have informed the Commission that administrative and/or judicial procedures have been finalised at national level for 10 655 of these cases and that some €1.73 billion has been recovered.

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<sup>72</sup> These are multiannual programmes. This figure does not include projects directly financed under the Structural Funds and Cohesion Fund.

<sup>73</sup> Situation according to the data in the ECR database as at 15 April 2009.

Recovery rates throughout the 2000-06 programming period are good (exceeding 50% — almost as good as for the 1994-99 programming period, which is 53%) but may be heavily influenced by the practice of excluding projects found to be irregular from the expenditure declaration to the Commission. In this way EU resources can be re-used to finance other eligible projects and the burden of recovery is shifted onto national budgets.

Member States should deploy further efforts for the recovery of irregular amounts.

At the end of 2009, the total amount of *financial corrections* concerning the 1994-99 and 2000-06 programming periods was €2 510 million (€515 million in 2009) and €5 119 million (€1 806 million in 2009) 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 that 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 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.

#### 5.2.4. *Pre-accession funds*

In 2009 amounts reported as to be recovered increased by 135%. The highest amount to be recovered comes from SAPARD (€61.6 million, out of which €41 million has to be recovered by Bulgaria). For PHARE almost €7 million needs to be recovered and for ISPA €4 million. The recovery rate decreased in comparison to 2008, reaching only 27.2% in 2009.

Analysis of the recovery rate for suspected fraud reveals a rate of only 4.6% for the whole programming period. The recovery process in cases undergoing prosecution is complex and lengthy. Administrative procedures and criminal investigation do not go hand-in-hand in most countries, a fact which influences recovery rates.

As recovery rates are low, safeguard measures should be implemented for suspected fraud cases (in the form of seizure of assets, suspension of payments, bank guarantees, etc. — see point 5.1.3. above) to make sure that recovery can still take place after the final court ruling. The Member States concerned should pay special attention to the recovery of pre-accession funds.

#### 5.2.5. *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 EU 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 2009, full or partial recovery has already been announced in 478 reported cases. The Commission has recovered €15.5 million. In 463 cases the full irregular amount has been recovered. An amount of €12 million still remains to be recovered, concerning 242 cases.

The Commission will continue procedures for the full recovery of these amounts.
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#### 5.2.6. *Recovery following an OLAF case*

Where the final report on an OLAF case concludes that certain amounts have probably been paid to a beneficiary against the rules or that amounts 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 monitors the course of these recovery proceedings.

In 2009, OLAF formally closed the financial follow-up procedure for more than €249.2 million. In total €137.2 million was recovered in the agricultural sector and €49.1 million in the field of structural funds.

OLAF will continue to work together with the authorising Directorates-General within the Commission responsible for the budget sectors concerned to further improve recovery following OLAF cases.
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