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**Prevention of fraud by building on operational results:
a dynamic approach to fraud-proofing**

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Achievements of the fraud-proofing mechanism set up under the Commission communication on fraud proofing of legislation and contract management adopted on 7 November 2001

1. INTRODUCTION

This document sets out the achievements of the procedure established by the Commission communication on fraud proofing of legislation and contract management¹ and the main results for the period 2001-2006.

Those results contributed to meeting the obligations laid down in Article 280 of the Treaty², notably that of adopting preventive measures to deter fraud.

All departments and institutions have contributed to this common effort, either directly or through close cooperation with both the European Anti-Fraud Office (OLAF) and control bodies.

The process set out in the communication is being replaced by a new fraud prevention method based on OLAF's investigative activities. However, it will remain available for two specific purposes: (a) assessing the fraud risks of legislative proposals upon request and (b) drafting standard procurement contracts and grant agreements.

2. FRAUD PROOFING ACHIEVEMENTS

2.1. Legislation

Since the adoption of the 2001 communication, OLAF has shortlisted the most vulnerable legislative proposals for fraud proofing (approximately 15-20 proposals per annual legislative exercise). The legislative proposals were selected from those included in the Commission's work programme and the necessary analysis was carried out by specialised OLAF departments.

The inter-departmental group of representatives (fraud proofing correspondents) was useful in selecting the initiatives to be fraud-proofed, raising awareness of the importance of prevention and the fraud proofing dimension and building a network of correspondents with OLAF.

OLAF was closely consulted on the revision of the Financial Regulations governing the execution of the EU's budget, the cornerstone of the Communities' financial rules.

The current Financial Regulation applicable to the general budget of the European Communities³, (Financial Regulation) and its Implementing Rules⁴, have been

¹ Commission communication concerning the fraud proofing of legislation and contract management, SEC(2001) 2029, 07.11.2001 — not published in the OJ.

² Treaty establishing the European Community (consolidated version), OJ C 325, 24.12.2002.

³ Council Regulation (EC, Euratom) N° 1605/2002 of 25 June 2002 on the Financial Regulation applicable to the general budget of the European Communities (OJ L 248, 16.9.2002, p.1), as last amended by Council Regulation (EC, Euratom) N° 1995/2006 of 13 December 2006 (OJ L 390, 30.12.2006, p.1)

⁴ Commission Regulation (EC, Euratom) N° 2342/2002 of 23 December 2002 laying down detailed rules for the implementation of Council Regulation (EC, Euratom) N° 1605/2002 on the Financial Regulation applicable to the general budget of the European Communities (OJ L 357, 31.12.2002, p.1), as last

applicable since 1 January 2003 and constitute one of the key products of the White Paper on reform. This legal framework was successively revised in 2005, 2006 and 2007, in order to reflect the adoption of the public procurement directive⁵ and to promote simplification of financial procedures and sound financial management⁶.

OLAF was involved in drafting basic acts⁷ (and implementing rules) such as those adopted for cohesion policy under the new financial perspectives (2007-2013).

Standard clauses to protect the EU's financial interests were included in basic acts in adopting the current financial perspectives for the period 2007-2013. The legal bases for European operational policies offer improved preventive protection:

by ensuring the adoption of preventive measures (by the Commission and/or delegated entities for the management of funds) and effective controls — thus, when irregularities are detected, there is due provision for recovering unduly paid funds and applying effective, proportionate, and dissuasive penalties;

by ensuring, on the one hand, that the Commission (or its representatives) and the European Court of Auditors are entitled to perform audits of the projects and, on the other hand, that OLAF is entitled to conduct investigations in accordance with the applicable legislative framework⁸;

by clarifying the notion of irregularity with regard to Community expenditure under centralised⁹ or shared management¹⁰.

Standard anti-fraud provisions were drafted by OLAF in cooperation with the lead Commission departments for the following texts:

- (1) preferential trade and customs cooperation agreements with third countries (as and where appropriate provisions on mutual administrative assistance and special administrative cooperation are included in these agreements, thereby providing a legal basis for, *inter alia*, the exchange of information between the non-member authorities and the Commission/Member States, Community

amended by Commission Regulation (EC, Euratom) N° 478/2007 of 23 April 2007 (OJ L 111, 28.4.2007, p.13).

⁵ Directive 2004/18/EC of 31/03/2004 on the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts, OJ L 134, 30.04.2004, p. 114.

⁶ E.g. in order to help fight corruption and fraud, the IRs now provide that, where substantial errors, irregularities or fraud are attributable to the contractor, all the contracts concluded with that contractor can be terminated.

⁷ Council Decisions or Regulations governing the general framework for financing European specific policies.

⁸ Regulation (EC) No 1073/1999 of the European Parliament and of the Council of 25 May 1999 concerning investigations conducted by the European Anti-Fraud Office (OLAF), OJ L 136, 31.5.1999.

⁹ Any infringement of a provision of Community law, including infringements of a contractual obligation resulting from an act or omission by an economic operator, which has, or would have, the effect of prejudicing the general budget of the EU or budget managed by it, falls within the scope of the relevant anti-fraud regulations.

¹⁰ Commission Regulation (EC) No 2035/2005 of 12 December 2005 amending 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 (OJ L 328, 15.12.2005), and the corresponding Regulation (EC) No 1831/94 concerning irregularities with regard to the Cohesion Fund, as amended by Regulation (EC) No 2168/2005, Regulation (EC) No 1083/2006, Article 2(7), for the Structural Funds and Cohesion Fund for the period 2007-13, and Regulation (EC) No 1198/2006, Article 3(q), for the European Fisheries Fund for the period 2007-13.

on-the-spot checks and certain safeguard procedures in the event of failure to provide administrative cooperation);

- (2) financial regulations applicable to the Common Agricultural Policy (CAP);
- (3) standard agreements for the participation of candidate countries and non-member countries in Community programmes (including specific annexes laying down detailed rules on financial control, investigation, preventive measures, recovery and sanctions);
- (4) standard financial agreements with candidate countries, accession countries and/or non-member countries benefiting from Community external aid programmes;
- (5) Commission decisions setting up and delegating tasks to executive agencies;
- (6) Council decisions setting up Community bodies (notably regulatory agencies).

Fraud prevention received greater attention in major areas of the EU budget. This was made possible thanks to OLAF intervention in the law making process.

2.2. Procurement contracts and grant agreements

The Directorate-General for the Budget operates a standard contracts policy in the Commission, for both public procurement and grant procedures. This role entails direct links and close cooperation with OLAF, which have proven productive, flexible and efficient.

The Commission adopted the following contract models¹¹ in 2003 and 2004:

- (a) For procurement: direct service contract, framework service contract, direct supply contract, framework supply contract, order form, purchase order for low-value contracts, and general terms and conditions for low-value contracts. These models were revised in line with revisions of the legal framework.
- (b) For grants: grant agreement for an action, operating grant agreement, framework partnership agreement, specific grant agreement for an action, and specific operating grant agreement. DG Budget elaborated in 2005 and 2006 three other standard grant agreements, derived from the standard grant agreement for an action: a grant agreement for an action with multiple beneficiaries, a grant agreement for mixed financing and a grant agreement for financing using flat-rate. Those models were revised according to the afore-mentioned revisions of the legal framework. A standard grant decision will be available by the end of 2007.

The Financial Regulation adopted in 2002 provided for a database for legal entities which are in an exclusion situation. The Commission created such a database in the framework of its Early Warning System¹², which contains warnings concerning entities in exclusion situations and entities presenting potential financial risks. The

¹¹ Communications on model contracts adopted by the Commission by decision C(2003)5144 of 23/12/2003 and by decision C(2004)2814 of 23/07/2004.

¹² Commission Decision on the Early Warning System (EWS) C(2004) 193/3 of 3 February 2004, as last amended by Commission Decision C/2007/433 of 21 February 2007.

Commission ensures a monthly exchange of information on entities in exclusion situations between the EU Institutions and agencies. Pursuant to the revision of the Financial Regulation adopted in 2006, information on contractors and grant beneficiaries who are in situations of exclusion from Community budget financing¹³ will be shared with all entities involved in managing EU money, including the Member States, with effect from 1 January 2009 at the latest.

The Commission put in place new rules based upon the International Public Sector Accounting Standards (IPSAS) and the International Financial Reporting Standards (IFRS) in 2005. The objective pursued was to increase financial transparency and accountability towards users, audit and control bodies, and citizens and to insure completeness and accuracy of the balance sheet, offering a precise view on assets and liabilities.

3. CONCLUSION

The objectives of the fraud proofing procedure have been reached. The most sensitive pieces of legislation have been subject to the procedure. A set of model contracts and agreements has been adopted at central or departmental level. The fraud-proofing process has contributed to improving the prevention of fraud, corruption, irregularities and other illegal activities both in legislation and contracts.

¹³ Article 93(1) of the Financial Regulation defines the situations under which tenderers or grant applicants should be excluded from procurement and grant procedures.