

EN

EN

EN



COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 22.7.2008  
COM(2008) 475 final

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

**Protection of the Communities' financial interests – Fight against fraud – Annual report  
2007  
[SEC(2008) 2300]  
[SEC(2008) 2301]**

## CONTENTS

Introduction .....	4
1. Results of the fight against fraud: statistics on fraud and other irregularities.....	5
1.1. Statistics on fraud and other irregularities reported by the Member States and Commission departments in 2007 .....	5
1.1.1. Traditional own resources .....	8
1.1.2. Agricultural expenditure (EAGGF and EAFRD) .....	8
1.1.3. Structural measures .....	9
1.1.4. Pre-accession funds .....	10
1.1.5. Statistics on expenditure directly managed by the Commission.....	5
1.2. Statistics on OLAF's activities .....	11
2. Major developments in 2007.....	12
2.1. Progress in the customs field .....	12
2.1.1. Mutual assistance under the first pillar .....	12
2.1.2. Conventions under the third pillar and specific national measures.....	13
2.2. Efforts to combat the smuggling and counterfeiting of cigarettes .....	14
2.3. Irregularities and suspected fraud in the area of “direct expenditure” .....	15
2.4. The new approach to fraud proofing.....	15
2.5. Protection of the euro against counterfeiting .....	16
2.6. The Hercule II programme.....	16
2.7. Other measures taken in 2007 to protect the Community's financial interests .....	17
3. Checks to identify fraud and other irregularities.....	18
3.1. Checks concerning the Structural Funds.....	19
3.1.1. Improvement of the control framework .....	19
3.1.2. Management checks by the Member States in the area of the ERDF .....	20
3.2. The framework for checks in the agricultural sector .....	21
3.3. Control of traditional own resources.....	23
3.4. On-the-spot checks and inspections under Regulation (Euratom, EC) No 2185/96..	24
4. The limitation period applicable to proceedings and decisions concerning irregularities .....	25
4.1. Limitation period for proceedings concerning irregularities .....	25

4.2.	Limitation period for implementing the decision establishing an administrative penalty .....	26
4.3.	Limitation period for implementing the decision establishing an administrative measure (recovery).....	26
5.	Recovery .....	26
5.1.	Agriculture .....	27
5.2.	Structural Funds .....	28
5.3.	Own resources.....	29
5.4.	Direct expenditure.....	29
5.5.	Recovery following an OLAF case.....	29

## INTRODUCTION

Protection of the Communities' financial interests and the fight against fraud are areas in which responsibility is shared between the Community 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 280 of the EC Treaty. The report is sent to the European Parliament and the Council and is published.<sup>1</sup>

The **first part** of the report gives a **summary of the statistics concerning irregularities** reported by the Member States in those areas where the Member States implement the budget (agricultural policy, Structural Funds and pre-accession funds, i.e. approximately 80% of the budget) and for the collection of the Community's own resources. It also gives an estimate of the irregularities that occurred 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 3 and 5.

By their very nature, the figures set out in this report are indicative, preliminary and non-final. As a precaution, the amounts indicated often cover the whole of the action concerned, before the irregular part has been established precisely. Although the Member States are under an obligation to report irregularities, they do so with different degrees of compliance. It is also the Member States that identify in principle from among the reported irregularities those which they see as being suspected fraud. And only at the end of legal proceedings conducted by the national authorities, often after a considerable time lag, is it established whether or not fraud is involved and what the real financial impact of the fraud is. When it comes to finally classifying a case as fraud or not, the Commission depends for its information on the Member States (which may or may not be forthcoming with it).

The **second part** of the report sets out the **main developments of 2007** at the level of fraud prevention and repression and in the area of other irregularities.

The **third part** concerns **checks to detect fraud and other irregularities**, with a large section being devoted to checks in the field of the Structural Funds and in particular management checks. The **fourth part** discusses the limitation period for proceedings concerning irregularities and the limitation applicable to the implementation of a decision establishing an administrative measure or penalty. These two parts are based on Member States' replies to a questionnaire.

The **fifth part**, for which the same kinds of reservation apply as for part 1, deals with recoveries made in 2007 in all budget areas.

---

<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)

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

## **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 2007**

In the fields where the 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. The information thus collected is used for analysis and monitoring purposes. It provides a better insight into the impact of irregularities on the Community budget.

It is important to distinguish between fraud and other irregularities. 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 among the irregularities reported those which 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 for the first time includes statistics on fraud and other irregularities detected by Commission departments in the areas of the budget under centralised direct management.

#### *Conclusions concerning the irregularities reported by the Member States*

- The number of irregularities reported has decreased in every area apart from that of structural measures.
- The estimated financial impact of the irregularities has increased in every sector. As regards own resources and agriculture, the increase relates in part to irregularities occurring or discovered in previous years but reported only in 2007. In the area of expenditure, the accession of new Member States and the recent increase in payments in those countries goes some way towards explaining the increase. In budget percentage terms, the financial impact remains fairly stable. A number of irregularities with a financial impact estimated to be heavy have been detected in the context of the closure of the programming period of the pre-accession funds for the 10 new Member States.
- The estimated impact of the cases with suspected fraud remains stable for expenditure and shows a slight decrease for own resources. It should again be

---

<sup>2</sup> SEC(2008) 2300 and SEC(2008) 2301.

<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> SEC(2008) 2301.

made clear that what is involved here is reported suspicions of fraud and not cases confirmed by the courts, and that the real financial impact, after recovery and financial correction, can be known only at the end of the legal and administrative proceedings.

- Although most irregularities are reported to the Commission within the time limits provided for, there is room for improvement here: the average time lapse for notifications in the agricultural sector is 1.2 years, while in the area of structural measures it is 0.9 years. Some Member States often notify their irregularities well after the event. Speedy notification is essential if there is to be an effective follow-up.
- The proportion of Member States which notify irregularities electronically, and in particular with the AFIS/ECR<sup>6</sup> electronic modules proposed by the Commission for the agricultural and structural fund sectors, is increasing. Use of the modules simplifies the processing of data and improves their quality and comparability. Some Member States still notify irregularities on paper or make use of electronic means other than AFIS/ECR.
- Thanks to the efforts of national authorities (briefing and training of staff responsible for reporting) and the increased use of ECR modules, the quality of notifications has steadily improved in all sectors, allowing a better follow-up and easing the strategic analysis of data. Further efforts have still to be made by several Member States, notably in relation to classifying the different types of irregularity.

---

<sup>6</sup> Anti Fraud Information System/External Communications Registry.

Table 1: Number of irregularities and amounts – 2007

Area	Number of irregularities reported		Total estimated financial impact of irregularities, including suspected fraud (€ million)		Estimated financial impact of suspected fraud only (€million)	
	2006 <sup>7</sup>	2007	2006	2007	2006	2007
<b>Agriculture (EAGGF Guarantee Section)</b>	3 249	1 548	87	155	29.8 (~0.06% of allocations)	44.8 (~0.1% of allocations)
<b>Structural Funds and Cohesion Fund</b>	3 216	3 832	703	828	157.56 (~0.41% of allocations)	141 (~0.31% of allocations)
<b>Pre-accession funds</b>	395	332	14	32	1.57 (~0.03% of allocations)	5 (~0.38% of allocations)
<b>Direct expenditure</b>	-	411	-	33	-	18.1 (~0.17% of allocations <sup>8</sup> )
<b>Total expenditure</b>	6 860	6 123	804	1 048	188.93 (~0.2% of the expenditure in the four areas)	208.9 (~0.22% of the expenditure in the four areas)
<b>Own resources<sup>9</sup></b>	5 705	5 321	353	377	134.39 (~0.94% of the total amount of own resources)	106.57 (~0.62% of the total amount of own resources <sup>10</sup> )

<sup>7</sup> The figures have been updated for certain sectors since the 2006 report.

<sup>8</sup> The calculation covers the entire 2000-06 financial perspectives period.

<sup>9</sup> Customs duties and agricultural levies.

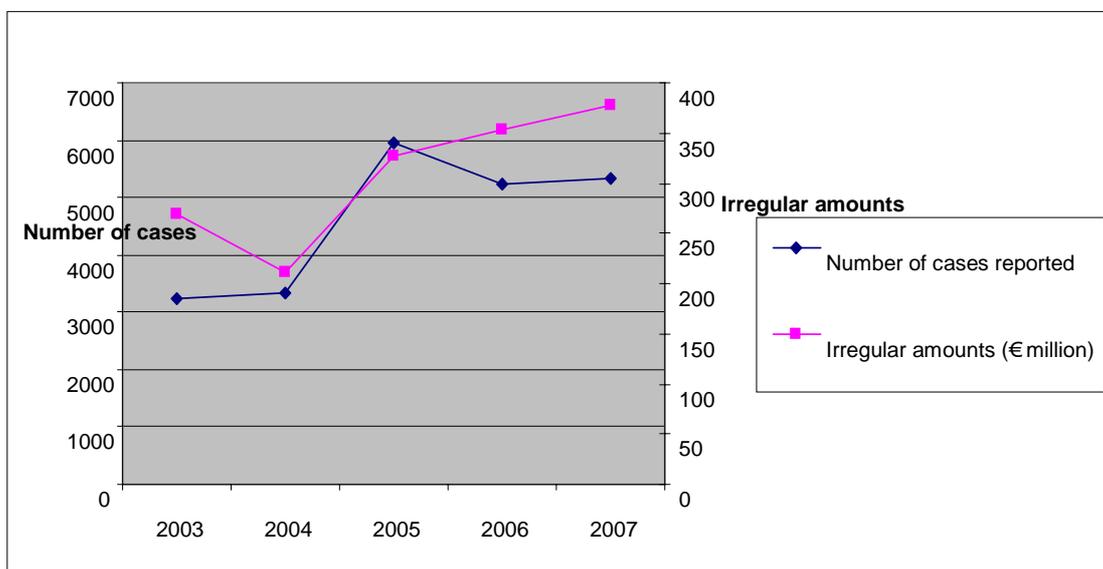
<sup>10</sup> This percentage is calculated on the basis of an estimate of traditional own resources in the 2007 general budget, and not on the basis of accounts.

### 1.1.1. Traditional own resources

The number of cases of irregularities reported was down 7% (5 321 cases in 2007, compared with 5 705 in 2006). The estimated amount involved (€377 million) rose by over 6%. Suspected fraud accounted for approximately 23% of the cases of irregularities reported, with an estimated financial impact of €106.57 million, equivalent to approximately 0.62% of the total amount of own resources in 2007 (compared with €134.39 million, or around 0.94%, in 2006). It should again be made clear that what is involved here is reported suspicions of fraud and not cases confirmed by the courts, and that the real financial impact has not yet been established.

The goods most affected were, as in previous years, electronic and multimedia products, especially TVs and monitors. The most frequent irregularities were incorrect product classification and misdescription of origin. The second most affected product was tobacco. The Commission continues to pay particular attention to these sectors. Vegetables (in particular garlic) increased in importance, as did footwear, car and motor cycle parts and clothing, whereas meat, articles of iron and steel and cereals declined in importance. However, it must be borne in mind when analysing the figures that the date on which a fraud or irregularity is discovered and notified to the Commission is not necessarily the date on which it occurred.

*Graph 1: Number of irregularities reported and estimated financial impact - traditional own resources – 2003-07*



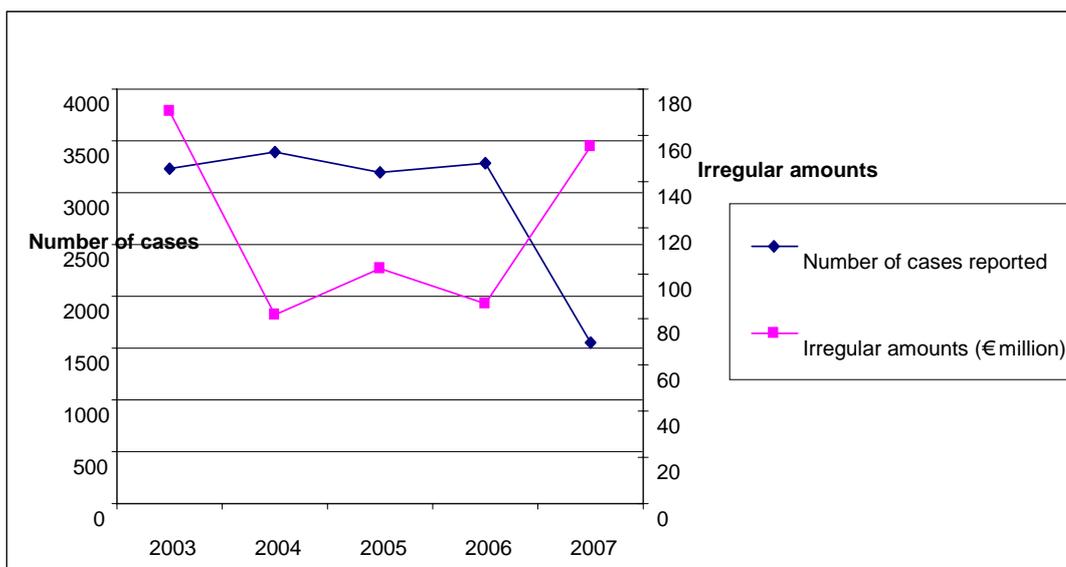
### 1.1.2. Agricultural expenditure (EAGGF and EAFRD)

The number of irregularities reported was down 53% (1 548 cases, compared with 3 294 in 2006). This sharp decrease was foreseeable and is due to the application as

from 1 January 2007 of a new Commission Regulation<sup>11</sup> which raised from €4 000 to €10 000 the threshold above which Member States are required to report irregularities to the Commission. The amount involved (€155 million, or approximately 0.33% of total appropriations for the agricultural sector) was up 44%. The increase relates in part to cases with a significant financial impact which arose or were discovered in previous years but were reported only in 2007. Suspected fraud accounted for around 10% of the cases of irregularities reported, with an estimated financial impact of €44.8 million, or 0.1% of total appropriations, in 2007 (compared with €29.8 million, or around 0.06% of total appropriations, in 2006). It should again be made clear that what is involved here is reported suspicions of fraud and not cases confirmed by the courts, and that the real financial impact has not yet been established.

The highest amounts related to milk and milk products, fruit and vegetables, sugar and rural development. These four sectors together account for about 77% of the total amount affected by irregularities.

*Graph 2: Number of irregularities reported and estimated financial impact - agricultural expenditure - 2003-07*



### 1.1.3. Structural measures

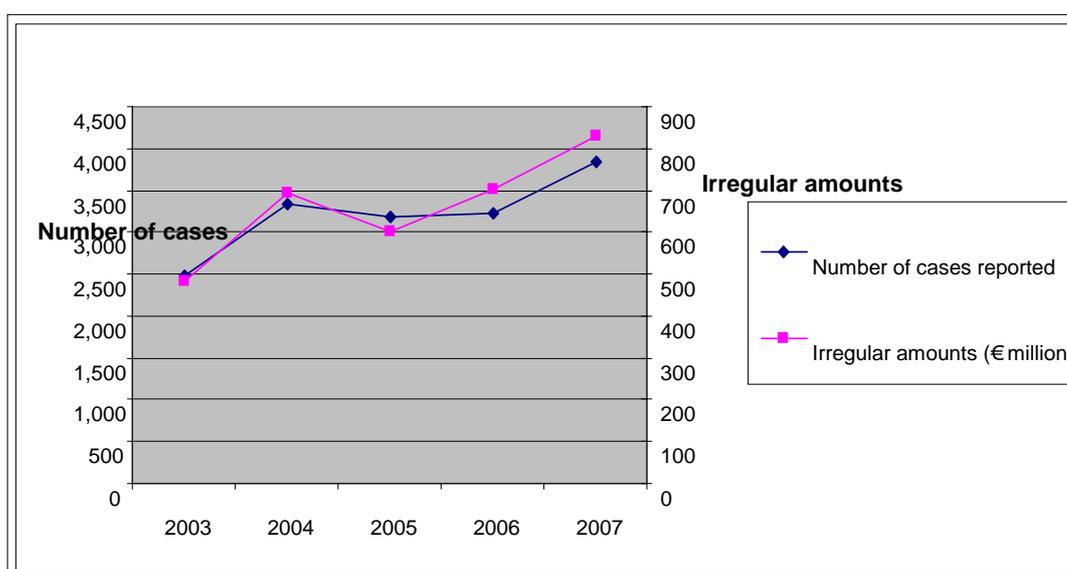
The number of irregularities reported concerning the Structural Funds and the Cohesion Fund was up 19.2% (3 832 cases, compared with 3 216 in 2006). Their

<sup>11</sup> Regulation (EC) No 1848/2006 of 14 December 2006 concerning irregularities and the recovery of sums wrongly paid in connection with the financing of the common agricultural policy and the organisation of an information system in this field and repealing Council Regulation (EEC) No 595/91 (OJ L 355, 15.12.2006).

estimated financial impact (€28 million, or around 1.83% of commitment appropriations) was up 17.7%. Suspected fraud accounted for approximately 12.4% of the cases of irregularities reported, with a financial impact estimated at €41 million, or around 0.31% of total commitment appropriations (compared with €57.56 million, or 0.41%, in 2006). It should again be made clear that what is involved here is reported suspicions of fraud and not cases confirmed by the courts, and that the real financial impact has not yet been established.

As in previous years, the ERDF<sup>12</sup> and the ESF<sup>13</sup> accounted for most irregularities (around 83%). 76% of irregularities affected projects or operations implemented in Objective 1 and 2 regions.

*Graph 3: Number of irregularities reported and estimated financial impact - structural measures - 2003-07*



#### 1.1.4. Pre-accession funds

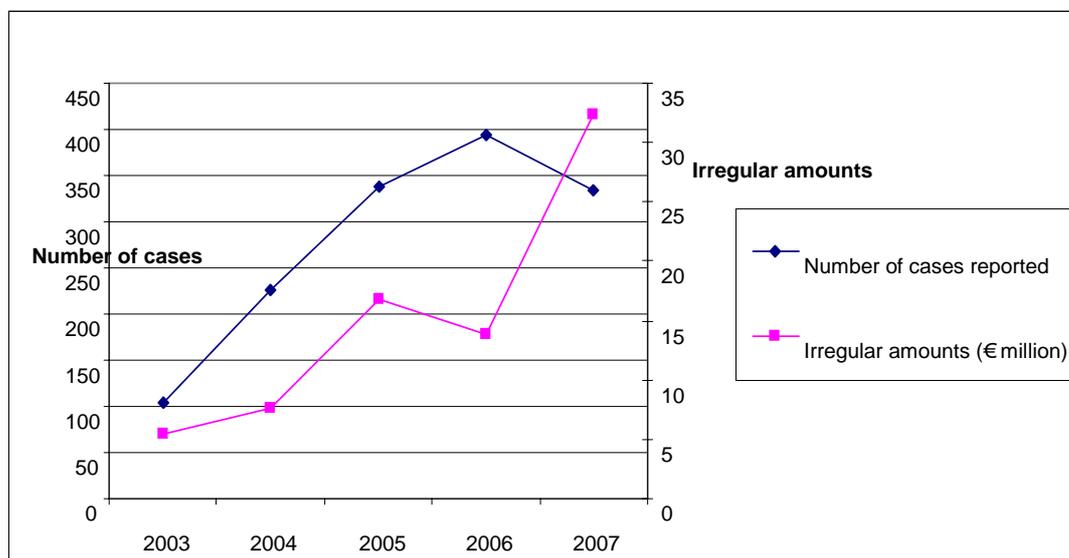
The number of irregularities reported concerning the PHARE, SAPARD and ISPA Funds decreased by 13% (332, compared with 395 in 2006). The presumed financial impact increased from €14 million in 2006 to €32 million in 2007 (approximately 1.92% of the total eligible amount). Suspected fraud accounted for approximately 15.5% of the irregular amounts reported in 2007, with a financial impact estimated at €5 million, or around 0.38% 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, and that the real financial impact has not yet been established.

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

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

The most frequently reported type of irregularity for each of the pre-accession funds was “non-eligible expenditure”.

*Graph 4: Number of irregularities reported and estimated financial impact - pre-accession funds – 2003-07*



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

This is a first step towards integrating the areas of the budget directly managed by the Commission into this report. As the system for classifying suspected cases of irregularity and fraud was set up in 2008 (see point 2.3), it has been necessary to limit the scope of the analysis for 2007. The data presented should therefore be treated with extreme caution and not as empirical evidence of the level of fraud and irregularity.

The presumed number of irregularities in this area came to 411, with a presumed financial impact of €3 million, €18.1 million of which was accounted for by 136 reported cases of suspected fraud. The irregular amount notified in the sector of external actions was €19.1 million and in the area of internal policies €3.9 million. As far as the 2000-06 financial framework is concerned, the estimated financial impact of possible fraud cases amounts to 0.17% of the total value of the contracts concluded directly by the Commission.

## 1.2. Statistics on OLAF's activities

Following a preliminary evaluation of the information received, OLAF can decide to open one of four types of case: an internal investigation, an external investigation, a coordination case or a criminal assistance case. The number of cases opened each year is stable (210 in 2007, against 194 in 2006 and 216 in 2005). Since 2004, the number of investigations opened by OLAF on its own initiative (internal and external investigations) has equalled then exceeded the number of cases 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 fallen (408 at the end of 2007, compared with 431 at the end of 2006 and 452 at the end of 2005), owing in large measure to efforts by OLAF to deal with the backlog of old cases.

*Table 2: Cases ongoing as at 31 December 2007 by sector, and their financial impact*

Sector	Cases pending at 31 December 2007	Estimated financial impact (€million)
Customs/VAT	76	781.3
Agriculture	50	108.8
Structural Funds	48	172.4
Direct expenditure	140	206.7
Internal investigations	94	289.6
<b>Total</b>	<b>408</b>	<b>1 558.8</b>

For more details and a comparison with previous years, see the OLAF report.<sup>14</sup>

## 2. MAJOR DEVELOPMENTS IN 2007

### 2.1. Progress in the customs field

#### 2.1.1. Mutual assistance under the first pillar

In response to a proposal from the Commission,<sup>15</sup> the Council amended the Regulation on the monitoring carried out at the time of export of agricultural products<sup>16</sup> so that Member States applying risk analysis in conformity with Community law can choose to apply the minimum checking rate at national level

<sup>14</sup> [http://ec.europa.eu/comm/anti\\_fraud/reports/index\\_en.html](http://ec.europa.eu/comm/anti_fraud/reports/index_en.html)

<sup>15</sup> COM(2007) 489.

<sup>16</sup> Council Regulation (EC) No 14/2008 amending Regulation (EEC) No 386/90 (OJ L 8, 11.1.2008).

rather than at the level of the customs office of export, in order to achieve a better spread of checks among national customs authorities.

The Regulation of the Parliament and of the Council on controls of cash entering or leaving the Community<sup>17</sup> came into force in June 2007. This Regulation refers to the provisions of Regulation (EC) No 515/97<sup>18</sup> on mutual assistance and stipulates that information must be sent to the Commission where there are indications that sums of cash are related to the proceeds of fraud or any other illegal activity adversely affecting the financial interests of the Community.

The Commission proposal<sup>19</sup> for the amendment of the Regulation on mutual assistance in customs and agricultural matters<sup>20</sup> moved through the legislative process in 2007. The European Parliament approved it at first reading in February 2008, with certain amendments. The instrument lays down the legal framework for the European Customs Files Identification Database (FIDE) and makes provision for the creation of a European data directory. The FIDE should enable national and Community (OLAF) operational bodies to identify departments which investigated the same person(s) or enterprise(s). The aim of the directory is to collect, for analysis purposes, data commonly used in international trade.<sup>21</sup> The proposal is due to be finally adopted sometime in 2008.

Two proposals<sup>22</sup> arising from the Lisbon Strategy are aimed at modernising customs procedures. With the entry into force of the new Customs Code, use of electronic declarations will gradually become the norm and under the e-customs project data from national customs IT systems will become increasingly compatible thanks to a central platform. These reforms will reduce costs, ensure that data can be accessed more quickly and make it possible to carry out risk assessments at European level.

### 2.1.2. *Conventions under the third pillar and specific national measures*

In 2007 Malta signed the Convention on mutual assistance and cooperation between customs administrations (“Naples II”).<sup>23</sup> The Convention has been ratified and is in force in all Member States except Italy, but it is already applicable between 22 Member States.<sup>24</sup>

Malta has ratified the Convention on the use of information technology for customs purposes.<sup>25</sup> The Convention, which creates a Customs Information System (CIS) and came into force at the end of 2005, has now been ratified by all the Member States.

---

<sup>17</sup> Regulation (EC) No 1889/2005 (OJ L 309, 25.11.2005).

<sup>18</sup> OJ L 82, 22.3.1997.

<sup>19</sup> COM(2006) 866.

<sup>20</sup> Regulation (EC) No 515/97, referred to above.

<sup>21</sup> For example, the movement of containers.

<sup>22</sup> These proposals were adopted in 2008: 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), and Decision No 70/2008/EC of the European Parliament and of the Council of 15 January 2008 on a paperless environment for customs and trade (OJ L 23, 26.1.2008).

<sup>23</sup> Convention of 18 December 1997 (OJ C 24, 23.1.1998).

<sup>24</sup> In accordance with the declarations provided for in Article 32(4) of the Convention.

<sup>25</sup> Convention of 26 July 1995 (OJ C 316, 27.11.1995).

After being ratified by Sweden and Finland, the Protocol amending the Convention on the use of information technology for customs purposes<sup>26</sup> came into force. Latvia acceded to the Protocol in 2007.<sup>27</sup> The Protocol creates the FIDE (referred to above).

Romania and Bulgaria acceded to the above-mentioned two Conventions and Protocol when they joined the EU.<sup>28</sup>

Belgium has signed bilateral agreements with several third countries. The definition of smuggling has been modified and clarified in the Hungarian Criminal Code. Finland reported on a major reorganisation of its customs authority which targets better risk management. In Ireland a new computerised system has been put in place with the same objective.

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

In 2004 the European Community and 10 Member States<sup>29</sup> concluded a cooperation agreement with Philip Morris International (PMI). During the period between the signing of the agreement and the end of 2007, PMI paid almost USD 575 million (approximately €364.5 million). Since that time, 16 Member States<sup>30</sup> have signed the agreement, which provides for the payment of approximately USD 1 250 million over a 12-year period for possible use in combating the smuggling and counterfeiting of cigarettes.

In December 2007 the European Commission and 26 Member States<sup>31</sup> signed a cooperation agreement with Japan Tobacco International (JTI). The agreement, which runs for 15 years, makes provision for the payment of USD 400 million (approximately €253.6 million), which may be used to combat the smuggling and counterfeiting of cigarettes.

One of the key features of the two agreements is the establishment of a mechanism to prevent the smuggling of PMI and JTI cigarettes in the long term on the European market. In cooperation with OLAF and the Member States, the agreements provide for procedures to monitor and trace products in order to determine the point at which real cigarettes (of the PMI and JTI brand) are diverted from the legal supply chain and fall into the hands of smugglers.

In 2007 the new strand of the Hercule II programme on combating the smuggling and counterfeiting of cigarettes (see point 2.6) provided for the co-financing by the Community budget of scanning equipment used to detect smuggled cigarettes, for a total estimated amount of more than €5 million. The programme also continues to provide funding for training courses, the purchase of specialist technical equipment and technical support for the monitoring of illegal activity in this area.

---

<sup>26</sup> Protocol of 8 May 2003 (OJ C 139 of 13.6.2003).

<sup>27</sup> UK and MT ratified the Protocol on 15 January 2008. AT, BE, EL, IT, IE and PT have not ratified it.

<sup>28</sup> Council Decision 2008/39/JHA of 6 December 2007 (OJ L 9, 12.1.2008) and Council Decision 2007/764/EC of 8 November 2007 (OJ L 307, 24.11.2007).

<sup>29</sup> BE, DE, EL, ES, FR, IT, LU, NL, PT and FI.

<sup>30</sup> UK is not a party to this agreement.

<sup>31</sup> UK is not a party to this agreement.

The Commission (OLAF and SANCO) actively participated in preparations for the negotiations on a protocol to the WHO Framework Convention on Tobacco Control,<sup>32</sup> dealing specifically with the efforts to combat the illicit trade in tobacco products. An OLAF official has been elected Chairman of the Intergovernmental Negotiating Body which is negotiating the Protocol.

### **2.3. Irregularities and suspected fraud in the area of “direct expenditure”**

Until this year data on detected irregularities and suspected fraud and the corrections made were collected only in the case of shared management expenditure. To remedy this situation and to improve reporting on irregularities and suspected fraud within the framework of this report, the Commission’s departments are henceforth going to enter in the Commission’s accounting system, ABAC, more information about the findings and corrections made.

In order to provide an initial analysis already this year, the Commission’s departments have identified cases of detected irregularities and suspected fraud in those areas of the budget that are subject to the centralised direct management mode.

### **2.4. The new approach to fraud proofing**

In 2001 the Commission decided<sup>33</sup> to put in place a fraud-proofing mechanism to make legislation and the management of contracts more “resistant” to fraud. Since 2002, new legislative initiatives and new legal bases of Community financing (such as standard contracts) which specifically seek to protect the financial interests of the Community have been identified jointly with the other departments and services and have been identified and examined as to their resistance to fraud and improved whenever necessary.<sup>34</sup>

In December 2007 the Commission took another step forward by introducing a new approach to fraud-proofing,<sup>35</sup> the cornerstone of which involves exploiting the results of investigations conducted by OLAF. This operational experience will be used on a more structured and adequate basis and shared more effectively with the other Commission departments and with other EU bodies and institutions. The purpose of this new approach is to identify shortcomings not only in legislative proposals but also in the implementation of EU legislation and in management and control systems.

The new policy, which will apply initially to direct expenditure, will improve fraud prevention by using all the information available (results of investigations, audits, analyses, etc.).

---

<sup>32</sup> Document OMS WHA 56.1 of 21 May 2003, entered into force on 27 February 2005.

<sup>33</sup> Communication from the Commission SEC(2001) 2029 final.

<sup>34</sup> The results of implementing the fraud-proofing mechanism for the period 2002-07 were the subject of a detailed report (SEC(2007) 1676 final).

<sup>35</sup> COM(2007) 806 final.

## 2.5. Protection of the euro against counterfeiting

A proposal for a Council Regulation<sup>36</sup> is aimed at improving protection against counterfeiting by introducing an obligation for the institutions concerned to check the authenticity of coins and notes before they are put back into circulation. The proposal also aims to authorise the transfer of counterfeit money between the national authorities and the EU institutions and bodies so that the authenticity of money can be checked.

In a report, the Commission took stock of the criminal penalties and other sanctions against counterfeiting adopted by the Member States,<sup>37</sup> following the framework decision adopted by the Council in 2000.<sup>38</sup> The measures introduced would generally appear to be as effective and efficient as they are required to be under the framework decision, given that the requisite charges and penalties have, for the most part, been incorporated into the legislation of the Member States.

At operational level, the Commission has continued, through the measures taken under the Pericles Programme,<sup>39</sup> to promote cooperation between the national, European and international authorities responsible for combating the counterfeiting of the euro. More than 80% of the 2007 Pericles budget having been implemented, twelve projects have been launched, of which seven proposed by the Member States and five by the Commission (OLAF).

Most of these projects, designed for experts in the Member States and candidate countries, were training-related (organisation of training sessions and activities to familiarise participants with counterfeit detection techniques, etc.). Pericles also contributed to two large-scale seminars bringing together representatives from the Member States, Latin America and the Caribbean for the purpose of strengthening cooperation with third countries on combating euro counterfeiting.

In 2007 approximately 211 000 euro coins were withdrawn from circulation. This figure is some 29% up on 2006, thanks largely to increased cooperation with Member States' competent authorities.

## 2.6. The Hercule II programme

The Hercule programme was set up to promote activities aimed at protecting the Communities' financial interests.<sup>40</sup> In 2007 the European Parliament and the Council decided to extend the programme for the period 2007-13.<sup>41</sup>

The budget for the programme has been increased by €6 million a year to include within it a new strand to provide financing for training measures and the purchase of equipment in order to combat cigarette smuggling.

---

<sup>36</sup> Proposal for a Council Regulation amending Regulation (EC) No 1338/2001 (COM(2007) 525 final).

<sup>37</sup> Third report from the Commission based on Article 11 of the Council Framework Decision of 29 May 2000 (COM(2007) 524 final).

<sup>38</sup> Framework Decision 2000/383/JHA (OJ L 339, 21.12.2001).

<sup>39</sup> Council Decision of 17 December 2001 (OJ L 339, 21.12.2001).

<sup>40</sup> [http://ec.europa.eu/anti\\_fraud/programmes/index\\_en.html](http://ec.europa.eu/anti_fraud/programmes/index_en.html)

<sup>41</sup> Decision No 878/2007/EC (OJ L 193, 25.7.2007).

The 2007 budget of €13.574 million has made it possible to co-finance 15 projects in the education field, 21 projects in the field of technical assistance and 10 actions in the field of legal research. Among these projects there are several activities at the international level, such as conferences to ease theoretical and operational exchanges, but also individual support to certain national authorities, such as the purchase of equipment to facilitate smuggling detection or technical assistance for a specific investigation.

## 2.7. Other measures taken in 2007 to protect the Community's financial interests

As part of the *European Transparency Initiative*,<sup>42</sup> it was proposed that information on the beneficiaries of EU funds be systematically published, irrespective of how the funds were managed. After the inclusion of this obligation in 2006 in the Financial Regulation<sup>43</sup> and in the Commission Regulation on the Structural Funds and the Cohesion Fund<sup>44</sup>, two Regulations<sup>45</sup> were adopted in 2007 which place the Member States under an obligation to publish a list of the beneficiaries of the agricultural funds and of the European Fisheries Fund, together with the amounts they receive.

In response to the Communication on a European strategy against fiscal fraud<sup>46</sup> and the request made by the EU Council of Ministers in June 2007, the Commission adopted a Communication containing key elements to combat *VAT fraud*, in particular missing trader fraud.<sup>47</sup> In their contribution to this report, several Member States reported having taken measures at national level to fight VAT fraud more effectively.<sup>48</sup>

The *Convention on the Protection of the European Communities' Financial Interests*<sup>49</sup> and its protocols<sup>50</sup> were ratified in 2007 by Slovenia. Romania and Bulgaria automatically acceded to it when they joined the EU.<sup>51</sup> The Commission urges the Member States that have not ratified the Convention and/or its protocols to do so as soon as possible.<sup>52</sup>

---

<sup>42</sup> COM(2007) 127.

<sup>43</sup> Council Regulation (EC, Euratom) No 1605/2002 of 25 June 2002 on the Financial Regulation (OJ L 248, 16.9.2002), as amended by Regulation (EC, Euratom) No 1995/2006 of 13 December 2003 (OJ L 390, 30.12.2006).

<sup>44</sup> Commission Regulation (EC) No 1828/2006 of 8 December 2006 (OJ L 371, 27.12.2006).

<sup>45</sup> Council Regulation (EC) No 1437/2007 of 26 November 2007 (OJ C 181, 3.8.2007); Commission Regulation (EC) No 498/2007 of 26 March 2007 (OJ L 120, 10.5.2007).

<sup>46</sup> COM(2006) 254.

<sup>47</sup> COM(2007) 758.

<sup>48</sup> BE, CZ, HU, MT and RO.

<sup>49</sup> Referred to above.

<sup>50</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 2007 (OJ C 221, 19.7.1997).

<sup>51</sup> Council Decision 2008/40/JHA of 6 December 2007 (OJ L 9, 12.1.2008).

<sup>52</sup> To date, CZ, HU, MT and PL have not ratified the Convention or its protocols. EE has not ratified the protocol on the interpretation of the Convention by the CJEC. IT has not ratified the second protocol, thereby delaying its entry into force. In its second report on the implementation of the Convention and its protocols (COM(2008) 77 final), the Commission also notes shortcomings in the transposal of a number of provisions in seven Member States. The Commission will contact the Member States individually in order to ensure that transposal is completed.

In 2007 the Commission signed *administrative cooperation arrangements* with the competent authorities in certain third countries<sup>53</sup> to combat fraud, corruption and any other illegal activity which harms the financial interests of the Community or of the signatory third country. It is holding negotiations in order to conclude similar agreements with other third countries which receive financial assistance from the EU.

Slovakia adopted a *national strategy to protect Community financial interests* which provides for measures in all relevant fields in the coming years. The Romanian Criminal Code and other annexed laws were amended in order to introduce the criminal liability of legal persons. In Italy the Committee for the Prevention of Community Fraud has been tasked with coordinating all activities in the fight against fraud and other irregularities in the fiscal, agricultural and structural fund sectors. Sweden reinforced its internal control system applicable to national and European funds.

New *administrative penalties* applicable to certain serious irregularities were introduced into Maltese and Romanian law. Latvia increased the level of *criminal sanctions* applicable to infringements against Community Funds perpetrated by an organised group. Several Member States reported that they had adopted or modified manuals and guidelines aimed at harmonising the *treatment and communication of irregularities*.<sup>54</sup> In Estonia all irregularities for which a definitive solution was found are published on the Finance Ministry's website.

In Belgium and France the criminal law as it applies to *corruption* was amended in order to comply with European and international conventions in this field. In Slovakia an inter-service group was created in order to update the National Programme against Corruption. In Portugal several control authorities launched a joint action against corruption which led to the publication of a final report in 2007. Belgium and Cyprus adopted measures to fight *money laundering* more effectively.

With regard to *recovery*, debts to the European Communities are now dealt with in the same way as national tax debts in Romanian law.

### 3. CHECKS TO IDENTIFY FRAUD AND OTHER IRREGULARITIES

For the collection of the Community's own resources and in those areas where the Member States implement the budget, responsibility for carrying out checks to identify fraud and other irregularities is shared between the authorities of the Member States and the Community authorities.

This chapter briefly describes the conduct and the results of these checks.

---

<sup>53</sup> The national authorities in Morocco (this agreement also covers the customs field), Djibouti, Congo Brazzaville, Senegal, Argentina and the *Forum des inspections générales d'État d'Afrique (FIGE)*.

<sup>54</sup> DE, IT and SK.

### 3.1. Checks concerning the Structural Funds

In order to lend new impetus to improving the financial management of the EU funds, in particular those managed by the Member States, and in the light of Opinion No 2/2004<sup>55</sup> of the Court of Auditors, the Commission adopted an action plan towards an integrated internal control framework in January 2006.<sup>56</sup> The strategic aim is to obtain a positive statement of assurance from the Court of Auditors.

#### 3.1.1. Improvement of the control framework

The new legislation on structural expenditure<sup>57</sup> which has been applicable since the start of the 2007-13 programming period simplifies and clarifies certain aspects of the procedure for granting and paying funds. It improves the provision of information to all those involved, in particular to potential beneficiaries, on the applicable legislation. The systems of internal control are defined more clearly.

For each operational programme the Member States designate a *managing authority*, responsible for the proper implementation of the programme and for carrying out management checks.

The Member States also designate a *certifying authority* (“paying authority” in the legislation which applied to the period 2000-06), responsible for sending the Commission certified statements of expenditure and requests for payment. It is also responsible for following up any irregularities which are discovered (including fraud) and providing the Commission with regular reports on this.

The Member States finally designate an *audit authority* (“winding-up body” for the period 2000-06). The rules governing the control and auditing of transactions by the audit authority have been harmonised for the new programming period and the exchange of information with the Commission has been reinforced. Henceforth, the audit authority is required to submit to the Commission an auditing strategy for the operational programme for which it is responsible.

The audit authority sends the Commission an *annual report* summarising the results of its audits. For the new programming period, this report must be drawn up in a standard format and must mention the margin of error identified. Another important step forward is the requirement that the audit authorities deliver an *opinion* every year as to whether the management and control systems work effectively in order to

---

<sup>55</sup> OJ C 107, 30.4.2004.

<sup>56</sup> COM(2006) 9 and SEC(2006) 49. “Integrated control framework” should be taken to mean complementary systems of oversight and scrutiny which are sufficient to provide reasonable assurance that the risk of error is properly managed at all transaction levels. In late 2008 the Commission will be publishing a communication on the costs and benefits of control relative to the residual risk. On the other aspects, see the first report (COM(2007) 86) and the final report (COM(2008) 110) on the implementation of the action plan.

<sup>57</sup> Council Regulation (EC) No 1083/2006 of 11 July 2006 laying down general provisions on the ERDF, the ESF and the Cohesion Fund; Regulation (EC) No 1080/2006 of the European Parliament and of the Council of 5 July 2006 on the ERDF; Commission Regulation (EC) No 1828/2006 of 8 December 2006 setting out rules for the implementation of Regulations (EC) Nos 1083/2006 and 1080/2006. Similar rules apply in the fisheries sector, Regulation (EC) No 1198/2006 (OJ L 223, 15.8.2006).

provide reasonable assurance that the statements of expenditure are correct and the underlying transactions are legal and regular.

The Member States are now required to produce *annual summaries* of all declared expenditure and all performed audits.<sup>58</sup> This also applies to the 2000-06 programming period. At the end of April 2008, almost all Member States had produced annual summaries that were in compliance or largely in compliance with the minimum conditions laid down. The Commission has taken steps to initiate legal proceedings against one Member State.

For its part, the Commission has put in place a procedure for assessing the compliance of Member States' management and control systems in accordance with Article 71 of Regulation (EC) No 1083/2006. It examines and approves the audit strategies produced by Member States' audit authorities. On the basis of its own checks and audits and the information provided by the Member States, the Commission evaluates the assurance provided by the systems in place in the Member States. This evaluation is contained in the annual activity report of each competent Directorate-General and in the summary report by the Commission. This evaluation is based on the harmonised indicators of legality and regularity.

The Commission has the power to interrupt or suspend payments. It can also apply financial corrections.

### 3.1.2. *Management checks by the Member States in the area of the ERDF*

The information contained in this point is based solely on data transmitted by the Member States on the basis of a questionnaire<sup>59</sup> and concerns only the ERDF. The questionnaire requested information on control systems in place at the end of 2007 and statistics concerning checks conducted in 2005.

Most irregularities inevitably occur at the level of the final recipients or at the level of final beneficiaries. The management authorities carry out "management", or "first-level", checks to discover these irregularities at an early stage in the procedure. These checks comprise administrative checks of documents relating to each request for reimbursement submitted by the beneficiaries and on-the-spot checks.

The vast majority of Member States stated that during *desk-based administrative checks* all the documents concerning the projects and the expenditure claims are systematically submitted to in-depth checks. In all Member States, in-depth checks cover the eligibility of expenditure. In approximately half of Member States, authorities also systematically check the adequacy of supporting documents; in one third of them the authorities check the delivery of products or services co-financed.

The checking rate for the budget verified in 2005 by *on-the-spot checks* was considerably different from one Member State to another and even from one programme to another. When the rate was less than 100%, Member States combined representative or random sampling methods with risk analysis to direct the controls.

---

<sup>58</sup> Article 53b(3) of the Financial Regulation.

<sup>59</sup> This information has not been cross-checked with data available in the Commission's Regional Policy DG. All the replies have been published in document SEC(2008) 2300.

In 2005 on-the-spot checks were in general carried out by intermediate bodies. In five Member States the management authorities themselves carried out such checks in a large proportion of cases. Only one Member State significantly externalised on-the-spot checks.

All Member States stated that checks carried out and irregularities detected are recorded for each project in the *programme monitoring database*. However, they were rarely in a position to supply reliable statistics on the *results of the controls* carried out in 2005. This indicates that these data are not centralised.

On the basis of the statistics provided, the most frequent cases of detected irregularities concerned ineligible expenditure, missing or incomplete supporting documents and non-compliance with horizontal rules or the terms of the grant agreement. The largest number of irregularities was in general detected during desk-based administrative checks, but the proportion of irregularities detected during on-the-spot checks remains significant (between 20% and 50%).

Detecting the irregularities at this early stage, close to the beneficiaries, facilitates taking simple and effective *measures*, such as requesting provision of the missing documents, or withdrawing and re-allocating funds to another expenditure or project if the expenditure is non-eligible. When an irregularity is detected, Member States must ensure follow-up, sometimes by means of integrated computer systems. When the irregularity exceeds a certain threshold, it is communicated to the Commission (OLAF).

Among the more frequent causes of irregularities referred to by Member States are unclear eligibility rules, lack of guidance, and staff issues. Some also mention bankruptcies, the risk of over-financing, or criminal behaviour. The recent improvements to the control framework seek to reduce the number of beneficiaries who submit, either deliberately or otherwise, spurious requests (at least for ineligible expenditure) and to limit the risk of error for the competent authorities.

### **3.2. The framework for checks in the agricultural sector**

*Controls by national authorities.* Under the common agricultural policy, according to the principle of shared management the Member States are responsible for paying subsidies to the final beneficiaries through *paying agencies*<sup>60</sup> accredited by the Member States. They are responsible in particular for checking the admissibility of claims and their compliance with EU rules before payment.

For each aid scheme, the relevant sector regulations lay down detailed rules on checks carried out by the paying agencies or by delegated bodies operating under their supervision.

All aid applications are subject to administrative checks before any payment is made. *On-the-spot checks* are carried out on a sample basis, which normally ranges between 5% and 10% but may or must go up to 100% depending on the risk in the sector concerned.

---

<sup>60</sup> Regulation (EC) No 1290/2005 (OJ L 209, 11.8.2005).

The most important control system is the Integrated Administration and Control System (IACS). It covers all direct payments to farmers. The IACS includes a computerised database, an identification system for farmers, for agricultural parcels and for animals in case of payments linked to animals, and a system for identification and registration of payment entitlements and aid applications. The European Court of Auditors has repeatedly confirmed that, where properly applied, the IACS is an effective control system to limit the risk of irregular expenditure.

For aid schemes which do not fall under the IACS, such as storage of products or export refunds, complementary checks must be carried out after the payment to the beneficiary has been made.

At the end of each financial year, the *certification body* draws up a certificate stating whether it has gained reasonable assurance that the accounts transmitted to the Commission are true, complete and accurate and that the internal control procedures have operated satisfactorily.

The Member States must send to the Commission the annual accounts of each paying agency, accompanied by a *statement of assurance* signed by the paying agency's director. The statement of assurance may be qualified by reservations, which must quantify their financial impact. In that case, it must include a remedial action plan and a precise timetable for its implementation. The statement must provide for effective supervision of the management and control system in place throughout the year.

Starting in 2007,<sup>61</sup> Member States with more than one paying agency must also draw up at the end of the financial year an annual summary report (*synthesis*) covering the statements of assurance and certificates issued by the certification bodies. Coming on top of the statement of assurance and certification, this is designed to strengthen the chain of responsibility between the Member States and the Commission.

*Controls by the Commission.* The Commission verifies, firstly, the completeness, accuracy and veracity of the paying agencies' accounts (clearance of accounts) and, secondly, mostly by means of on-the-spot checks, whether the expenditure has been effected by Member States in conformity with the Community rules. Where this is not the case, it excludes the expenditure concerned from Community financing (financial corrections). This latter mechanism, called "conformity clearance", has over the years proved to be a very effective means of protecting the Community's financial interests.

Conformity clearance shields the Community budget from expenditure which should not be charged to it. It is not a mechanism by which irregular payments to final beneficiaries are recovered, something which, according to the principle of shared management, is the sole responsibility of the Member States. Its purpose is to examine the management and control systems implemented by the Member States and to recover from national authorities any expenditure which is not in conformity with Community law. Financial corrections are determined on the basis of the nature and gravity of the infringement and the financial damage caused to the Community.

---

<sup>61</sup> Regulation (EC) No 885/2006 (OJ L 171, 23.6.2006).

The amount is calculated on the basis of the loss actually caused or on the basis of an extrapolation. Where this is not possible, flat-rates are used which take account of the severity of the deficiencies in order to reflect the financial risk for the Community. In 2007 the Commission excluded approximately €86.6 million from Community financing under the EAGGF and the EAFRD<sup>62</sup> on grounds of its non-compliance with Community rules.

Where individual irregular payments are or can be identified as a result of the conformity clearance procedures, Member States are required to follow them up by recovery actions against the final beneficiaries. However, even where this is not possible because the financial correction relates exclusively to deficiencies in the Member State's management and control system, correction remains an important means of improving the functioning of that system and thus of preventing or detecting and recovering irregular payments to final beneficiaries. Conformity clearance thereby contributes to the legality and regularity of transactions at the level of final beneficiaries.

### **3.3. Control of traditional own resources**

The Member States are responsible for recovering traditional own resources, keeping accounts and conducting the necessary checks and investigations.<sup>63</sup> They must keep “A accounts” for the registration of paid and/or guaranteed customs debts, and “B accounts” for the registration of either unpaid or not guaranteed debts (or debts guaranteed but contested). Many debts appearing in the B accounts are the result of fraud or detected irregularities. Primary national inspections (either physical inspections or inspections of documents) and national post-clearance inspections are the detection methods which reveal most frauds and other irregularities (80% in 2006 and 2007).

The Commission monitors the correct functioning of the traditional own resources system. It ensures that traditional own resources are made available on time and charges interest for failure to do so. The control methods include on-the-spot inspections in the Member States, Joint Audit Arrangements,<sup>64</sup> follow-up of statements of preliminary findings (ex-sector letters) and annual reports of the Court of Auditors and specific monitoring in case of signals from other Commission departments (e.g. signals from OLAF in individual cases with a significant financial impact and which involve mutual assistance).

In its 32 inspections in 2007 DG Budget detected 114 anomalies in the area of traditional own resources. As in previous years, only a very limited number of anomalies had to be treated as infringements (no new files were opened in 2007; currently 31 files are pending), as they are regularly discussed bilaterally with Member States and submitted to the Advisory Committee on Own Resources.

---

<sup>62</sup> Decisions 2007/243/EC (OJ L 106, 24.4.2007), 2007/247/EC (OJ L 261, 6.10.2007) and 2008/68/EC (OJ L 18, 23.1.2008).

<sup>63</sup> Council Regulation (EC, Euratom) No 1150/2000 (OJ L 130, 31.5.2000).

<sup>64</sup> Joint Audit Arrangements cover AT, DA and NL. These Member States do the audits themselves on a subject agreed on with DG Budget, which then monitors the process and the results of the audit during an evaluation visit.

As part of the follow-up to anomalies described in the Court of Auditors' Annual Reports and Preliminary Findings, 20 new letters containing observations were received by DG Budget in 2007.

The control findings do not change the general picture of timely and prompt financing of the EU budget by traditional own resources. All in all, Member States comply with the Community legislation in this field.

### **3.4. On-the-spot checks and inspections under Regulation (Euratom, EC) No 2185/96<sup>65</sup>**

Regulation (Euratom, EC) No 2185/96 confers on the Commission responsibility for carrying out on-the-spot checks and inspections in the Member States and, in accordance with the cooperation agreements in force, in third countries. Since 1 June 1999, this responsibility has been borne by OLAF.<sup>66</sup>

On-the-spot checks and inspections, conducted on the premises of economic operators, are actions which are typically carried out during external investigations, i.e. administrative investigations conducted by OLAF outside the Community institutions and bodies in order to combat all forms of illegal activity which undermine the financial interests of the European Union.

The way in which OLAF implements Regulation 2185/96 corresponds to the guidelines contained in a *Vademecum*<sup>67</sup> which was adopted in October 1997 and is currently being updated.

In 2007 OLAF carried out 74 on-the-spot checks within the meaning of Regulation 2185/96 (comparable to the 72 checks carried out in 2006), including:

- 25 relating to agriculture;
- 26 relating to structural policies;
- 21 relating to direct expenditure and external aid; and
- 2 relating to internal investigations.

All the on-the-spot checks took place within the territory of the European Union, apart from one which was carried out in a third country in the field of external aid.

Experience has shown that on-the-spot checks constitute, quantitatively and qualitatively, a very important tool for conducting external investigations.

However, the operational outcome is very much dependent on the effectiveness of the cooperation forthcoming from national authorities. In this connection, OLAF is currently preparing a new report on the implementation of Regulation 2185/96

---

<sup>65</sup> Council Regulation (Euratom, EC) No 2185/96 (OJ L 292, 15.11.1996).

<sup>66</sup> Regulation (EC) No 1073/1999 and Regulation (Euratom) No 1074/1999 (OJ L 136, 31.5.1999).

<sup>67</sup> UCLAF/12/SEC(97)9989.

outlining “good practices” for each stage in the on-the-spot checks. The report should be adopted in 2008 together with the new version of the *Vademecum*.

#### **4. THE LIMITATION PERIOD APPLICABLE TO PROCEEDINGS AND DECISIONS CONCERNING IRREGULARITIES**

The Member States are responsible for bringing proceedings against the authors of irregularities committed in areas covered by shared management and traditional own resources. They are also responsible for the application of any penalties and administrative measures which are imposed as a result of such proceedings.

The limitation periods provide legal certainty. However, when the limitation period has passed, the irregularity cannot be proceeded against or the penalty applied. In order to protect the Communities’ financial interests, Article 3 of Regulation (EC, Euratom) No 2988/95 provides for minimum limitation periods. The Member States can provide for a longer period.

In order to identify which national laws make provision for longer periods than the minimum periods and which periods apply in cases not regulated by Community law, the Commission asked Member States to answer a questionnaire. A summary of the answers is presented below. The analysis has been limited to administrative procedures.<sup>68</sup>

For expenditure managed directly by the Commission, the five-year limitation period laid down in Article 73a of the Financial Regulation, as defined more closely in Article 85b of the implementing rules,<sup>69</sup> is applicable. This area is not dealt with in this report.

##### **4.1. Limitation period for proceedings concerning irregularities**

“Normal” limitation period. Article 3(1) of Regulation 2988/95 lays down a limitation period for proceedings<sup>70</sup> of four years from the time when the irregularity was committed. European sectoral rules may provide for a shorter period, which may not be less than three years. These periods are directly applicable in the Member States, unless national rules provide for longer periods.

In all, 21 Member States provide for longer periods than those set by the Community rules. Usually the periods range between 5 and 10 years and, in exceptional cases, 12 or even 20 years.

Regulation 2988/95 provides that the limitation period is interrupted by any act of the competent authority, notified to the person concerned, relating to investigation or legal proceedings concerning the irregularity. Moreover, some national laws consider

---

<sup>68</sup> Some Member States expressly indicated that the rules of civil procedure applied also to administrative procedures. The civil law rules alone have been taken into account in these cases.

<sup>69</sup> Commission Regulation (EC, Euratom) No 2342/2002 of 23 December 2002 (OJ L 357, 31.12.2002).

<sup>70</sup> Proceedings are administrative or judicial procedures initiated in order to discover or establish irregularities.

also as grounds for interruption the negotiation of a settlement procedure with a potential debtor.

*“Absolute” limitation period.* Regulation 2988/95 provides that, without prejudice to any interrupting acts, the limitation becomes effective if, after an “absolute” limitation period equal to *twice* the “normal” limitation period has passed, the competent authority has not imposed a penalty, except where the cause of the interruption is the initiation of criminal proceedings against the person concerned in connection with the same facts.

Nine Member States have established longer “absolute” periods in certain specific sectors. These periods are generally 10 years, except in one case where it is 20 years.

#### **4.2. Limitation period for implementing the decision establishing an administrative penalty**

Regulation 2988/95 lays down a limitation period of *three years* for implementing the decision establishing an administrative penalty.<sup>71</sup>

Altogether 15 Member States reported that they have laid down longer periods ranging from 4 to 10 years following the decision establishing the penalty. A period of 5 years is the most common. In general, the period starts to run as soon as the decision is taken, but in some Member States it starts to run on 1 January of the following year, after notification of the decision or after expiry of the payment deadline set in the decision. The grounds for interruption are similar to those generally applying to proceedings.

#### **4.3. Limitation period for implementing the decision establishing an administrative measure (recovery)**

Community law does not provide for a limitation period for implementing the decision taken in national proceedings establishing an administrative measure. This period is, however, of particular importance for the success of recovery procedures. Whereas one would expect all 27 Member States to provide for such periods in their national laws, only 21 indicated national provisions, which nevertheless differ considerably as they allow time limits ranging from 3 to 10, or even 20, years.

The starting point of the period and the grounds for interruption are similar to those applying to the limitation period for implementing the decision establishing an administrative penalty.

### **5. RECOVERY**

Where the budget is implemented under shared management and for traditional own resources, responsibility for recovering amounts from final beneficiaries lies in the first instance with the Member States. At Commission level, the authorising officers by delegation have sole responsibility for financial follow-up. OLAF contributes

---

<sup>71</sup> This concerns the enforcement of penalties within the meaning of Article 5 of the above-mentioned Regulation.

solely to financial follow-up activities directly linked to operational activity. However, where the Structural Funds are concerned, OLAF contributes, during a transitional period as part of a phasing out of its activities in this area, to the follow-up of irregularities notified by the Member States relating to the 1994-99 programming period.<sup>72</sup> A new electronic interface will establish a direct link between each authorising officer's data warehouse and the register of notifications of irregularities (ECR).

## 5.1. Agriculture

Article 32 of Council Regulation (EC) No 1290/2005 introduced a new 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 automatically charged to the budget of the Member State concerned within the framework of the annual financial clearance of the EAGGF and EAFRD accounts. In certain cases of negligence on the part of the Member State, the entire amount may be charged to it.

This mechanism was first applied by a Commission decision of April 2007<sup>73</sup> which cleared all pending non-recovered cases dating from before 2003 or 1999 (cases that were four or eight years old respectively) by charging €131.7 million to the Member States. A further €100 million was or will be charged to the Member States by subsequent Commission decisions clearing the accounts for the 2006 financial year, having been disjoined in April 2007.

For the 2007 financial year, the Member States reported the financial information about recovery procedures by DG AGRI. On the basis of the final situation as established on 11 April 2008, €154.3 million was recovered by the Member States during the 2007 financial year, and the outstanding amount still to be recovered at the end of that financial year was €1.438 billion. The financial consequences of non-recovery for cases dating from 2003 or 1999 were determined according to the "50-50" rule mentioned above by charging €37.6 million to the Member States in the April 2008 accounts clearance decision.<sup>74</sup> Moreover, €65 million will be charged to the Community budget for cases reported irrecoverable during the 2007 financial year.

After the first 50% has been charged to the national budget, Member States are still required to continue their national procedures for recovering the unduly paid amounts from the beneficiaries and to credit 50% of the amounts effectively recovered afterwards to the Community budget.

---

<sup>72</sup> Communication C(2007) 5709 on the clarification of activities in the Commission concerning the financial follow-up of irregularity cases.

<sup>73</sup> Decision 2007/327/EC (OJ L 122, 11.5.2007).

<sup>74</sup> Decision 2008/396/EC (OJ L 139, 29.5.2008).

## 5.2. Structural Funds

In the area of the Structural Funds, the recovery from the beneficiaries of amounts unduly paid owing to irregularity or fraud is also carried out by the Member States. The recovery of these amounts at Commission level can be done by reduction or cancellation of 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 presentation of the request for final payment to the Commission was 31 March 2003. In that period, the Community co-financed around 1 000 programmes worth around €159 billion in total.<sup>75</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 11 647 cases of irregularities (74 in 2007) corresponding to a financial impact estimated at €1.52 billion<sup>76</sup> for the Community contribution (€68 million for 2007).

Of these cases, 5 686 have been closed definitively at Commission level and an amount of €30 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 1 610 cases, with a financial impact of €101 million for the same period. The Commission departments have started reconciliation procedures with a view to closing these cases.

Furthermore, in 2007 the Commission adopted a Commission decision on the financial treatment to be applied to expenditure financed by the EAGGF, Guidance Section, for 27 notifications for which the Member States concerned had asked that the irrecoverable amounts be charged to the Community budget.

For the *2000-06 programming period*, the Member States have so far communicated 12 161 cases of irregularities (3 428 in 2007) with a financial impact of approximately €1.79 billion for the Community contribution (€30 million for 2007).

The Member States have informed the Commission that administrative and/or judicial procedures have been finalised at national level for 4 471 of these cases and that some €09 million has been recovered.

The total amount of *financial corrections* concerning the 1994-99 and 2000-06 programming periods was €141 million (€176 million in 2007) and €156 million (€20 million in 2007) respectively. These financial corrections are the result of audits by the Commission and the Court of Auditors, OLAF investigations and the closure procedure for programmes from the 1994-99 period. They consist of official financial correction decisions following the detection of an irregularity,

---

<sup>75</sup> These are multiannual programmes. This figure does not include projects directly financed under the Structural Funds and Cohesion Fund.

<sup>76</sup> Situation according to the data in the ECR database as at 15 April 2008.

decommitments on programme closure because the Member State did not declare sufficient eligible expenditure, and reimbursements of amounts recovered following the completion of court cases still pending when the programmes in question were closed.<sup>77</sup>

Most of the amounts taken into account following irregularities notified to the Commission are included into these financial corrections. However, some irregularities are notified, but deductions are made before payment and hence are not included in the financial corrections.

### **5.3. 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 2007 is approximately €377 million.

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

At present, the recovery rate for irregularities occurring in 2007 is 40% (approximately €150 million).<sup>78</sup> This is a good starting position: the overall recovery rate for 2006 recorded in last year's report was 32% and it has since climbed to 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 2007 the Commission refused Member States' write-off requests in 16 cases totalling some €28 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 €20 million because they did not establish customs debts where they should have done so.

### **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:

- estimate and establishment of the entitlement by the authorising officer (who must ensure that the claim is certain, of a fixed amount and due),

---

<sup>77</sup> The figures do not include financial corrections that did not result in recovery, such as those made when a Member State detected an irregularity or accepted the financial correction proposed by the Commission and the irregular amount was reallocated to another project.

<sup>78</sup> The figures used have been calculated on the basis of data available as at 9 March 2008.

- 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:

- the adoption of 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);
- the securing of an order before the national or Community courts. This also includes a civil action within criminal proceedings in those jurisdictions where this is possible.

In those cases where recovery orders were launched during the course of 2007, full or partial recovery has already been announced in 226 reported cases. Commission departments have recovered €3.7 million. In 184 cases the full irregular amount has been recovered, and in 223 cases the amount to be recovered has yet to be determined. An amount of €10.7 million still remains to be recovered, concerning 204 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 2007, OLAF formally closed the financial follow-up for more than €203 million. €197.67 million was recovered in the field of the Structural Funds, following the closure of 53 cases of which 35 were part of the backlog of “old” cases. This amount appeared in the Commission’s accounts for previous financial years. Substantial amounts were also recovered in 2007 in connection with cases not yet closed.