

COMMISSION OF THE EUROPEAN COMMUNITIES

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REPORT FROM THE COMMISSION

ON TOUGHER MEASURES TO FIGHT AGAINST FRAUD AFFECTING
THE COMMUNITY BUDGET

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OBJECTIVE AND BACKGROUND

1. At a time when it is proposing the Community be given new resources and budgetary discipline be tightened, the Commission must also show that it is conducting an effective and determined fight against fraud. The straight question asked of it in this connection is what it intends to do now to protect Community finances more effectively. Since the rules governing Community revenue and expenditure operations have been drawn up gradually as the corresponding policies developed, it is perhaps time for the whole question of Community control and anti-fraud measures to be reviewed, now that the CAP has existed for 25 years, own resources for 17 years and the Regional Fund for 12 years.
2. This report has also been drawn up in response to demands by the various Community institutions for the Commission to step up its measures against cases of fraud affecting the Community budget.

In April 1986 Parliament's Committee on Budgetary Control organized a public hearing on frauds involving own resources and agricultural expenditure and in December 1986, this Committee sent to the Commission a questionnaire about the measures taken by the Commission to combat fraud more effectively. Finally, in its resolution of 7 April 1987 deferring the discharge for 1985, Parliament called on the Commission:

"to submit a convincing plan to improve the monitoring of revenue and expenditure and the prevention of fraud and irregularities, indicating the organizational and legislative measures to be taken within the Commission and in cooperation with the Member States."

In a similar vein, Parliament inserted ten headings for anti-fraud measures in the 1987 budget, its intention being to continue this operation for 1988 and 1989.

3. At the same time, the Council decided to insert a new Article 720 in its draft supplementary and amending budget No 1/1987 for revenue generated by the measures against frauds and irregularities and, in a statement, clearly displayed its political determination to make progress in this sector and to cooperate on any appropriate measures. The Council also took this opportunity to ask the Commission to step up its internal coordination in this field.
4. After repeatedly pointing out various shortcomings in the Community's methods for combating fraud and irregularities in its annual reports, the Court of Auditors included a special chapter on this subject in its draft report for 1986 and concluded that the Commission needs to be much more effective in its action, in particular by means of greater coordination of the resources at its disposal.
5. More generally, the idea that European integration has increased the possibilities for growing rich on fraud and that the Community institutions are not effective enough in fighting these abuses has taken root not only in Parliament but also in the media and public opinion.
6. In this context this report follows up the Commission's reply to the letter of the Parliament's committee on budgetary control and the investigations of a working party consisting of the main departments concerned and set up by the Commission following this reply. It is designed to identify the basis for the overall plan on tougher measures against fraud and to set out the consequences of this plan for the administrative operation of its departments, so that the Commission will be able to take the necessary decisions as soon as possible.

A. THE MEMBER STATES AND THE COMMISSION IN THE FIGHT AGAINST FRAUD

ANTI-FRAUD MEASURES

7. For the purposes of this report, the term "fraud" covers any infringement, whether intentional or not, of a legal provision committed by private persons or bodies and having adverse financial consequences for the Community budget.

When Member States apply Community law incorrectly, this constitutes an "infringement" which may be the object of the ad hoc procedure of Article 169 of the Treaty or of financial adjustments during the annual clearance of EAGGF Guarantee accounts. In principle, infringements are not in the same category as frauds and are not covered by this report. However, they may sometimes be connected with cases of fraud and may always be detected as a result of the Commission's control activities.

8. Parliament and the media often claim that some Community rules lead to cases of fraud involving considerable amounts of money. Specific cases arise regularly to lend credence to such claims. However, it should be firmly pointed out that the figures given for the financial losses resulting from frauds are not based on any really reliable study. Frauds do occur; but there is no verifiable source to justify claims that they amount to 10% or even more. It should also be pointed out that the fight against fraud is a continuous operation which cannot have immediate results - presenting any kind of situation picture is therefore very tricky.

9. Despite the lack of any precise quantifiable information, the Community must still take effective measures against fraud. This is a financial necessity which is particularly acute in the current budgetary circumstances. But it must also be pointed out that any shortcoming in the application of the customs, agricultural or tax regulations can produce distortions in the conditions of competition

or shifts in trade, which can have extremely serious consequences for the operation of the internal market and the plan to complete this market by 1992.

10. Without wishing to underestimate the problem of fraud, its political repercussions or its financial and economic consequences, this problem should not be allowed to hide the great mass of everyday financial operations which comply with the rules. At the same time, specific efforts to fight fraud must not detract from the Commission's ordinary powers and means of control. There is a continuous interaction between these and the fight against fraud which makes any attempt to isolate them at operational level extremely tricky.

COMPLEMENTARITY BETWEEN THE MEMBER STATES AND THE COMMISSION IN THE FIGHT AGAINST FRAUD

11. For the purposes of the following analysis, the fight against fraud may be divided into four stages:

- (i) detection, which mainly raises the question of sources of information;
- (ii) investigations of presumed cases of fraud, the effectiveness of which will depend in particular on the powers granted to the inquiry team and its responsibilities;
- (iii) the follow-up to these cases, as regards legal proceedings, changes to the rules or the financial aspects;
- (iv) prevention.

12. At each of these stages, there is a different division of responsibilities between the Member States and the Commission. However, the general principle for this division is simple. In the most important sectors of Community finance (agricultural expenditure and own resources in particular), it is Member States which manage operations and which are also responsible for the initial control to

check that the measures have been properly implemented. The Commission's main role is to check whether these activities comply with its rules.

13. The Member States also have most of the powers of authority needed to fight fraud. Except in the agricultural sector - and in certain Funds - where it can take direct action against the operators involved, the Commission must go through the national departments for any action in the Member States.
14. Most of the fraud detection function is the responsibility of the Member States. However, the Commission has some resources, although these are modest compared with the size of the undertaking: agricultural surveys, statistical analyses, missions to non-member countries and direct information.
15. The most important element is the Commission's information system for cases of fraud detected by the Member States. As regards the information which the Commission received on cases of fraud, the system of official notification for the agricultural sector is based on Regulations No 729/70 and No 283/72, which require Member States to send a quarterly list of cases of irregularities detected by the national authorities and to communicate new fraudulent practices immediately. This legal base may be considered satisfactory and the information supplied often triggers off Commission inquiries. However, the quality of this information varies from one Member State to another.

As regards duties on imports from non-Community countries, Regulation No 2891/77 states that the Member States must submit six-monthly reports on their activities to combat fraud. However, these reports, which differ enormously in quality between Member States, at present give no more than a statistical analysis of overall control activities and cannot be used for individual cases of fraud. In its proposals for amending this Regulation, the Commission has already asked for a substantial improvement in the content and presentation of these reports.

Finally, under the recently amended Regulation No 1468/81 on mutual assistance, the Member States must send the Commission information on various operations which do not comply with the customs or agricultural regulations. The Commission can then take effective measures and coordinate the Member States' action within the Community or in non-member countries. This instrument is more binding than the regulation previously in force but is less so than in the agricultural sector. Application also varies and, because of its nature, the financial information needed is not generally supplied.

16. As regards investigations, the Commission is quickly hamstrung by the fact that it is the Member States which have the necessary police and legal powers. It therefore depends to a large extent on the work of the national authorities.

Here too, it is mainly in controlling the activities of the national authorities that the Commission's role is most developed. In the agricultural sector, the Commission has the power to carry out at any time the controls which it considers useful, including on-the-spot inspections of individual beneficiaries, and to ask Member States to make the administrative inquiries which it considers necessary and to associate itself with them.

As regards traditional own resources (customs duties, agricultural levies, sugar levies), the Commission can only be associated with national administrative inspections to ensure that the operations of establishing and paying over these own resources have been properly conducted; it may also make a duly substantiated request for additional inspection. It is thus only through indirect channels that the Commission can gain access to files concerning cases of fraud. In the VAT sector, the Commission may control only the calculations of the VAT base from the receipts collected by the Member States; it may not control the receipts themselves.

17. This division of powers goes a long way towards explaining why it is so difficult to set up the "flying squads" which Parliament has demanded for several years. The possibility of using this type of

investigation team effectively is largely conditional on increased Community powers in the field and, at all events, the establishment of new forms of cooperation with the national anti-fraud squads.

18. As regards the following, it is the Member States which are responsible for legal proceedings and the recovery of the amounts involved. The Commission controls recovery operations from the angle of their consequences on the Community budget; it also decides whether any changes need to be made to the rules in the light of the cases encountered.

19. This latter aspect is also one of the main angles from which the problem of prevention should be approached at Community level. Because they are so complicated, the Community rules are often considered as one of the main factors behind fraud and an effort must therefore be made to make these rules clearer and simpler. The training of both national and Community officials is also an asset which should not be neglected.

20. To sum up, it should be clearly stated that the Commission must not be accused of failing in its duties properly because it does not deal directly with all the cases of fraud and is not always informed in detail of the situation in the Member States. The main fight against fraud takes place in the field, under the responsibility of the national authorities. At a secondary level, the Commission's role is one of control, stimulus, coordination and reinforcement; it cannot take over the everyday operations of the Member States which have thousands of officials and the necessary powers. This is also the reason why its general activities to monitor the application of Community rules remain important.

B. HOW THE COMMISSION CAN PLAY ITS ROLE MORE EFFECTIVELY

INTENSIFYING COMMISSION ACTION

21. As the Commission has already told the Parliament's budgetary control committee (paragraphs 2 and 6), the Commission must improve its anti-fraud action on three fronts:

- (i) tougher statutory instruments;
- (ii) closer cooperation with Member States and tighter control of their activities;
- (iii) improved efficiency and internal organization.

22. The Commission must endeavour to secure powers which are better suited to its role, in particular as regards own resources, which are assigned to the Community but collected by the Member States in accordance with their national legislation harmonized as required by Community regulations. It is surprising to say the least that it still has no independent control powers over the Community's "own" resources, which are collected on its behalf by the Member States, nor even a reliable system for obtaining information on the control and anti-fraud measures taken by the Member States. The Commission's powers in the field of own resources must therefore be aligned on those it enjoys as regards the EAGGF.

23. This situation is all the more regrettable since appropriate proposals have been sent to the Council, some of them a long time ago. These include the proposed amendments to Regulation No 2891/77 and the proposed regulation on irregularities concerning own resources, which was presented in 1979 and would establish for own resources an information system on fraud very similar to the one which exists for EAGGF Guarantee. The Commission must now demand that the Council take a very early decision on all the proposals for regulations concerning the mechanisms for traditional own resources and where appropriate recast these proposals in the light of changes that have occurred since they were presented. As regards VAT, the proposed changes to the arrangements and the introduction of a

clearing mechanism in connection with the completion of the internal market must also be used to give the Commission sufficient powers of control.

In addition, the Commission is examining whether it might not be able to make better use of national legal remedies to protect its interest, for instance by bringing civil proceedings in cases before national courts where its financial interest are at stake.

24. The Commission must also tighten up its control of Member States' activities in connection with the execution of the budget in both revenue and expenditure and improve its cooperation with the Member States.

A number of officials in all Member States have duties relating essentially, or even exclusively, to the Community. This underlines the need for more effective cooperation with the national departments concerned, to be achieved by improving exchanges of information, by giving national departments and officials a clearer picture of the Community aspects of their work and by installing a better climate of confidence.

25. A specific point here is the protection of the confidentiality of information transmitted by the Member States. It is absolutely essential, in particular in cases of fraud, that secrecy be maintained: the amount of information that Member States will be prepared to give the Commission depends on how far they trust their correspondents in the other Member States to keep this information secret; watertight guarantees must therefore be given.

26. Similarly, a number of Community rules - obligation to pay over all established own resources, regardless of whether or not they are collected, disallowing of certain items of national expenditure in connection with the clearance of EAGGF accounts - can result in certain amounts having to be met by Member States' national budgets and thus penalize the Member States which are most active in combating fraud. While, for own resources, the proposed amendments

to Regulation No 2891/77 will make this less of a problem, it will always be a real difficulty for the EAGGF, as there can be no question of relieving the Member States of all responsibility in the management of Community finances.

27. Information channels already exist, both under the mutual assistance arrangement and for the EAGGF Guarantee. They must now be made to operate more intensively and more rationally. This will involve developing interconnected computerized networks between national departments and with the Commission. The creation of SCENT, a computerized communications network between national customs authorities and with the Commission, is a particularly important element.

28. But this development of information networks must be accompanied by efforts to make national departments and officials aware of the objectives and constraints of the Community policies they are helping to execute. Meetings and seminars between Community and national officials responsible for control and anti-fraud action must be stepped up, as must exchanges between national and Community officials or any other means of involving national officials more closely in Community activities.

THE ORGANIZATION OF THE COMMISSION AT PRESENT

29. The Commission's internal organization as regards its specific control and anti-fraud functions is at present based - with the sole exception of revenue - on the principle that the departments responsible for control and anti-fraud action are, in each field, attached to the Directorates-General which administer the corresponding policies.

30. Within DG VI (Agriculture), one department is concerned with controls in connection with the clearance of accounts and another with frauds and irregularities.

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It should also be noted that agencies have just been set up to carry out controls of olive oil producers; they began work in Italy in 1986 and are now being set up in Greece, Spain and Portugal. This is an entirely new instrument in the history of the CAP and the initial results are very encouraging.

Although not concerned with the control of operations having direct financial consequences, a team of inspectors of quality standards for fruit and vegetables exists within DG VI, which also operates in connection with the withdrawal of produce from the market and processing and can organize special operations. Work is in progress on setting up a Community control team and organizing specialized action for wine controls. There are also inspection activities in the veterinary field.

Similarly, DG XIV has a team of fisheries inspectors whose work is more especially concerned with the protection of biological resources.

31. Own resources controls are carried out by DG XIX, whose responsibility, as already stated, is to ensure that the rules on establishment and making available are correctly applied. Action more specifically concerned with combating fraud in this area is carried out by DG XXI, which is responsible for the application of Regulation No 1468/81 and for specific surveillance in the field of textiles. By virtue of its role and its contacts with national departments, it has main responsibility for the operation of the customs union.

The structural Funds and other financial instruments also have officials or departments responsible for checking that Community funds are properly used.

32. Financial Control, which neither administers funds nor is directly responsible for the application of rules and regulations in any given sector, is responsible for the control of budgetary revenue and expenditure as prescribed by the Financial Regulation. It is

associated with most controls and can organize controls of its own. It is responsible for the interdepartmental working party on the coordination of on-the-spot controls which, in addition to this function, coordinates the quarterly report to Parliament's Committee on Budgetary Control on cases of fraud brought to the Commission's notice.

33. The Commission therefore has only two groups of officials specifically concerned with combating fraud against the budget; the Frauds and Irregularities Department of DG VI, which has fourteen officials, and DG XXI, which has five officials concerned with anti-fraud and mutual assistance operations.

But all the other departments which administer expenditure or revenue and Financial Control engage in general control operations which are not always easy to distinguish from anti-fraud action.

34. This situation has come in for criticism because of the dispersion of activity and duplication which it causes. In particular Parliament has frequently complained that when it deals with the problem of fraud, in particular when the quarterly report mentioned in paragraph 32 is presented, the Commission has to have a number of different representatives. On this specific point, however, it must be borne in mind that in view of the complexity of the subjects, they must inevitably be handled by specialists. Having these cases presented to the political authority by the specialists who handle them is a guarantee that the information provided will be of the highest quality.

35. On a more fundamental level, it must be emphasized that there is coordination between all departments and this coordination is not ineffective. But it is based essentially on working practices, or even personal relations, even if, in some instances, it is backed by specialised interdepartmental working parties.

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The Commission has also developed a computerized general information system on frauds (IRENE) which, after a certain delay in starting up, now covers over 3 000 cases of fraud in agriculture and is designed ultimately to record and handle all cases of fraud brought to the Commission's notice.

36. But the Commission does not have a structure for coordinating control and anti-fraud action. Efficiency could be improved if there were greater coordination or if the activities of the units responsible for control and anti-fraud measures were combined.

All these units have a number of common concerns:

- the need to develop the legal bases or to make optimum use of existing bases;
- utilization, in particular by improving dissemination, of the information available within the various Commission departments concerned;
- the interest for a common strategy to strengthen the Commission's possibilities of action;
- the need for close coordination between departments responsible for control and those responsible for anti-fraud action;

CONCLUSIONS

37. Commission action in combating fraud embraces a very large number of fields and is divided up among all its departments. The diversity of the problems still justifies this situation amply, but analysis of the structures and activities involved shows that in many cases the activities of individual departments can no longer be carried out in isolation and require close cooperation with other departments concerned.

The Commission is convinced that there is need not only to step up its anti-fraud action, but also to make it more transparent. The possibility of obtaining additional resources, particularly additional staff, is henceforth closely tied to the Commission's ability to convince its partners that it is determined to combat fraud still more effectively. For the European Parliament, as also for the Court of Auditors, this means, among other things, greater centralization of its anti-fraud activities.

It follows from the above two considerations that, as well as increasing its powers and resources for monitoring and for combating fraud, **the Commission must improve the coordination of anti-fraud activities.**

38. This greater coordination should be expressed through two complementary measures, which should come into operation simultaneously:

- (i) **the setting up of a coordination unit,**
- (ii) **the generalization of anti-fraud cells within all the departments concerned.**

This would make it possible to combat fraud more intensively in all fields where this proves essential and to establish a clear coordinating structure. Being decentralized, the structure would not have the drawback of creating a new administrative level that was both too heavy and too remote from the management departments, which indeed would keep their individual responsibilities, while meeting the vital need for clarity and effectiveness.

39. The coordination unit would be responsible for:

- 1. examining all information relating to fraud, on the basis of a systematic and compulsory communication from the DGs concerned, which would enable it to:

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- (a) make sure the DGs concerned were following the situation and take the initiative for coordinating action where a number of departments were involved (which would include arranging for specific checks),
 - (b) take part as appropriate in checks and enquiries arranged by Commission departments;
2. Approaching the responsible departments to ensure:
 - (a) a better use of the legal provisions as well as the strengthening of these in order to remedy any legal deficiency which comes to light;
 - (b) the best possible working methods and staff training and also a widening of relations with the national administrations (which could include exchanges of officials).
 3. thinking out, establishing and running joint infrastructure, particularly computerized infrastructure;
 4. looking after a committee that brought together all the departments concerned, which would hold regular meetings;
 5. representing the Commission in matters relating to fraud with Member States and Community Institutions;
 6. reporting every six months to the Commission on anti-fraud action
 7. assessing after one year what had been done to coordinate anti-fraud action.

This unit would replace the existing interdepartmental working parties in this field, both standing and ad hoc.

40. The coordination unit, under the direct responsibility of the President, would be attached to the Secretariat-General and should at the start consist of a team of 10 officials (including 5 A grades), under the authority of an A/2 official. Whatever additional staff could be obtained later would be assigned to the operational departments and the coordination unit.

41. As regards anti-fraud work within the departments, only DG VI has a department specifically responsible for this. DG XXI has a team of officials in Directorate B which is responsible exclusively for anti-fraud action; a specific unit is to be set up.

In all the other DGs, although a few officials take part, regularly or occasionally, in anti-fraud activities, this is not their sole task and cannot hence be distinguished from their other work.

42. It is therefore necessary that the Commission sets up cells clearly identified as being responsible for combating fraud as quickly as possible and in all the DGs concerned; the cell would act as the correspondent for the coordination unit. The nature of the cell could vary depending on where there are major problems to the assignment to this job of a single official (and this might not be his only job). At all events, whatever their nature and size, these anti-fraud cells should gradually, depending on the needs arising, receive substantial reinforcements.