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**PROTECTION OF THE FINANCIAL INTERESTS  
OF THE COMMUNITIES**

**FIGHT AGAINST FRAUD**  
**Annual Report 1997**

**LIST OF FREEPHONE NUMBERS IN THE MEMBER STATES**

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| Austria | 06605845   | Ireland        | 1800553295   |
| Belgium | 080012426  | Italy          | 167878495    |
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## INTRODUCTION

The Commission's Annual Report on the Protection of the Community's Financial Interests takes stock of its actions in the fight against fraud. European taxpayers demand that all public money is spent efficiently and in a fraud-proof manner. This goes both for the national and the EU budgets.

For 1997 the budget balance is slightly above ECU 82 billion.

It is financed partly from the Community's traditional own resources. Customs duties and agricultural levies on imports from non-member countries amount to ECU 14 billion or 17%. VAT receipts amount to ECU 35 billion or 42%. The remainder is covered by the fourth resource paid directly by Member States into the budget. This amounts to ECU 32.9 billion or about 40%.

Community expenditure goes to a large extent to agriculture which amounts to ECU 41 billion or 50%. Structural policies amount to ECU 26.6 billion or 32%. The Commission directly manages expenditure such as foreign assistance, research and development, social funds, etc. amounting to ECU 9.7 billion or 12%. The remainder of the budget of about ECU 4.7 billion or less than 6% covers administrative costs in the Commission as well as in the other Institutions (the European Court of Justice, the European Parliament, etc.).

In analysing the figures for detected fraud and irregularities great caution must be observed. First of all the two concepts differ. A precise definition is provided by Community legislation<sup>1</sup>. At the outset it is difficult to establish if a case is a fraud or an irregularity. This requires a criminal investigation which can extend over several years before it can be concluded that there has been a fraud in the strict sense of the term.

Moreover, higher figures for detected fraud and irregularities may be due to improved detection or improved notification of cases or both together. They may reflect an increase in the underlying number of irregularities or a more efficient investigations in certain targeted areas. Also a small number of very significant cases may shift numbers considerably from year to year. Finally an investigation may bring to light a fraud which took place much earlier, while the amounts are counted in the year in which the fraud is quantified.

With these precautions in mind, the main findings on fraud and irregularities for 1997 are as follows:

In the area of traditional own resources, the amounts involved in cases known to the Commission have risen from ECU 796 million in 1996 to ECU 1 billion in 1997. This represents an increase in fraud incidence from 5.8% in '96 to 6.5% in '97. Three times as much money is typically lost by national budgets in the same fraud cases in the form of excise duties and VAT.

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<sup>1</sup> See glossary in annexe.

It is to be recalled that the reporting obligations in own resources were tightened-up in mid-1996. This probably implies a better notification of actual fraud to the Commission. Secondly, the Commission has been called upon more often to deal with sophisticated transnational fraud, in which the Commission has achieved a good track record.

The common agricultural policy and structural policies managed by the Member States account for the bulk of expenditure on the budget. In both those areas detected fraud and irregularities have declined.

In the common agricultural policy guarantee section the reduction amounts to 13%. Detected irregularities and fraud is down from ECU 365 million to ECU 317 million in 1997. In the structural funds detected irregularities and fraud has been reduced by 50%. It is down from ECU 152 million to ECU 77 million in 1997.

Both on the income and on the expenditure side organised crime is defrauding the budget. International criminal networks are targeting highly taxed products (cigarettes or alcohol) agricultural products of high value or with a high world market/internal market price differential (e.g. beef, olive oil, butter) and finally goods from third countries traded under a preferential tariff regime (fisheries, textiles, electronics, motor vehicles).

Experience has shown that a tight co-operation between the Commission's anti-fraud services and Member States allow for efficient investigations into this type of transnational organised crime. The economic weight of these complex cases is rising. While cases dealt with by a Member State alone on average cost ECU 120,000 in fraud or irregularities, a case dealt with by the Commission in co-operation with Member States on average involves ECU 3.7 million. Cases dealt with by the Commission in co-operation with Member States account for 3% of all cases. The volume of detected fraud involved, however, accounts for half the total amount detected.

The dismal recovery record constitutes another major concern highlighted in this Annual Report. In agriculture 65% of money defrauded before 1994 remains unaccounted for. A certain progress has been achieved in 1997. Better procedures have been set up to determine what sums are to be written off, what sums could be recovered or what sums due are to be finally charged to the Member States. And in the area of structural policy new guidelines on net financial adjustments will sharpen financial control with expenditure in Member States. But, more needs to be done to improve recovery.

The report mentions certain improvements in the fight against fraud against the Community budget. Investigations have been intensified and more focused on organised crime. The use of task groups charged with coordinating the investigations in specific sectors has been extended to the alcohol sector; it has led to a number of successes in complex and transnational cases. The Commission has carried out jointly with the Member States the first 'on the spot' checks in the investigation of irregularities at economic operators. Generally, cooperation between the Member States in carrying out these investigation has been improved.

The 1997 Annual Report offers many examples of typical antifraud investigations. Also the various forms of co-operation with Member States and technical assistance are highlighted. A special chapter is devoted to co-operation with third countries. Emphasis is put on the pre-accession strategy towards candidate countries in Central and Eastern



Europe. The objective is to ensure that their capacity to combat fraud and corruption is developed in parallel with their preparations to take part in the common policies.

In the legislative area, the year 1997 has seen the adoption of regulation 515/97 concerning mutual assistance in the customs and agricultural areas. Also the second protocol to the Convention on the protection of financial interests dealing with money laundering and judicial cooperation was signed by ministers. However, the Commission refrained from taking major new legal initiatives in 1997. Rather the full implementation and ratification by Member States of the instruments agreed the years before was expected.

A dual conclusion may be drawn: the first pillar instruments in the form of the regulation on the protection of the financial interests and the regulation on on-the-spot checks are in place and working. The third pillar instruments (conventions and protocols) aiming for an equivalent criminal law protection throughout the Union have not yet been ratified by a single Member State. It is recalled that the Amsterdam European Council set a deadline for ratification by mid-1998.

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## 1. ANALYSES AND STATISTICS

The purpose of this chapter is to present an overview of developments in fraud against the Community budget and detailed analyses of the data available, to give as accurate a picture as possible of the situation on the ground.

### 1.1. The situation in 1997

The number of cases of irregularity or fraud detected in 1997, and the overall impact of such cases on the budget, were once again up on the previous year. In all, 4 939 cases were detected by the Member States and notified to the Commission in 1997. These cases involved a loss of ECU 585 million to the budget. The Commission also launched 223 new investigations in cooperation with the Member States. The overall impact on the budget of cases under investigation by the Commission in 1997 came to an estimated ECU 827 million.<sup>2</sup>

These trends show, firstly, that the fraud prevention systems (especially the notification systems) are steadily becoming more efficient. They also reflect the fact that dismantling complicated organised crime networks is a long-term exercise which can tie the relevant departments down for years. Hence the cyclical fluctuation of varying degrees in the amounts involved from one year to the next.

The fact is that the Member States notify irregularities under the regulations for particular sectors,<sup>3</sup> as soon as the facts have

been established. The notifications quantify the effects on the Community budget, so that recovery procedures can be started.

With cases which the Commission is investigating in cooperation with the Member States, on the other hand, no figures are immediately established, and as a result there is no official notification by the Member States concerned. It is often not possible to make a preliminary estimate of the impact on the budget of cases investigated by the Commission in cooperation with the Member States until the investigations have made substantial headway. The Member States confirm the findings of such investigations by means of an official notification in a subsequent financial year.<sup>4</sup> The figures given for the effect on the budget of investigations of this kind are therefore only estimates or relate to cases opened in previous years.

In the field of traditional own resources, the Member States reported 2 572 cases, involving a total of ECU 364 million. The Commission launched 76 new investigations in cooperation with the Member States: the sums involved (results of the missions of inquiry, whether new or ongoing, carried out in 1997) were estimated at ECU 642 million (see Graph 1). Table 1 contains a breakdown by Member State of the cases notified.

There was a slight increase in the number of cases detected in relation to EAGGF Guarantee Section expenditure, though their impact on the budget was less (down by 13%). The Member States notified 2 058 cases, involving a total of ECU 164 million. The Commission launched 48 fresh investigations; the sums involved (results of the investigations, whether new or ongoing, carried out in 1997) were estimated at ECU 153 million (see Graph 2). Table 2

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<sup>2</sup> This included investigations initiated before 1997 for which a preliminary estimate of the impact on the budget could only be produced on the basis of findings made in 1997.

<sup>3</sup> Council Regulation (EEC) No 1552/89 (OJ L 155, 7.6.1989) as amended by Council Regulation (Euratom, EC) No 1355/96 (OJ L 175, 13.7.1996) as regards own resources; Council Regulation (EEC) No 595/91 (OJ L 67, 14.3.1991) as regards EAGGF Guarantee Section; Council Regulation (EEC) No 4253/88 (OJ L 374, 31.12.1988), Commission Regulations (EC) Nos 1681/94 (Structural Funds, OJ L 178, 12.7.1994) and 1831/94 (Cohesion Fund, OJ L 191, 27.7.1994); Council Regulation (EC) No 515/97 (mutual assistance, OJ L 82, 22.3.1997), previously Council Regulation (EEC) No 1468/81 (OJ L 144, 2.6.1981).

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<sup>4</sup> This applies to all investigations, including those under the mutual assistance arrangement and, in particular, those relating to organised crime.

contains a breakdown by Member State of the cases notified.

The number of cases detected by the Member States or the Commission in cooperation with the Member States in relation to structural operations (Structural Funds and the Cohesion Fund) remained relatively stable, while the sums involved were considerably smaller. In 1997 the Member States notified 309 cases, involving a total of ECU 57 million; the Commission launched 57 investigations, involving ECU 20 million (see Graph 3). Table 3 contains a breakdown by fund and by Member State of the cases notified.

The number of new investigations into direct expenditure (contracts directly administered and monitored by the Commission without the Member States' administration being involved; see Graph 4) remained stable, at 42 cases, while the total amount involved fell (ECU 11 million).

## 1.2. Trends

One must be extremely cautious in trying to compare trends in the numbers of cases detected and their effects on the budget over succeeding years. Complicated cases developing over the course of several financial years may have a major influence on the statistics for any given year. There are, inevitably, fluctuations.<sup>5</sup> We must also be cautious about interpreting the trends in fraud itself since a substantial increase over previous years in the number of cases detected and the amounts involved does not necessarily mean there has been a major change in the real scale of fraud. It may also be a sign that the monitoring systems have become more efficient.

The number of cases detected in 1997 and the amounts involved are confirmation of a tendency for irregularities and fraud to affect own resources more heavily than expenditure.

The average impact on the budget of the cases detected in 1997 was clearly up on previous periods. The average impact of cases notified by the Member States remained comparatively stable, at about ECU 120 000 as against ECU 140 000. The estimated impact of cases under investigation at the Commission in cooperation with the Member States rose from ECU 2.3 million in 1996 to ECU 3.7 million in 1997. However, the average budgetary impact of a case under investigation at the Commission in cooperation with the Member States is not really comparable with that of a case notified by a Member State. A single investigation into a transnational case, coordinated by UCLAF, may cover fraudulent operations in several Member States. Moreover, UCLAF concentrates on the more significant cases in particular those involving organized crime. The budgetary impact of such complex cases is logically greater than it would be for one "typical" case without transnational ramifications.

### 1.2.1. Traditional own resources

Both the number cases and the total amount of money involved as notified by the Member States rose considerably compared with 1996 and 1995.

The entry into force of the amendment to Council Regulation (EEC, Euratom) No 1552/89,<sup>6</sup> which requires the Member States to give more detail in their notifications and establishes the new system of notification by electronic mail, is starting to produce results, and it will now be possible to compare information from different sources more effectively and analyse cases detected more thoroughly.

Although the number of new investigations launched by the Commission in cooperation with the Member States in 1997 was down on the preceding period, the amounts involved (the estimated effect on the budget at the end of 1997) are growing larger, reflecting the fact that the cases concerned

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<sup>5</sup> See the annual report on the "Fight against fraud" for 1995, Chapter 7, section 2, page 68.

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<sup>6</sup> Council Regulation (Euratom, EC) No 1335/96, cited above.

almost exclusively concern organised crime networks.

The cases notified by the Member States in respect of 1997, and the cases under investigation at the Commission in cooperation with the Member States, mostly concern cigarette trafficking. Even so, the figures do not reflect the true scale of fraud involving cigarettes (or, even more so, that of fraud involving alcoholic beverages), as they only represent the impact on the Community budget. The impact on national budgets is several times greater than the loss to the Community budget.<sup>7</sup>

The second major group of products particularly affected by fraud involving traditional own resources is dairy products (butter, milk powder and cheese). These figures are clearly influenced by the impact of a number of very important cases as they have developed over time.<sup>8</sup>

### 1.2.2. Expenditure

The cases detected in the area of EAGGF Guarantee Section expenditure primarily concern measures in the “market support” category.<sup>9</sup> Of all the cases notified by the Member States, these have the largest impact on the budget, accounting for 50% of the overall notified impact in 1997 (71% in 1996). The proportion of the estimated overall impact of cases investigated by UCLAF for which they account rose from 25% in 1996 to 47% in 1997.

Export refunds still occupy an important place, accounting in 1997 for 32% of the sums involved in cases notified by the Member States (as against 21% in 1996).

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<sup>7</sup> The impact on the Community budget in terms of own resources (customs duties and the Community’s share of VAT) represents, on average, only 25% of the total impact on the budget (customs duties, VAT and excise duty).

<sup>8</sup> One single case investigated on the Court of Auditors’ initiative and concerning butter has an overall impact on the budget estimated at ECU 118 million (an assessment based on the findings of the investigation in 1997), of which ECU 24 million was the subject of an official notification by the Member State concerned in 1996.

<sup>9</sup> Particularly expenditure in a common organisation of markets involving quotas and intervention measures.

This trend runs counter to the fact that there was actually a considerable decrease in export refunds. The explanation for this contradiction may be that the investigations conducted by the Commission in cooperation with the Member States mainly concern that category of payments (more than 50% of the overall impact of cases investigated in 1997 as compared with 75% in 1996). The fact is that fraud involving export refunds is usually carried out by organised crime and the resources a Member State by itself can put into dismantling the networks concerned are limited.

Lastly, there has been a steady increase in the effects produced by cases involving direct aid,<sup>10</sup> from 5% of the overall impact of cases notified by the Member States in 1996 to 17% in 1997. This is due to implementation of the reform of the common agricultural policy (CAP) with its tendency to give priority to direct aid for farmers. Cases involving direct aid form a minute proportion of those investigated by the Commission in cooperation with the Member States, due to the fact that such measures are monitored by the Member States, and, what is more, there are very few cases in this sector involving more than one country (e.g. through a single aid recipient operating in a number of Member States).

From 1994 to 1996 there was a major increase in the number of cases notified by the Member States and the overall financial impact in the area of expenditure on structural operations. In 1997 the figures stabilised around the level reached in 1996. Regarding the number of cases notified by the Member States, the European Social Fund is still the worst affected (with 40% of the number of cases). The amounts involved are higher in the case of the ERDF (with nearly 50% of the total).

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<sup>10</sup> In particular, production premia and premia for ceasing production.

### 1.3. Financial monitoring

#### 1.3.1. Recovery

Where the Community budget is harmed, whether the sums involved in a case of irregularity or fraud can actually be recovered depends on a number of factors, particularly the type of infringement, the economic and legal circumstances and the area of the budget involved. Apart from direct expenditure, responsibility for recovery procedures lies with the Member States.

In the area of traditional own resources, the determining factor is the incurring of the customs debt. If an attempt to smuggle goods into the customs territory of the Community is detected in time, the batches of goods seized are usually destroyed or re-exported if the debtor refuses to pay the duties. Smuggling being what it is, it is virtually impossible to collect the evidence needed to recover a debt in relation to goods which have disappeared (having been sold on the black market).

Special problems arise when it comes to recovering sums in cases involving organised crime or other sophisticated types of fraud. Even if the dismantling of an organised crime network means that the quantity of goods already smuggled into and sold on the black market can be "calculated" after the event, it is almost always impossible to identify the person liable for the customs debt and work out exactly how much it is. In such cases recovery in the strict sense of the term is impossible. In other forms of sophisticated fraud, the traders concerned often organise themselves in such a way that only "smokescreen" companies or people who cannot afford to pay the amounts due can be identified. It is therefore vital to attack organised criminal networks in such a way that trafficking is halted at source and criminals are prosecuted.

The situation as regards recovery in the cases notified by the Member States in relation to 1997 in the area of traditional own resources is shown in Table 1. It is not, on the other hand, possible at this stage to quantify the amounts still to be recovered in the cases of

irregularity and fraud notified under previous financial years. This is because until July 1996, when Council Regulation (Euratom, EC) No 1355/96 took effect, the relevant authorities in the Member States who are supposed to instigate the recovery procedures relating to traditional own resources were not officially required to supply the Commission with detailed information about financial monitoring.

In July 1997 the Commission proposed an amendment to Council Regulation (EEC, Euratom) No 1552/89 designed to clarify the situations in which the Member States bear a financial responsibility.<sup>11</sup> This will provide more effective protection for the Community's financial interests since it involves setting up a transparent, formalised procedure for determining the sums not recovered for which an exemption from making them available may be granted and those which have not been recovered for reasons attributable to the Member State which henceforth justifies making the latter financially responsible. In October the Court of Auditors gave its opinion on the Commission's proposal.<sup>12</sup> In February 1998 the European Parliament adapted an amended version of the draft.

With regard to EAGGF Guarantee Section expenditure, Table 2 shows progress with recovery in the cases notified in respect of 1997. Three quarters of the amount involved (ECU 122 million out of 164 million) have yet to be recovered. The main problem is still the time taken by recovery procedures. The Commission thinks that four years can be regarded as long enough for determining whether there is a realistic prospect of recovering sums due and, where appropriate, launching the requisite procedures. This time limit allows for the limitation period and takes account of the new accelerated accounts clearance procedure.<sup>13</sup> By the time

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<sup>11</sup> COM(97)343 final.

<sup>12</sup> OJ C 15, 19.1.1998.

<sup>13</sup> Commission Regulation (EC) No 1663/95 (OJ L 158, 7.7.1995) laying down detailed rules for the application of Council Regulation (EEC) No 729/70 (OJ L 94, 28.4.1970) regarding the procedure for the clearance of the accounts of the EAGGF Guarantee Section.

the four-year period expires, the Commission should be in a position to take a decision as part of the clearance of accounts procedure, based on the explanations supplied by the Member State concerned.<sup>14</sup> Table 4 shows the position as regards recovery in cases notified before 1994.

Similarly, as part of the clearance of accounts procedure, the Commission may apply flat-rate adjustments to Member States which have not established adequate checks and have thereby created a risk of irregularities. This is not a “recovery” in the strict sense but another way of protecting the financial interests of the Communities. Such adjustments are an effective inducement to the Member States to tighten up their monitoring systems. Flat-rate adjustments for 1993 came to some ECU 520 million.

Structural measures are financed by instalments as part of multiannual programmes. If an irregularity involving one of the individual projects selected by the relevant authorities in the Member States and in receipt of Community co-financing is detected before the multiannual programme in question ceases to apply, the Member State concerned may usually withdraw the project and replace it with another which also meets the set objectives. The Community’s financial contribution may therefore be “reprogrammed”. In addition, payment by instalments is often a way of reacting to an established irregularity in financial terms before the final payment is made. The balance to be recovered can therefore only be accurately calculated after the multiannual programme has ended.

The Madrid European Council in December 1995 called on the Commission and the Council to look into the possibility of extending the accounts clearance procedure used for EAGGF Guarantee Section expenditure to other sectors, particularly the Structural Funds. On 27 October the

Commission accordingly sent the Member States’ Permanent Representatives the internal guidelines on net financial adjustments pursuant to Article 24 of Regulation (EEC) No 4253/88 and instructed its responsible departments to apply them. These guidelines set out the circumstances in which net financial adjustments have to be made. The main proposed criterion is that a net adjustment must be made if financial control in the Member States leaves major loopholes.

While recovery in the three budgetary areas referred to above is the responsibility of the member States, where direct expenditure is concerned the Commission itself, once it has conducted its investigation, recovers the amounts due from the end-recipient. The relevant authorising department issues a recovery order which is executed by the Commission Accountant. But there is no denying that the actual recovery of the amounts in question frequently runs into material or legal difficulties (such as the recipient going bankrupt or procedures before national courts taking a very long time).

### *1.3.2. Monitoring of investigations run by UCLAF in cooperation with the Member States*

Systematic financial monitoring of recovery procedures can only be done on the basis of official notifications from the Member States. Obviously, in the event of sophisticated transnational fraud, the Member States acting alone cannot bring the case to a close and recover the sums due, even in part (particularly in the areas of traditional own resources and agricultural expenditure, where goods are traded and it is difficult to identify who is liable to pay).

Even if an investigation by the Commission enables a figure to be put on the effect on the Community budget (in terms of own resources evaded or irregular expenditure) and the debtor or the end-recipient to be identified, UCLAF has to send the Member State concerned all the facts in the case and ask it to take whatever action is necessary to

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<sup>14</sup> Most recently, Commission Decision 97/333/EC of 23 April 1997 on the clearance of the accounts presented by the Member States in respect of the expenditure for 1993 on the EAGGF Guarantee Section (OJ L 139, 30.5.1997).

recover the amount due, including notifying the case officially if it has not been done.

In the area of own resources, Council Regulation (Euratom, EC) No 1355/96 amending Council Regulation (EEDC, Euratom) No 1552/89 introduced a requirement for the Member States, in their

## 2. INVESTIGATIONS

The chapter on investigations is a sign of the priority the Union gives to stepping up its operational presence in the field, that in fact being one of the mainstays of the Commission's strategy for combating fraud, supported by the European Parliament and the Council.<sup>15</sup>

The aims are clear-cut: to combat organised crime, while maintaining the credibility of the Union's basic policies and protecting the Community's finances.

Where organised crime is concerned<sup>16</sup>, the Community budget is a major target for organisations specialising in financial crime. Whenever our investigations have turned up complicated, usually international, operations involving large amounts of money, criminal networks using sophisticated techniques are found to be involved. Fraudulent operators, corruptors and counterfeiters of documents, are experts at diverting or switching goods, managing complicated flows of false invoices, moving capital to "front" companies and using bogus administrative documents. The Commission and the Member States have good reasons for running large-scale investigations in the field leading to penalties which deter fraudulent operators.

The Commission also has a duty to take firm action to protect the major Community policies. Whether it be the agricultural policy, the structural policy or the trade policy, what is at stake is the very credibility of the Union.

own resources notifications, to refer explicitly to any previous notification within the mutual assistance system for customs and agricultural matters. As UCLAF organises cooperation with the Member States within the mutual assistance framework, these references will make monitoring in future more systematic.

The malfunctioning of the preferential arrangements illustrates the risks which systematic fraud could pose to a dynamic trade policy open to the rest of the world. There are preferential tariffs on half the Union's imports.<sup>17</sup> Major risks remain, particularly in certain sectors such as fisheries, textiles and electronics or in relation to certain products subject to trade protection measures such as anti-dumping duties.

Within the Union fraud must not be allowed to undermine operations as fundamental as the agricultural or structural policies. The Commission is doing its job when it carries out investigations in the field into cases which are often complicated and spill over into several Member States or non-member countries, or when it coordinates the work done by national fraud-prevention departments.

In the area of VAT fraud, which raises a series of questions related to those raised by the taxation of high-risk products, further action needs to be taken to ensure that coordinated investigations are also developed.

### 2.1. Involvement of organised crime

It has been established beyond doubt that international crime syndicates target the Community budget. More than 50 crime networks have been identified in the course of large-scale investigations which have revealed the attacks being made on Community expenditure and revenue. The

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<sup>15</sup> COM(94)92 final.

<sup>16</sup> See glossary in annexe.

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<sup>17</sup> As the Court of Auditors noted in its annual report on the financial year 1996 (OJ C 348, 18.11.1997).

networks work with each other and are involved in other criminal activities as well as financial crime against the Community's finances. Organised crime has its sights trained on high-risk products in which trafficking brings in huge profits, such as alcohol and cigarettes: customs duties are evaded at the expense of the Community's financial interests, while excise duty and VAT are evaded primarily at the expense of national finances. In agriculture, investigations by the specialist national departments and the Commission more and more often uncover evidence of involvement by organised, international crime networks.

As the high-level group mandated by the Council in 1997 has emphasised, organised crime syndicates take advantage of the differences between national systems to operate with impunity and, where necessary, rely on non-member countries (Switzerland or tax havens) which shelter the real organisers behind the networks and launder the money siphoned off from the common budget.

Substantial results can be achieved, however, provided the national and Community authorities work together from the moment the investigations begin until any legal consequences which may ensue. The work of the task-groups on alcohol, cigarettes and olive oil specially set up on a Commission initiative so that the Commission and the Member States can keep track of the most sensitive cases has been stepped up.

#### *2.1.1. The work of the task-group on cigarettes*

Investigations coordinated by the Commission by the task-group on which UCLAF and the specialist departments in the Member States are represented have shown that organised crime syndicates are heavily involved in Europe and throughout the world. They adapt extremely well to the measures adopted to combat their activities and are very flexible, both geographically and operationally, when it comes to using different methods of transport and different distribution and money-laundering networks. Crime syndicates can only be fought by

seamless operational cooperation between the Member States, with help from the Commission and working closely with the judicial authorities.

In 1997 joint action and help from certain non-member countries led to the uncovering and prevention of certain types of trafficking; the main syndicates involved are described in this part. The overall financial impact of the kinds of fraud detected in this area in 1997 is estimated at ECU 1.6 billion, covering Community own resources and national revenue (customs and excise duties and VAT). The loss of Community receipts was estimated at ECU 423 million. Because of the scale of indirect taxation, particularly excise duty, such fraud goes on all over the Union, though it is traditionally more prominent in southern Europe.

##### 2.1.1.1. Sea and air trafficking

The Commission and the task-group on cigarettes set up an operation to combat the traffic in cigarettes by sea off Spain and Portugal.<sup>18</sup>

The cigarettes were first shipped from warehouses at ports in Benelux on board vessels declared as being bound for West Africa, and were then transhipped by sea. In January 1997, the operation coordinated by the Commission led for the first time to the seizing of two vessels. The operation continued throughout 1997, and several vessels involved were seized by the Spanish and Portuguese authorities in collaboration with their opposite numbers in France and Belgium.

One consequence of the seizures was that it prompted the crime networks to move the warehousing operation from Benelux ports to other ports, particularly in Cyprus. The way the fraud operated was changed, and now involved making a false declaration as to the type and actual origin (Morocco) of the goods. The cigarettes were now moved through ports in Cyprus or other non-member countries in the Mediterranean,

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<sup>18</sup> See the annual report on the "Fight against fraud" for 1996, Chapter 3, Section 1.1, page 27.



where they were loaded with other, less sensitive goods into containers which, when they entered the European Union, were declared as containing only the less sensitive goods, to escape the notice of the inspection authorities.

The Commission coordinated the information about the movements of these containers and more than 93 000 cases of cigarettes<sup>19</sup> were seized by the Member States' authorities. The outstanding help the Community received from the Cypriot authorities was highly appreciated. The trafficking of cigarettes to Spain and Portugal by sea has been dealt a serious blow. Arrests have been made in Spain, France and Belgium, leading to the dismantling of crime networks, whose members are now being prosecuted.

The crime syndicates then thought up other ways to go on supplying the black market in Europe. In April 1997 the task-group, working with the Spanish and Greek authorities, heard that a cargo plane belonging to the Ukrainian armed forces and coming from Greece was landing at an airport in northern Spain and unloading a cargo under a false declaration (as electrical spare parts sent from Greece).

The operation led to the seizure of an Ilyushin 76 aircraft and the arrest of its crew by the Spanish authorities. The aeroplane was then seized and the members of the crew convicted in the criminal courts. The cargo, which was concealed in wooden crates, contained more than 1700 cases of cigarettes. Further investigations showed that the intercepted flight had been the seventh of its kind since February, and six more flights were scheduled before the end of April. The cigarettes came from a large warehouse in the Netherlands, were loaded at Ostend Airport in Belgium, for Belgrade, and were then carried from airports in Greece, where the aircraft in fact only stopped to refuel.

It was established that more than 17 760 cases of cigarettes had been brought into Spain fraudulently as described above. The

estimated loss in terms of customs duties, VAT and indirect contributions was ECU 15 million. According to the Ukrainian Government, the seized aircraft was on hire from a Ukrainian company. The authorities nevertheless refused to cooperate in clearing up the case, despite the agreement with the Community (in force since 1996) which provides a legal basis for mutual assistance in customs matters.

#### 2.1.1.2. Cigarette trafficking under cover of TIR carnets

A crime syndicate based in Switzerland and regarded as the main supplier of cigarettes to the networks in the Community was proposing to smuggle some 175 000 cases of brand-name cigarettes from Romania into the Community. The fraudulent operations started at the beginning of 1996.

The cigarettes, which were first sent by road and by air from a customs warehouse in the Netherlands through Belgium to Bucharest in Romania, were brought back into the Community after being transported from Bucharest to the Hungarian border under Romanian transit arrangements. The criminals then declared the cigarettes as low-risk goods (crocery) and placed them under TIR arrangements,<sup>20</sup> under which they were carried back into the Community. The TIR carnets were falsely cleared and the cigarettes placed on the Community market.

The trafficking was brought to a halt in November 1996 when two of the TIR carnets were found in the hands of one of the main organisers of the fraud in the course of a criminal investigation in Switzerland into another case (drug trafficking and corruption of Swiss officials).

The investigation departments of three Member States were sent the information, which implicated several haulage companies. But it was difficult to carry their investigations through as there was no evidence of the scale of the fraudulent operations or the level of responsibility borne

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<sup>19</sup> A case contains 50 cartons, i.e. 10 000 cigarettes.

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<sup>20</sup> TIR is the international transport arrangement laid down by the 1975 TIR Convention.

by the companies and individuals concerned. At the request of these Member States, the Commission's fraud-prevention department undertook to coordinate the investigations.

A Community mission was set up in collaboration with the Romanian customs authorities. It found enough evidence for the national investigating departments in the Member States and Romania to be able to institute criminal proceedings. The outcome was that several criminals were jailed and the debtors were notified of the amounts of import duty evaded. Of the projected total of 175 000 cases, 35 000 had already been smuggled into the Community, representing approximately ECU 38 million (customs and excise duties and VAT) in lost revenue.

#### 2.1.1.3. Cigarette trafficking from Montenegro

One of the main routes the crime syndicates use for trafficking cigarettes to the Community is through the Federal Republic of Yugoslavia, where large quantities of cigarettes are sent in transit by air, road or sea from customs warehouses in the Community and Switzerland. The cigarettes are then loaded onto speedboats declared to be bound for Italy and are offloaded on the Adriatic coast as contraband.

This is a substantial operation: more than 100 cargo plane flights to Montenegro were identified in 1997. Investigations in the same year confirmed the figures from an initial mission in 1996 for the very high level of trafficking taking place, involving some 800 000 cases per year, or a loss of at least ECU 700 million in Community and national resources per year.

The investigations showed that 678 250 cases of cigarettes were carried from the European Union and non-member countries to Montenegro in the first nine months of 1997. The sole purpose of taking the cigarettes through Montenegro is to divert them to the black market in the EU. With an estimated 10% of these cigarettes earmarked for the local market, it can be deduced that about 610 000 cases of cigarettes are intended for the black market in the EU,

representing a loss of some ECU 610 million in customs and excise duty and VAT.

A mission organised by UCLAF and the Guardia di Finanza in cooperation with the Italian legal authorities laid hands on documents and other evidence showing that 31 665 cases had been brought into the European Union irregularly. With the documents obtained in a subsequent mission, the Italian police were able to bring charges against 42 people linked to crime syndicates and involved in cigarette trafficking.

#### 2.1.1.4. Cigarette trafficking by rail

Because of the measures planned in relation to Community/common transit,<sup>21</sup> particularly the requirement for an individual guarantee for cigarettes carried by road, the crime syndicates are exploiting the weak points of other methods of transport. For example, 77 410 cases of cigarettes carried by rail from Switzerland to Portugal between February 1995 and April 1997 were smuggled into the Community, representing a loss of some ECU 65 million in Community own resources and national revenue.

The cigarettes in question, which were of American origin, were sent from warehouses in the Netherlands, Germany and Belgium to warehouses in Basle and Buchs in Switzerland. There the cigarettes were declared for export to destinations outside the Union, bound for Angola, Senegal, Gambia and Guinea via Portugal, where they were fraudulently taken off the trucks and removed from the Community/common transit arrangements. This traffic was stopped in April when the Portuguese authorities seized the 70th truck in this particular operation.

Investigations by the judicial authorities are under way in Portugal to identify those

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<sup>21</sup> Arrangement for movement of goods under duty- and tax-suspension arrangements from an office of departure to an office of destination by way of a document-checking procedure (the common transit arrangement is an extension of the Community transit arrangement to the EFTA countries and the Visegrad countries – Poland, Hungary, the Czech Republic and Slovakia). Cf. Chapter 3, section 3.3.

responsible for the fraud. UCLAF coordinated a mission to Switzerland under the mutual assistance agreement with that country. Even though loopholes have come to light in implementing the agreement, particularly as regards the responsibilities of the Swiss authorities, the results of the mission at this stage show that the organisations involved in the fraud are known from other cigarette smuggling cases.

#### 2.1.1.5. Trafficking from Andorra

For several years now Andorra has been one of the sources of cigarettes smuggled into the European Union, particularly Spain. The cigarettes used to be either manufactured under licence in Andorra or manufactured in non-member countries and imported into Andorra.

In 1995-97, however, the operations began to take place on a very large scale. Large quantities of cigarettes smuggled out of Andorra were seized by the Spanish, French, British and Irish authorities.

Thorough analysis of the tobacco products imported into and manufactured in Andorra showed that the quantities concerned were very much in excess of the requirements for local consumption and duty-free sales to tourists. Officially, however, Andorra does not export cigarettes.

In 1997 it was found that twice as many cigarettes had been imported into Andorra as in 1996, while the quantities of cigarettes manufactured in Andorra had risen slightly over the five preceding years. The brands of cigarettes imported into Andorra in 1997 suggested that a large part of them was intended for the British and Irish contraband market, which is run by crime syndicates.

The total tax receipt loss was estimated at some ECU 200 million in 1996 and ECU 400 million in 1997. There is solid evidence to show that the traffic is being carried on by organised criminal gangs based in various countries inside and outside the European Union.

Various steps have been taken by the Spanish authorities (the Guardia Civil) and

tougher police and customs control should put a halt to this type of operation. The relevant departments in the Commission and the Andorran authorities are discussing what action to take.

#### 2.1.2. *The role of organised crime in agricultural fraud*

Investigations into the agriculture sector frequently uncover well-organised crime networks. Organised crime is particularly involved in the extra-Community trade in agricultural products, through complex networks of producers, dealers, carriers, invoice clerks, smugglers, counterfeiters and so on.

The cases involving alcohol, olive oil, butter, beef and veal referred to above are good illustrations of the kind of crime the Community is faced with. The British beef example shows that as well as an attack on the Community's financial interests there may be circumvention of the bans imposed by the Community to protect public health.

##### 2.1.2.1. Alcohol

At the end of 1996, the investigations into alcohol and alcoholic beverages (except wine) under way in UCLAF<sup>22</sup> were brought together under a task-group on alcohol responsible for gathering the available information together in one place and coordinating fraud-prevention activities, which are inevitably international. The group is able to initiate investigations and exercise operational supervision over them. The early warning system (transit system) and the coordination of investigations by a special task group have proved useful tools in fraud detection. Experience also shows that it is in the interests of all the Member States to cooperate with each other and with the Commission: the problems fully identified in 1997 cannot easily be confined just to the

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<sup>22</sup> See the annual report on the "Fight against fraud" for 1996, which reported, in Chapter 3, Section 3.1.1, p. 27, that the Member States had told the Commission on several occasions that there had been an upsurge in alcohol smuggling.

Member States which have worked with the Commission.

What is more, the principal instances of fraud are carried out by well-organised criminals. They can only be fought by constantly upgrading the exchange of information and cooperation between the Member States and the Commission.

In 1997 the task group launched investigations into movements of alcohol and alcoholic beverages either under the Community external transit system<sup>23</sup> or under excise - duty - suspension arrangements.<sup>24</sup> Investigations showed that both systems had been used fraudulently. Large amounts of alcohol and alcoholic beverages disappeared while being transported across the Community. The fraud methods used include using forged documents and stamps, giving false descriptions of goods or specifying false companies as the declared consignees, and setting up “front” companies which go bankrupt before duties fall due.

It is very difficult in most cases to discover what the end-destination of the alcohol is, either because it has not left the Member State of departure at all or because it has left that Member State but not the Community (which involves it simply being diverted onto the market in another Member State or exported but then smuggled back into the Community), or because it has left the Community and then been put on the market illegally in non-member countries, particularly in central and eastern Europe.

Inside the Union a great deal of the trafficking goes on in northern Europe, where excise duty is higher. Very obviously, it is in the shared interest of the Community and

non-member countries, particularly those of central and eastern Europe, to prevent fraud on their respective markets and contain organised crime.

- Consignments under the Community transit customs arrangement

Because of the information passed on by the Member States in 1997 about exports of sensitive products, the investigation was targeted on two Member States which export large quantities to declared destinations in the former Soviet Union (particularly Russia, Ukraine and Lithuania).

It was thus established that at least 1.4 million litres allegedly exported from one of these two Member States had not reached the declared destination. The customs documents had not been produced at customs offices on the way out of the Community, or had been stamped using forged stamps.

If, as seems likely, the quantity involved did not in fact leave the customs territory of the Community, the financial impact, assessed on the basis of average taxation in the European Union, and including customs duty, would come to about ECU 15.7 million. The investigation is continuing in order to determine both where the products concerned went and what happened to another 4.4 million litres of exports bound for countries in the former Soviet Union (with a potential impact of some ECU 49 million).

- Consignments under the excise-duty-suspension arrangement

Thanks to outstanding cooperation from one Member State, it was possible to analyse movements of alcohol under the excise-duty-suspension arrangement and show that, over a period of a little over a year, nine companies evaded payment of excise duty and VAT by means of fictitious exports of 6.7 million litres of alcohol.

The customs authorities also uncovered irregular dispatches of 14.3 million litres by another eight companies over a period of less than three years. The estimated potential loss of national revenue (based on average

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<sup>23</sup> Consignments covered by a T1 document.

<sup>24</sup> Consignments under an accompanying administrative document. Council Directive No 92/12/EEC of 25.2.1992 on the general arrangements for products subject to excise duty and on the holding, movement and monitoring of such products (OJ L 76, 23.3.1992), and Commission Regulation (EEC) No 2719/92 on the accompanying administrative document for the movement under duty-suspension arrangements of products subject to excise duty (OJ L 276, 19.9.1992).

taxation in the European Union) would be some ECU 563 million.

#### 2.1.2.2. Olive oil

Investigations in this field show how sophisticated the techniques used by crime syndicates are. To achieve their aims they set up mechanisms which distort the economy in a particular sector. The idea that there is a type of fraud which works to the advantage of one sector is mistaken: here, producers, processors and consumers are the victims of a concerted operation. Large-scale fraud has been taking place in the olive oil sector in relation to both consumption aid and production aid. Import and export operations have also been subject to fraud. The Commission took this problem into account in the proposals which it put forward for the reform of the common organisation of this market.<sup>25</sup>

The cases involving olive oil are a good illustration of the usefulness of a structure like the specialised task group, not just conducting one-off investigations but, as an ongoing exercise, coordinating research departments which have to deal with organised financial crime operating in several countries and in a variety of ways.

- Olive oil adulterated with hazelnut oil

It emerged during 1995 that sizeable quantities of oil cleared through customs as sunflower oil had been dispatched to Belgium, Netherlands, Germany and Portugal on board ships from Turkey. Fraud was suspected: it could have been hazelnut oil intended for mixing with olive oil, as that type of adulteration is very difficult to detect if the amount of hazelnut oil mixed in does not exceed 18% or 20%. Oil adulterated in that way loses its quality and is no longer entitled to any form of Community aid.

Having the oil cleared through customs in various ports in Northern Europe and Portugal diverted attention, as did declaring it as sunflower oil - and, incidentally, thereby

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<sup>25</sup> COM(97)57 final.

side-stepping the requirement to provide a security for the importation of hazelnut oil.<sup>26</sup>

After repeated cross-charging via companies established in tax havens (Panama and others) and holders of Swiss bank accounts, the oil was taken to Italy and Spain on lorries, usually French.

An investigation which the Commission carried out in Turkey in 1995 in association with the customs departments of the Member States concerned found evidence that the vessels had indeed been loaded with hazelnut oil. The documents produced on arrival in the Community were forged documents concocted during the journey. The false declarations of type and value related to a total of 20 680 tonnes of hazelnut oil.

The French, Belgian and Dutch customs investigation departments investigated the carriers and identified the end-consignees of the goods. At each stage of the investigation UCLAF, through the olive oil task group, coordinated the inquiries by the specialist departments from the Member States concerned.

The loss to European consumers who bought olive oil adulterated with hazelnut oil can be put at ECU 40 million, allowing for the fact that hazelnut oil was three times as cheap as olive oil on the world market at the time. The loss to Community finances was ECU 30 million through the failure to provide the security required for hazelnut oil (involving 16 145 tonnes), plus large sums improperly collected in consumption aid totalling ECU 43 million, if we consider that the 20 680 tonnes of hazelnut oil were mixed with the olive oil to make up 20% of the total, thereby enabling 103 400 tonnes of adulterated olive oil to be placed on the market. Recovery procedures and legal proceedings are under way in these cases.

- Fraudulent importing of olive oil

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<sup>26</sup> A security of ECU 800 per 100 kg, released on certain conditions of use, is required by the regulation to reduce the risk of fraud involving hazelnut oil. Cf. Commission Regulation (EEC) No 2828/93 (OJ L 258, 16.10.1993).

A joint inspection carried out in Greece in connection with developments in an earlier case involving fraudulent importing of olive oil into Italy<sup>27</sup> found evidence in a ship's log of another fraudulent operation set up by the same crime syndicate. An investigation by UCLAF in collaboration with the Italian Guardia di Finanza and the French customs investigation department uncovered a complicated operation involving fraudulent importing of olive oil without payment of customs duties.

The olive oil, which came from a non-member country, was claimed to be in transit for Israel and Turkey. It was in fact unloaded on the customs territory of the Community by means of an ingenious subterfuge. Two ships sailed from Marseilles and Sète in France, each carrying 1700 tonnes of olive oil in transit and 1700 tonnes of French sunflower oil. They called at Monopoli in Italy, allegedly in order to unload the sunflower oil. They then set off again for Turkey and Israel with the olive oil (with supporting manifests and bills of lading).

The investigation proved that it was the olive oil which was in fact unloaded in Italy and the sunflower oil which was cleared through customs in Turkey and Israel, the papers being altered *en route*.

The 3400 tonnes booked in the Italian consignee's accounts as sunflower oil were then re-established as olive oil: a set of false invoices was issued with the connivance of other companies to establish that the company concerned had sold the sunflower oil and bought the same tonnage of olive oil. To complete the fiction, carriage invoices had been issued, with lorries actually moving about (and thereby justifying purchases of fuel) but empty!

The investigation showed that all the invoices were bogus and that no goods had ever been physically moved. The only purpose of the

whole set-up was to justify the presence of olive oil surreptitiously unloaded at the consignee's premises, when the two vessels had been officially declared as carrying sunflower oil.

The amount involved in this case, in terms of evaded customs duty and securities which were not lodged, came to ECU 5.1 million. Consumption aid which was drawn without entitlement came to ECU 1.83 million. Legal proceedings have been instigated.

Uncovering the mechanisms in this particular instance of fraud took several years of research, as there were a great many people involved in the organised crime network which carried it out: three companies (French, Swiss and British), all run by an international dealer and producer based in the UK, with the connivance of the manager and captains of the ships involved and from a well-organised Italian network consisting of officials from a great many trading and transport companies.

#### 2.1.2.3. Butter

In October 1996 the Commission was told by the Belgian authorities that a dairy products firm was suspected of involvement in bogus exports of butter to Albania through an Italian trader. The Belgian firm was getting export refunds. Under the responsibility of the trader in Italy, the product was placed under the transit arrangements and then earmarked for export from Bari to Albania.

Close cooperation between the Commission and the relevant national administration led to the seizure of the butter consignments in Italy, while the carriers were caught in the act of unloading the lorries in private warehouses.

An investigation by the fraud-prevention departments in Belgium and Italy showed that 15 consignments intended for Albania had been improperly withdrawn from transit using falsified Community transit documents and then diverted to the Italian market between July and November 1996. Once the fraud had been identified, the Italian trader was charged before the Italian courts with fraud against the Community budget.

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<sup>27</sup> See the annual report for 1993 on the "Fight against fraud", p. 27. The case in question came to trial recently; the Community's finances were defrauded of ECU 27.6 million.

Shortly afterwards the Commission discovered that between January and April 1997 the same trader had bought 13 consignments of butter intended for Albania from a French exporter. A fresh investigation was set up, ending in the arrest of the trader in Italy on charges of smuggling and conspiring to defraud the Community budget with the French exporter.

After this case, a third instance of fraud was discovered, in which the same Italian trader had first exported French butter to Croatia and then brought it back into the Community fraudulently, declaring it as margarine.

These three cases, in which the amounts to be recovered come to ECU 1 million, have uncovered a crime syndicate involving exporters and traders in Belgium, France and Italy and designed to defraud the Community budget. Commission departments coordinated and steered the investigations and thereby helped to stamp a crime syndicate out at an early stage, before it could take advantage of Community aid. The Commission received exemplary assistance in this case from the national departments responsible (the Guardia di Finanza in Italy, the Belgian customs and the customs investigations department in France) and the judicial authorities responsible for prosecuting crime.

#### 2.1.2.4. Infringement of the embargo on British beef

On 27 March 1996, as a precautionary measure against bovine spongiform encephalitis, the Commission decided to ban all exports to the Member States and non-member countries of live cattle from the UK and of various products obtained from cattle slaughtered in the UK.<sup>28</sup> The Commission worked with the Member States to obtain information about any infringements. Suspicion fell on a Belgian crime syndicate already well-known for its involvement in the unlawful traffic in hormones or other types of agricultural fraud.

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<sup>28</sup> Commission Decision 96/239/EC (OJ L 78, 28.3.1996), amended by Commission Decision 96/362/EC (OJ L 139, 12.6.1996).

In April 1997 Dutch customs found a UK health label in a consignment of frozen beef which had allegedly come from two Belgian establishments. After thorough checks, several UK marks were found. The principal organiser of the fraud was a Belgian company linked to a British firm which bought and processed British beef in a cold store in the UK.

The fraud involved removing animal health marks saying "UK" and packing the meat in cases bearing bogus Belgian health labels. Carriage to the Continent by lorry and ferry was done under cover of false papers claiming that it was Belgian meat which had been taken to the UK and sent back.

The meat was then stored in the Netherlands and sold to a French company, by the Belgian company which organised the fraud, as meat of Belgian origin. The meat was then exported by the French company, export refunds being paid in the Netherlands to a total value of ECU 1 074 000.

Subsequently French and Irish health labels were also found in the same cold store in the UK. Another fraud on the lines of that described above was uncovered. At the end of July the French customs physically inspected goods on a lorry coming from Northern Ireland (20 tonnes of beef) and identified a "UK" mark on the meat. The consignment, which was on its way to a German company, was seized. The Commission was notified of these findings in the middle of August, and the report was passed on to the German, Irish and British authorities.

The German authorities then established that between August 1996 and August 1997 the German firm had bought 1277 tonnes of beef declared as being from Ireland, with falsified Irish health certificates and transport documents. The meat was then either exported as Irish beef by the German purchaser, with refunds being paid, or sold on to another German firm as beef with German health certificates (and then exported with refunds paid or sold on the internal German market). The amount to be recovered in Germany comes to ECU 1.3 million.

Lastly, after the investigations in Germany, the authorities uncovered a similar scheme (UK beef with the health marks cut off by a company based in Northern Ireland) involving four Dutch and Belgian companies and some 2000 tonnes of beef.

In connection with the investigations into the illegal trade in beef, the Commission twice applied Council Regulation (Euratom, EC) No 2185/96 concerning on-the-spot checks and inspections carried out by the Commission in order to protect the European Communities' financial interests against fraud and other irregularities.<sup>29</sup>

The investigations into the beef and veal industry showed that suspicions of fraud in relation to agriculture also need to be notified, both under the mutual assistance regulations and so that offenders can be put on the agricultural black list set up by Council and Commission Regulations.<sup>30</sup>

In all the cases mentioned which are now being dealt with by the judicial authorities, UCLAF coordinated the investigations and organised all the relevant meetings with the various authorities responsible in the Member States concerned. When authorities are faced with this kind of fraud involving an organised crime network, there has to be such coordination, including when on-the-spot visits are made to traders' premises.

## **2.2. Fraud: an assault on the Community's policies**

There is a political price to pay for fraud against the Community budget as well as the financial impact. Not only do the accounting losses add up, it also poses a direct threat to the credibility of the Community's policies, whether it be the external trade policy, the agricultural or structural policy or internal or external operations financed by direct expenditure.

### *2.2.1. Own resources: assaults on the Community's trade policy*

The investigations in 1997 have helped to shed a great deal of light in the current debate about the management of the tariff arrangements which are one of the Community's main operational instruments in promoting its external policy. The Commission's communication on this subject<sup>31</sup> reviews the shortcomings in the operation of the arrangements which have come to light during investigations in the field and sets out an action programme aimed at reducing the instances of fraud which represents a threat to the very existence of these arrangements.

These shortcomings should not obscure the primary aims of the system, which are to help the recipient countries develop, to encourage cooperation with the partner countries and to prepare for the incorporation of countries which have applied for membership.

The object of the communication referred to above is to reconcile two objectives which are by no means contradictory: the first is to facilitate trade by giving preference only to products from partner or beneficiary countries, and the second is to combat fraudulent exploitation of the arrangements so that tariff preference is granted only on goods from countries which are the intended beneficiaries.

Preferential treatment is given only to goods from beneficiary countries where they have been obtained in their entirety or processed to a sufficient degree. The goods must then have been brought to the Community directly with special certificates<sup>32</sup> showing that they were obtained on the required terms. There are also cumulation rules applying to goods produced using products from two, three or more partner countries (or two or more countries belonging to a regional grouping).

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<sup>29</sup> OJ L 292, 15.11.1996. See Chapter 5, section 5.1.

<sup>30</sup> See Chapter 3, section 3.2.

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<sup>31</sup> COM(97)402 final, 23.7.1997.

<sup>32</sup> The beneficiary countries are responsible for granting certificates of origin (system based on cooperation and trust).



There are a great many weaknesses, despite there being a system for administrative cooperation between the Community and each of the partner countries. The types of irregularity or fraud found relate to the most sensitive products, reflecting specialisation in the exporting industries of the beneficiary countries (electronic products, fisheries and textiles primarily), and involve the production of certificates which are not in the due form or are actually authentic but relate to a product which is not covered by the agreement or arrangement (these are the easiest to detect), or have been issued in respect of products not obtained in the beneficiary countries (or even obtained in the beneficiary country without complying with the rules of origin).

The responsibility borne by traders outside the Community is obvious. They are in a position to know whether the products they make comply with the rules of origin or not. By supplying Community importers with certificates of origin for products which are not eligible, they give them a way of evading payment of the customs duties which would normally be payable. The Community importers concerned are also supposed to be familiar with the rules of origin. If they produce a certificate of origin with an import declaration, they are liable for any duty payable on the import.<sup>33</sup>

The other major category of fraud involving the rules of origin sets out not just to secure tariff advantages but to get round market protection measures such as the anti-dumping provisions or the measures imposing all-out bans adopted under the Union's policy on the environment.

In all these instances, the Community's interests (which are financial, commercial and sometimes also wider in scope, as the case of products which destroy the ozone

layer shows) can only be protected by coordinating the work of the Member States and the beneficiary countries, with help from the Commission.

This applies both to the prevention stage, when the terms for granting trading advantages are being studied, and to the suppression stage, when traders who behave improperly have to be thwarted and sanctioned. Such traders not only encroach on the Community's financial interests, they actually distort trade in ways which cannot be tolerated, penalising fair traders and non-member countries which meet their obligations and cooperate with the Community in the interests of proper implementation of the preferential arrangements.

#### 2.2.1.1. Fisheries

Applying the preference rules to fisheries, where customs duties are comparatively high and the rules of origin difficult to police, still creates problems. One example of a clever kind of fraud is the case of the shrimps from Surinam.

As far back as 1995 the Commission found out that there were suspicions of fraud in relation to tariff preferences. There was a likelihood that frozen shrimp on board Japanese vessels were being imported into the Netherlands with certificates of origin from Surinam.

Research showed that fleets flying the flags of a number of countries (Korea, Honduras, Japan, Vanuatu and others) were operating off Surinam. Shrimp landed from the boats appeared to be getting some superficial form of treatment before being exported to the Community. The Member States were told there was a suspicion of false declarations of preferential origin. A mission to Vanuatu in August 1996 also found evidence that vessels flying that country's flag and operating off Surinam in fact belonged to Korean and Japanese companies, which confirmed the original suspicions.

By agreement with the Surinam authorities, an administrative cooperation mission consisting of representatives of the

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<sup>33</sup> In the Bangladesh textiles case (see the annual report on the "Fight against fraud" for 1996, Chapter 3, Section 3.2.3, p. 29), the Commission notified importers (OJ C 107, 5.4.1997) that there were doubts as to whether the certificates of origin (A forms) submitted in the Community in respect of certain textile products from Bangladesh since January 1994 were authentic, and suggested that they take the necessary precautions.

Commission and the Member States mainly concerned (France and the Netherlands) went there in February. After virtually all exports since 1992, amounting to 2920 tonnes, had been checked, it was clear that the shrimp had been caught by some one hundred ships which, with four exceptions, belonged mainly to Korean or Japanese companies (under various flags) or did not satisfy the conditions laid down in respect of crew membership. The shrimp landed by the vessels concerned did not, therefore, satisfy the cumulative criteria for determining entitlement to preferential treatment (the total quantity involved was 2900 tonnes).

By making incorrect declarations the exporters got the Surinam authorities to issue certificates which they used to import the shrimp into the Community duty-free. The mission established that some of the importers had known from the outset that the product did not satisfy the rules of origin and sometimes advised their suppliers on ways of getting round any inspection which might take place.

The duty evaded came to ECU 4 million. The Commission referred the matter to the appropriate authorities in France and the Netherlands for further action to recover the duty and apply penalties to the offending importers.

#### 2.2.1.2. Textiles

This is another sensitive sector where large quantities are involved and tariff preferences play a major part. The Indonesian textile case described below shows how sensitive the sector is to fraud and how necessary it is that there should be cooperation at Union level and with non-member countries.

In this particular case an administrative cooperation mission to Indonesia was carried out in June 1997 by a delegation from the Commission and the UK. There were suspicions relating to certain textile goods for which preferential Indonesian origin was being claimed under the generalised system of preferences (GSP) on import into the UK.

The goods were apparently manufactured in Indonesia, but using imported cloth from

Taiwan, Hong Kong and Korea. Inquiries found evidence of an organised network operating in the UK, Hong Kong and Indonesia.

With the authorities responsible locally, investigations were carried out on the spot into the producing and exporting companies in order to check the suspect documents. It was found that raw materials (cloth) which did not satisfy the rules of origin had been used by the largest of the companies concerned and the finished textile products were then exported to the Community under cover of preferential Indonesian certificates.

The loss in terms of customs duties came to some ECU 2 million. With the findings of the mission, the UK is in a position to recover the duty due. Legal proceedings are also under way in the UK.

#### 2.2.1.3. Anti-dumping measures

By its very nature, which involves imposing high taxes on certain products originating in non-member countries by reference to manufacturing criteria which are less stringent than in the preferential schemes context, this type of measure is very sensitive and is under constant threat of deflection of trade to evade payment of anti-dumping duties.

One illustration is the case of the disposable Chinese lighters. In the middle of 1995 the anti-dumping measures on Chinese lighters were reviewed, and anti-dumping duty changed from a rate of 16.9% of value to a special levy of ECU 0.065 per item, which was equivalent to a rate of 100%.

Following information received from a Member State, the Commission launched an investigation into all imports of disposable lighters from a producer in Macao. There had been a considerable increase in the number of lighters exported from Macao from the middle of 1995 onwards, coinciding with the new anti-dumping measures.

The lighters had been imported into the Community with GSP certificates of origin, under which the goods were exempt from customs duty on entry. In checks carried out

both by the Member States and by the Commission, however, it was found that non-originating components had been used in manufacturing the lighters. The certificates had therefore been issued in error. An on-the-spot mission was therefore carried out jointly by the Macao authorities, the Commission and the Member States concerned to study the production of lighters in Macao. The mission, which took place in January 1997, confirmed that all the GSP certificates issued were inapplicable.

A total of 110 million lighters had been imported since 1995, 35 million of them under the preferential arrangement. The customs duties recoverable on the latter come to approximately ECU 200 000. The real reason for the fraud was the amount of anti-dumping duty evaded, which affected all the imports and came to some ECU 7 million.

Criminal proceedings were instituted in one Member State against the main importer, who had imported 61 million lighters into the Community between 1995 and 1997.

#### 2.2.1.4. Environment policy

When the Union's environment policy involves measures which restrict trade such as a ban on particular products, it must be the concern of any action to combat fraud to ensure proper application of the arrangements in question the abuse of which, aside from the financial impact, runs counter to certain fundamental policies of the Union. This was illustrated by the case of products containing CFCs which were fraudulently imported into the Community.

German, Belgian, British and Dutch customs, with UCLAF, took concerted action to halt imports of Chinese products which destroy the ozone layer. A German trader had declared to customs, in Germany, Belgium and the Netherlands successively, some 1000 tonnes of noxious chemical products subject to an import ban<sup>34</sup> under the

false description "cooling agent R227", which is a legal, inoffensive product authorised for importation.

The goods brought into the Community in violation of the total ban were also imported without payment of customs duty by the improper use of inapplicable Chinese certificates of preferential origin. The products, which contained CFCs, were then marketed in several Member States (the UK, Italy, France, Belgium, Germany, Austria and Greece).

The quantity imported illegally greatly exceeds the total annual recycling capacity of the Community. As the primary cost was very low, the import constituted unfair competition against traders who complied with the rules. The use of the product could generate sizeable unlawful profits.

A stop was put to the unlawful imports by the arrest of the presumed perpetrator of the fraud and the seizure of 150 tonnes of goods as they were being delivered.

Proceedings are currently under way in Germany against the importing company and the person running it. In Belgium and the Netherlands actions have been brought by the customs authorities against the forwarding agents for recovery of ECU 0.2 million in duty.

There was an outstanding level of cooperation between the national customs departments in this coordinated operation in a new field, a sign of the growing awareness and particular determination of the Member States and the Commission when it comes ensuring that environmental protection measures are implemented.

It also demonstrates the advantages of carrying out physical inspections of goods which do not pose a particular financial threat at the outset but can harm the Community's interests in other ways.

#### 2.2.2. *Fraud in the area of the common agricultural policy*

Mention was made above of agricultural fraud by powerful crime syndicates.

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<sup>34</sup> Three hundred and sixty-five tonnes of R12B1 and R13B1 halons usable for fire-protection materials and more than 630 tonnes of R12 CFC usable in freezer installations.

Sometimes, however, fraud is spread more diffusely and benefits a wide range of operators guilty of irregularities which adversely affect the Community budget. As the cases set out below show, however, this does not mean that the overall effects are by any means negligible; in fact the proliferation of such cases sows the seeds of a loss of credibility by what is one of the Community's most fundamental policies.

#### 2.2.2.1. Tobacco quotas

The Commission was notified by the Portuguese authorities of a case of fraud involving production aid paid to Portuguese growers. The fraud consisted of diverting quotas from Spain to Portugal during a season when production in Spain exceeded the national quota while in Portugal it was below the quota. A number of Spanish producers, through an intermediary, sold their surplus tobacco to Portuguese producers, who declared it as their own goods and thereby obtained production aid in Portugal.

The fraud was detected by the Portuguese paying agency, INGA, which searched through its database and identified producers who had declared that they had produced more than three tonnes of tobacco per hectare - a suspicious production figure, as it was probably too high for that particular year in Portugal. The producers had inflated their own production with the tobacco bought in Spain. The part played by the intermediary, a Portuguese haulier, also came to light. The operation involved 422 tonnes of tobacco.

On the basis of the information obtained from the Portuguese paying agency and the criminal investigation department in Lisbon, the Commission decided to carry out an investigation in Spain in November 1997 to look for any sales of surplus tobacco in other Member States and identify the Spanish producers involved in the trade. The investigation was carried out under Regulation (Euratom, EC) No 2185/96, concerning on-the-spot checks by the Commission, which allows traders to be investigated exhaustively. The inspection was carried out jointly with the Spanish authorities (FEGA) and looked at two

Spanish suppliers who accounted for three quarters of the amounts delivered to Portugal.

The Portuguese authorities will be notified of the results of the checks carried out in Spain. The producers who made false declarations will have to pay back all the production aid received during the year (approximately ECU 2.3 million). So far, ECU 1.3 million has been recovered by suspending payments due in respect of the succeeding year. The Portuguese intervention agency will recover the sums still due (some ECU 1 million). Criminal proceedings against the producers and the intermediary are now being brought by the relevant public prosecutor in Portugal.

#### 2.2.2.2. Investigation in the citrus sector

In February 1997, following information received, the Commission launched an investigation into a suspected fraud involving citrus processing aid in Greece. A mission set up in several regions (the Peloponnese, Crete and Arta) at the same time was coordinated by UCLAF in conjunction with DG VI (clearance of accounts) and the Greek authorities (the investigating departments at the Ministry of Finance and the Ministry of Agriculture).

Several professional associations of citrus producers were inspected in order to check whether producers had actually been paid the minimum price by the processing companies (through the producers' associations) and whether the products intended for processing had actually been delivered in the proper way.

On-the-spot checks came up with a number of irregularities. *Inter alia*, the investigators found that there had been deliveries of fruit not entitled to aid (because it was rotten or of an insufficiently high standard). They also found that withdrawal and processing operations had taken place in establishments which were not adequately secured against manipulation or diversion of the consignments (because, for example, the premises were not sealed or goods had simply been unloaded without any physical check being made as to quality or quantity).

It is clear from the ongoing analysis of the large amount of documentation collected in relation to the procedures for delivering and paying for products intended for withdrawal, processing or free distribution that irregularities may have occurred (involving, for example, incomplete contracts and unsigned consignment notes and receipts for payment).

Because of the complexity of the case and the scale of the mission, decisions on follow-up action as regards clearance or the penalties to be imposed are now under consideration. Several cases have been referred to the Greek judicial authorities.

#### 2.2.2.3. Loan to Georgia

In 1997 the Commission's fraud-prevention department began to suspect that there had been fraud in connection with the delivery of 7 million litres of Bulgarian sunflower oil to Georgia, involving the use of a Community loan.<sup>35</sup> The loan was supposed to be for the importing of agricultural and food products and medical supplies originating in the Community, Bulgaria and other eastern European countries.

A Belgian import-export company received a documentary credit of ECU 4.625 million issued at the National Bank of Georgia, Tbilisi, by the Government of the Republic of Georgia.

The documentary credit was to cover the dispatching of 7 million litres of sunflower oil of Bulgarian origin. However, false bills of lading were produced and part of the quantity concerned never reached Georgia. An investigation was carried out in Sofia in April 1997 under the customs mutual assistance arrangement which forms part of the association agreement with Bulgaria, and established what trading and financial links existed between the Belgian import-export

company and the Bulgarian company which executed the contract to supply the oil and showed that 792 160 litres had not been delivered.

On the instructions of its Belgian partner, the Bulgarian company then repaid the corresponding amount of the loan, or ECU 546 352, to a private bank account in the name of the actual person running the Belgian company.

Armed with this evidence from Bulgaria that a fraud had been perpetrated against the financial interests of the Community, the Commission reported the matter to the public prosecutor's office in Brussels and the Central Investigation Office of the Belgian gendarmerie so that criminal charges could be laid against the person running the Belgian company.

Following this investigation, the Georgian authorities stressed that it was important in their view to clear up the case and put a stop to the activities concerned.

#### 2.2.3. *Fraud involving the structural policies*

The Structural Funds accounted for approximately 32% of the Community's total budget expenditure in 1997. As their specialist government departments administer this expenditure, the Member States have a definite responsibility for financial control as regards the use of the funds.

On 15 October the Commission adopted the detailed arrangements<sup>36</sup> for the implementation of Council Regulation (EEC) No 4253/88, clarifying what kind of control has to be carried out by the Member States in relation to operations co-financed by the Structural Funds. They are also required to notify the Commission of any irregularities found and of the administrative and legal follow-up action taken as a result.

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<sup>35</sup> Council Decision 91/658/EEC granting a loan (OJ L 362, 31.12.1991) under Commission Regulation (EEC) No 1897/92 laying down detailed rules for the implementation of a medium-term loan to the Soviet Union and its constituent Republics (OJ L 191, 10.7.1992), established by Council Decision 91/658/EEC (OJ L 362, 31.12.1991).

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<sup>36</sup> Commission Regulation (EC) No 2064/97, OJ L 290, 23.10.1997.

### 2.2.3.1. Embezzlement of ESF funds

It was established in a criminal investigation that invoices for ECU 260 000 issued by a subcontractor in connection with a contribution to a public body in Portugal from the European Social Fund had been falsified. The Commission decided to launch an investigation into the whole of the programme concerned.

The approved Community contribution to the programme comes to ECU 4.4 million. Because of the size of the grants, the Commission's investigation has not yet been completed, but some conclusions can already be drawn.

A Member State had carried out a partial check but not set up proper monitoring. Very large amounts of ineligible expenditure were declared, however. Evidence was also found of non-existent or unsupported expenditure being charged and certain items of expenditure being inflated on fictitious grounds. The approved Community contribution to the programme comes to ECU 4.4 million. The current investigation will establish what proportion of that sum has been embezzled. In addition, the subcontractor, who is under judicial investigation, drew up false invoices for certain other programmes, and these are also under investigation.

Two officials from the public body and the chairman of the subcontracting agency were remanded in custody during the criminal investigation. The vice-chairman of the public body and the subcontractor were given prison sentences.

In this case, starting from a detected fraud leading to a criminal prosecution, the Commission carried out an overall analysis which brought to light the irregularities committed. The Member State's monitoring and checking measures proved to be inadequate.

### 2.2.3.2. Networks engaging in fraud against the EAGGF Guarantee Section

A small number of types of expenditure is administered by the Commission direct. In the area of the EAGGF Guarantee Section, this is the expenditure laid down by Article 8 of Council Regulation (EEC) No 4256/88.<sup>37</sup> Further to a report by the Directorate-General for Financial Control and to a letter of observations from the Court of Auditors about a suspicion of fraud in that area, Commission authorising departments, Financial Control and UCLAF, in cooperation with the Court of Auditors, have been running a targeted investigation into all financial projects on the basis of Article 8 of the Regulation since 1997. The grants for these projects come to ECU 18 million and are being paid to Spanish, French, Irish, Italian and Portuguese companies.

The Commission looked into the financing operations and circuits and found that there was systematic forgery, with overbilling or bogus invoicing between firms within the same circuit for non-existent services. The networks which had been set up included front companies in different offshore locations as beneficiaries and subcontractors. Shortcomings in the procedures followed in Commission departments had also made it easier to carry out the frauds.

The Commission referred the matter to the judicial authorities in Spain, Italy and Portugal in 1997. The existing networks are so complicated that coordination between the public prosecutors' departments and collaboration with Commission departments are vital if the investigation is to succeed. Major steps have been taken in that direction, and the Commission has done everything possible to encourage such coordination.

At the same time, the procedures laid down in Article 24 of Council Regulation (EEC) No 4253/88 for annulling decisions and

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<sup>37</sup> OJ L 374, 31.12.1988.

recovering amounts paid without entitlement are under way.<sup>38</sup>

#### 2.2.4. *Fraud involving direct expenditure*

Direct expenditure is expenditure which beneficiaries draw on in the form of contracts directly administered and controlled by Commission departments. In 1997 they accounted for some 12% of Community expenditure in the sectors of research, education or energy, which, as the case described below shows, are not immune from the risk of irregularity or fraud.

A German company which had received a great deal of aid from the Commission for various research projects in the field of renewable energy sources was under suspicion of fraud. Preliminary investigations were carried out inside the Commission. Subsequent investigations led to the bankruptcy department at the relevant court (Amtsgericht Duisburg), where the company in question had meanwhile been put through proceedings for bankruptcy. Information collected rapidly showed that the company had in fact embezzled large sums of money.

The Commission submitted the case, with the main items of evidence, to the appropriate public prosecutor, who instituted legal proceedings against the people responsible for running the company on charges of bankruptcy and fraudulent use of the grant.

The investigation showed that the company had not filed for bankruptcy, despite being legally required to do so, and had diverted the payments received from the Commission under research contracts for other purposes, such as paying off its creditors. The financial impact is estimated at ECU 2.1 million. Criminal proceedings are under way.

### 2.3. **VAT fraud: terms for expanding investigations**

The VAT fraud problem is comparable to that of fraud involving products with a high tax risk (alcohol and cigarettes): the financial impact is high and primarily affects national treasuries, though it is on a scale which calls for a joint response. In the interests of greater efficiency, a team to combat VAT fraud was set up in UCLAF in 1995. Since that time there have been regular contacts with the Member States to prepare the national administration for working jointly.

The VAT fraud team's work relies on the reports the Member States send it about suspected instances of fraud. In 1997 it took part in 18 investigations into cases involving more than ECU 300 million in tax.<sup>39</sup>

Cooperation between the Member States and the Commission is still not as effective as it might be, however,<sup>40</sup> as the following case shows.

Denmark asked the Commission for help in a situation where there appeared to be systematic violation of the VAT system by a number of companies in the scrap metal trade. Supply networks had been set up in which "mailbox" companies gave security for purchases of large quantities at prices above the official London Metal Exchange price. These companies then sold the metal on to large firms in Denmark or another Member State, but at prices lower than the official price.

The mailbox companies could not have gone on trading in this way unless they were systematically evading VAT on the transactions. An investigation therefore had to be carried out to determine the scale of the fraud and the degree of complicity of the client companies in various Member States.

Owing to legal difficulties, however, the department responsible in one of the Member

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<sup>38</sup> See Chapter 1, section 1.3.1.

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<sup>39</sup> The cases in question concern transactions involving silver, metal, copper, non-ferrous metals, electronic components, videos, cars etc.

<sup>40</sup> See also Chapter 3, section 3.5.2.

States was unable to take part. In particular, the Member State concerned has still not overcome the problem of tax secrecy, which means that it cannot play a full part in coordinated action to combat international VAT fraud, as most of the Member States do in specific, major cases.

In the same Member State, furthermore, the national auditors did not have power to take hold of the company's documentation and accounts directly. This lack of appropriate powers and the variations in powers between the different Member States severely curtail opportunities for carrying out effective investigation in complicated international fraud cases.

This case shows how urgent a need there is for the Member States to take the requisite steps, as regards organisation, procedures and powers, to ensure that there is effective cooperation at all levels in combating VAT fraud. Discrepancies in the application of Community law<sup>41</sup> in the Member States provide loopholes and opportunities for evading VAT. There needs to be harmonisation to prevent fraudulent operators from exploiting differences in the rules regarding tax secrecy or between the powers held by national tax departments.

To strengthen cooperation, Community legislation also needs to be clarified, while the Commission should be allowed to act in cases of VAT fraud of importance to the whole Community and to coordinate action in appropriate cases. Provisions such as those which already apply in relation to customs and agricultural matters would be appropriate.

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<sup>41</sup> Sixth VAT directive, Council Directive 77/388/EEC of 17 May 1977 on the harmonisation of the laws of the Member States relating to turnover taxes - Common system of value added tax: uniform basis of assessment (OJ L 145, 13.6.1977).



### 3. STEPPING UP COOPERATION WITH THE MEMBER STATES

This chapter reports on the stepping up of cooperation with the Member States, which is a keynote of the 1997-98 anti-fraud work programme for protecting Community finances.

The chapter starts with a review of certain important steps taken by Member States to protect the Community's financial interests. It goes on to look at operational cooperation with police forces and judicial authorities, which has been made possible by the adoption of new legal instruments, as discussed in detail in Chapter 5, and through informal contacts developed with national authorities for the purposes of on-the-spot investigations. However, most of the chapter is devoted to indirect taxation. Here we see how aware the Commission and the Member States are of the need to beef up the existing arrangements in order to combat financial crime affecting national and Community interests more effectively.

#### 3.1. Action taken by Member States to protect the Community's financial interests

In 1997, as in previous years,<sup>42</sup> the Member States continued their efforts to make appropriate organisational arrangements aimed at more effective protection of the Community budget and the Community's economic and commercial interests against fraud and financial crime.

For example, in Denmark a unit dealing with Community fraud in the area of customs (revenue and expenditure) was set up as part of the federal anti-fraud bureau.<sup>43</sup> The national police authorities also have a federal unit dealing with economic crime.<sup>44</sup> It is responsible for coordinating complex fraud investigations.

Greece set up SDOE (the economic and financial crime office) as part of the Ministry of Finance. Its mandate includes the specific task of protecting the Community's financial interests. It began operating in 1997 and has already been involved in effective cooperation with the Commission.

On 26 November Portugal announced that it would be setting up a special body with responsibility for coordinating customs and tax investigations. Known as UCLEFFA,<sup>45</sup> the body will have similar responsibilities at national level as UCLAF does at Community level. Like France's ICLAF and Italy's *Guardia di Finanza*, it will be a key partner for the Community.

The French police in the form of the *Gendarmerie nationale*, whose remit covers all kinds of crime including fraud, is currently engaged in a large-scale research project in connection with international investigations (notably the breach of the embargo on British beef). It invited UCLAF to present the Community's policy towards protecting its financial interests and the anti-fraud strategy in connection with the role of its central fraud prevention service as part of a seminar it will be holding in 1998 for heads of investigation departments.<sup>46</sup>

#### 3.2. Mutual administrative assistance instruments in the area of customs and agriculture

In a Europe with no obstacles to the free movement of goods, persons, services and capital, it is essential to make greater provision for investigations to be undertaken jointly by specialised national authorities with the assistance of the Commission,

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<sup>42</sup> See the 1995 fraud report, Chapter 5, page 40, and the 1996 fraud report, Chapter 4, page 39.

<sup>43</sup> *Svigsbekæmpelsekontoret*.

<sup>44</sup> *Afd. for Særlig økonomisk Kriminalitet*.

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<sup>45</sup> *Unidade de Coordenação da Luta contra a Evasão e a Fraude Fiscal e Aduaneira*.

<sup>46</sup> Investigation departments have operational and territorial powers for fighting crime. The districts they cover coincide with the jurisdictions of Courts of Appeal, which means that there are regular contacts between investigation departments and public prosecutors.

particularly when it comes to cross-border cases involving sensitive sectors or goods.

Cooperation between the Member States and the Commission on effectively combating customs and agricultural fraud and irregularities has traditionally taken the form of the mutual assistance scheme, which remains an important tool.

A new regulation on mutual assistance on customs and agricultural matters, Council Regulation (EC) No 515/97,<sup>47</sup> was adopted on 13 March 1997 on the basis of a Commission proposal dating from 1992. It concerns mutual assistance between the administrative authorities of the Member States and cooperation between the latter and the Commission to ensure the correct application of the law on customs and agricultural matters. It came into force on 13 March 1998, repealing Council Regulation (EEC) No 1468/81. It strengthens the Community rules on combating irregularities in these areas and also provides the legal basis for sensitive data on customs and agricultural irregularities to be stored on a central database. The database, known as the CIS (Customs Information System), can be accessed by the relevant departments of the Member States and the Commission, while safeguarding data confidentiality and protecting personal information.

The electronic bulletin board, SCENT,<sup>48</sup> has been in existence since 1992. It currently comprises around 400 terminals located mainly at customs investigation departments in the Member States and at major ports and airports in the Community. It is an information exchange system, rather than a data collection system.

These data of an administrative type<sup>49</sup> are to be kept in the CIS only for as long as they

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<sup>47</sup> OJ L 82, 22.3.1997. See also the 1995 anti-fraud report, Chapter 2, p. 27.

<sup>48</sup> System for a Customs Enforcement NeTwork

<sup>49</sup> The legal basis for this database to be set up for non-Community customs fraud (drugs etc.) will be provided by the convention on the use of information technology for customs purposes (OJ C 316, 27.11.1995), which is in the course of being ratified.

are being used for operational purposes of prevention, investigation or prosecution in cases of irregularities. Access to the data is to be restricted to departments specifically authorised by the Commission (such as UCLAF) and by the Member States.

This is a first step in the direction advocated by the European Parliament, which recommended that a central customs data office should be set up within the Commission for the Member States to notify of any strategic and operational information at their disposal concerning action against fraud in customs and agricultural matters.<sup>50</sup>

### 3.3. Other forms of cooperation in relation to customs, agriculture and own resources

- The goods movement rules (transit system) remain one of the most vulnerable areas. Reforms currently under way to the Community/common transit arrangement<sup>51</sup> serve to clarify and simplify the regulations and coordinate operational measures so as to achieve a balance between the facilities offered to reliable traders and the need for security in transit operations.

A basic procedure, in which the basic guarantee is the comprehensive, individual security, is available to all operators; there is also a “light” procedure – where an operator is found to be reliable and there are no risks, the operator is eligible for a simplified procedure in which, among other things, the amount of the guarantee may be varied.

Regarding security and checks, there is also provision for tougher preventive measures in the basic procedure and for subordinating simplification to risk-

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<sup>50</sup> Recommendation No. 3 of the final report from the European Parliament’s committee of enquiry into the Community transit scheme (doc. A4-0053/97, 20.2.1997).

<sup>51</sup> Plan of action for the reform of transit in Europe, presented by the Commission on 30.4.1997: COM(97)188 final, OJ C176, 10.6.1997.

analysis and review of the operator's reliability, having regard to the operator's own security measures.

Commission Regulation (EC) No 75/98,<sup>52</sup> amending Regulation (EEC) No 2454/93 laying down certain provisions for the application of the Community Customs Code,<sup>53</sup> made new provisions for the customs status and transit of goods carried by sea and recast the list of eligible goods.

A proposal for amendment of the Customs Code as regards the scope of the transit procedure and the application of guarantees was presented to the Council and parliament on 28 September.<sup>54</sup>

A European network of 21 national coordinators and 330 local correspondents was set up by all the countries involved (EC, EFTA (except Iceland) and the Visegrad countries). They are to be linked by e-mail in 1998.

Joint and coordinated control programmes have been established, covering in particular:

- documentary checks on the authenticity of customs stamps via the Community computerised register<sup>55</sup> and on guarantee certificates;
- controls on sensitive goods and goods deemed at risk;
- *a posteriori* controls on operations eligible for the simplified procedure (air and sea transit);

– identification of itineraries and other parameters deemed to be at risk.

As for computerisation of the transit system, the New Computerised Transit System entered Phase II (construction and initial implementation) this year.<sup>56</sup> To offset delays estimated at 18 to 24 months in establishing the hardware infrastructure, a new strategy is being devised with the countries participating in Phase II. The aim is to meet the original timetable despite unknown factors, partly by confining the system's functions in the initial implementation period to strictly essential messages in a limited number of customs offices monitoring transit operations.

- The Early Warning System used to exchange information once more proved to be a major and useful source of information. In 1997 customs staff exchanged more than 43 000 messages using the system.<sup>57</sup>

In the customs area, the Commission produced in 1997, in partnership with the Member States, a revised risk analysis guide aimed at reinforcing customs control techniques applied.

In contrast, the "blacklist", which is supposed to serve as an advanced warning system for agricultural transactions, has not yet achieved its target. The system was introduced by Council Regulation (EC) No 1469/95 and put into effect by Commission Regulation (EC) 745/96.<sup>58</sup> The arrangements were put in place in all the Member States, which by the end of 1997 had identified only a dozen or so traders as "unreliable".

- Once again the freephone numbers, which were introduced in 1995, were a useful

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<sup>52</sup> OJ L7, 13.1.1998.

<sup>53</sup> OJ L 253, 11.10.1993.

<sup>54</sup> COM(97)472 final, OJ C337, 7.11.1997.

<sup>55</sup> The TCT (Electronic Transmission of Customs Stamps) programme established by the Commission (DG XXI) in 1997 can be used for transmission to the customs authorities of all countries involved in the Community/common transit system of images and data relating to customs stamps and seals for transit operations.

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<sup>56</sup> Cf. 1996 report, Chapter 5.3, p. 42.

<sup>57</sup> Not all of the consignments reported in these messages turned out to involve irregularities.

<sup>58</sup> OJ L 102, 25.4.1996, regulation laying down the implementing provisions for Council Regulation (EC) No 1469/95 (OJ L 145, 29.6.1995).

independent source of additional information. UCLAF received nearly 1 500 calls in 1997 and about 10% of them are being followed up.

### **3.4. Examples of cooperation with police and judicial authorities in the Member States**

Cooperation between the Commission's UCLAF and the police authorities of the Member States is based on Articles 5 and 209a of the EC Treaty as well as on the conventions on protecting the Communities' financial interests. These conventions are still to be ratified by the Member States.<sup>59</sup>

The fourth axis of the Community anti-fraud strategy aims at improving the compatibility of national legislation to implement a policy of criminal law enforcement against those who defraud the Community budget. This objective has been met by the secondary legislation adopted under the first pillar of the EU Treaty and the instruments under Title VI of the Treaty.

In the course of its inspections and investigations and from the information it receives (from the Member States, the European Parliament, the Court of Auditors or other sources, such as the freephone), UCLAF may come across data or find material that has to be reported to national judicial authorities for prosecution purposes. Likewise, when the Member States discover an irregularity, they may have to pass on information to the judicial authorities, in accordance with national procedures. However, cases should be reported to the relevant judicial authorities in a uniform way throughout the Community, which is where the Commission comes into its own. It has the active role of passing on relevant information directly in the form of the mission reports drawn up by its inspectors, which can be used as evidence in court. In addition, it is setting up a criminal law expertise unit within UCLAF for the specific purpose of preparing prosecutions in cases of

cross-border fraud. This is a coordinating role to make contacts easier.

#### *3.4.1. The risk of counterfeiting the euro*

Following contact between the European Monetary Institute<sup>60</sup> and the Commission, the latter has undertaken an in-depth analysis of the issue of counterfeiting in conjunction with national experts.

An evaluation of the need for action on this subject arises out of the determination to protect the credibility and authenticity of the euro at Union level. In general, the risk of counterfeiting will be higher when the new currency is first launched, and adequate measures are under consideration to ensure an appropriate protection for the euro

The legal framework, instruments and resources needed to protect EMU and the euro cannot be put in place without first assessing the new situation and holding joint discussions with experts on counterfeiting. This is why the Commission proposed that the Luxembourg Presidency of the working group on police cooperation should call together all the police experts on counterfeiting together with UCLAF to produce a report with guidelines. This proposition has been accepted.

Since the single currency will be replacing the national currencies and the Member States have different structures for preventing and combating counterfeiting, there will need to be structures for exchanging information and cooperation between the specialised departments and all the institution and bodies concerned at Community and Union level. There will also need to be a common definition of currency counterfeiting and arrangements made to combat it in a concerted way. The action programme on organised crime, which was

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<sup>59</sup> See Chapter 6, section 5.4.1.

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<sup>60</sup> Under the EU Treaty, the European Monetary Institute was set up to carry out certain duties relating to preparations for economic and monetary union. Its principal task is to put in place the operational framework needed for the proper running of the European System of Central Banks, which is to be made up of the European Central bank and the national central banks.

adopted by the Council on 28 April, also calls on the Commission to examine the need to introduce common provisions on combating organised crime involving the counterfeiting of banknotes and coins in the run-up to the introduction of the single currency (Recommendation No 26).<sup>61</sup>

### 3.4.2. *The Commission's criminal law expertise unit*

The 1997/98 anti-fraud work programme stipulates the setting up of a "criminal law liaison and expertise interface" to strengthen contacts with national judicial authorities. This was also recommended by the European Parliament.<sup>62</sup> Part of UCLAF, the criminal law expertise and liaison unit is starting to bring together experts in criminal and financial law from the Member States with a view to improving relations with the national police and judicial authorities responsible for criminal prosecutions.

The unit is intended to provide these bodies with technical and operational assistance and to make cross-border coordination easier. It will use its expertise and familiarity with national laws to make investigators' jobs easier, for example, when they are preparing for on-the-spot investigations and inspections.

The unit is meant to be able to have cases speedily referred to the relevant prosecutors and magistrates as well as to identify the factual and legal aspects relating to the cross-border dimension of the proceedings in order to facilitate the coordination of judicial cooperation procedures in real time.

Judicial cooperation with non-member countries is also essential. Here too, a pragmatic approach will have to be adopted involving criminal law experts to try to resolve the problems that arise, which are particularly alarming when criminal networks are operating from other countries

outside the Community, such as Switzerland, Liechtenstein, the Virgin Islands and Panama.<sup>63</sup>

The new powers given to UCLAF inspectors by Council Regulation (Euratom, EC) No 2185/96 concerning on-the-spot checks and inspections will lead to an increasing need for judicial follow-up. Likewise, the second protocol to the convention on the protection of the Communities' financial interests states that the Commission must provide assistance for investigations into cases of fraud, corruption and money-laundering.<sup>64</sup> This is precisely what the Commission's criminal law expertise unit will be doing, particularly once the second protocol has been ratified by the Member States.

## 3.5. Cooperation in the area of indirect taxation (excise and VAT)

Whether large-scale or not, cases of fraud affecting the financial interests of the Communities have a knock-on effect on national finances. This is why it is essential to make use of the existing cooperation instruments in the area of indirect taxation and, where necessary, improve them after seeing how well they operate.

In 1997 the Member States and the Commission continued to discuss increased cooperation in this area in order to get a clearer picture of how fraud operates and to improve methods of combating it. In this vein, there were operational contacts on a virtually daily basis between the Commission and the national authorities responsible for excise and VAT.

### 3.5.1. *Excise*

In response to the alarming increase in tobacco and alcohol excise fraud, in March the Commission and the Member States set up a high-level group to find solutions to the

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<sup>61</sup> OJ C 251, 15.8.1997.

<sup>62</sup> Recommendation 18 in the final report, referred to above, from Parliament's committee of enquiry into the Community transit scheme.

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<sup>63</sup> For example, although there is a customs mutual assistance agreement with Switzerland, judicial follow-up is hindered by the lack of any judicial assistance agreement applicable to customs and tax offences.

<sup>64</sup> See Chapter 6, sections 5.1 and 5.4.2.

problems of fraud where tobacco and alcohol are involved.<sup>65</sup> The group's remit covers not only detection and prosecution, but also preventive measures.<sup>66</sup>

The high-level group met three times in 1997. It adopted a cross-sector approach, dealing with customs duties, VAT and excise. The group identified the nature and extent of this type of fraud. It also highlighted shortcomings affecting the operation of excise duty systems and the effectiveness of inspections carried out by the Member States as well as shortcomings in the legislation itself.

Since the Community transit system was recently tightened up,<sup>67</sup> criminal organisations have been turning their attention to excise duties, since the system suffers from similar weaknesses in terms of both inspections and the legislation itself.<sup>68</sup> The Commission is accordingly planning to focus its efforts on strengthening the system for imposing excise duties and, in particular, on the controls on movements of goods enjoying excise-duty suspension.

### 3.5.2. VAT

In 1997 the Commission continued its policy of cooperation with the Member States to combat internal VAT fraud.

The seminars held in 1997 under the Matthaues-Tax programme (which ran until the end of 1997, being replaced by the

Fiscalis programme in 1998<sup>69</sup>) dealt with fraud prevention, covering checks on how VAT is booked, the preparation and scheduling of tax inspections and the issues raised by electronic invoicing and electronic trade. In 1997 the Commission financed and organised two conferences for national VAT inspectors. The conferences, which were the idea of the Italian *Guardia di Finanza*, further consolidated the Community-wide operational contact network and provided an opportunity for exchanging information on detection techniques and investigatory powers. The Commission also organised several coordination meetings for Member States affected by the same cases as well as serving as the focal point for organising further action on cases under investigation by national authorities.

As part of the Matthaues-Tax programme, the Member States organised exchanges between their tax officials, who had the chance to see how other national authorities operate. This should help to forge stronger links between national authorities and make fraud fighting more effective. The 1997 programme of exchanges involved some 300 officials.

There are political obstacles to establishing proper cooperation between the Member States and the Commission, since several Member States continue to fail to acknowledge that the Community legislation on mutual administrative assistance<sup>70</sup> is the legal basis entitling the Commission to receive information and participate in discussions on fraud cases involving VAT.

The Anti-Fraud Sub-Committee (SCAF) of the Standing Committee on Administrative Cooperation on Indirect Taxation (CPCA) has been encouraging the Member States to make better use of the existing computerised system for exchanging information on VAT

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<sup>65</sup> The group is due to report to Directors-General of customs and indirect taxation in April 1998.

<sup>66</sup> A Matthaues-Tax programme seminar was held shortly after the first meeting of the high-level group on the subject of irregularities in intra-Community transactions involving goods liable for excise duties. The Matthaues-Tax programme is a Community action programme designed to prepare officials responsible for indirect taxation in the Member States for the implications of the creation of the internal market. See also Section 1.4.2 on VAT below.

<sup>67</sup> See the "Action plan for transit in Europe - a new customs policy", submitted by the Commission on 20 April 1997, COM(97) 188 final (OJ C 176, 10.6.1997).

<sup>68</sup> Here it is interesting to note that UCLAF has had no cases of intra-Community fraud involving mineral oils reported to it by the Member States.

<sup>69</sup> See point 3.5.3 below.

<sup>70</sup> Council Directive 77/799/EEC of 19 December 1977 concerning mutual assistance by the competent authorities of the Member States in the field of direct taxation (OJ L 336, 27.12.1977) and Council Regulation (EEC) No 218/92 of 27 January 1992 on administrative cooperation in the field of indirect taxation (OJ L 24, 1.2.1992).

called *SCENT fiscal*.<sup>71</sup> For this purpose it revised the standard forms used for exchanging data and proposed a sort of instruction manual designed to make the system more user-friendly. Nonetheless, the system is still disappointingly under-used. The Member States have all admitted that very little information has been exchanged and that there is little follow-up, particularly when it comes to actually taking further action.

There is, however, another aspect to the problem. Some Member States tend to pass on useful information only to the Member States directly involved in the fraud case or cases in question. Tax confidentiality and data protection are regularly quoted as the main reasons for not extending the distribution of information to automatically include the Commission. It is clear that this sort of restricted exchange of information, particularly where the Commission is left out, can only have harmful implications for operations in the field. If this state of affairs persists, it will be virtually impossible to devise a proper Community strategy for combating indirect taxation fraud.

#### 3.5.2.1. New administrative cooperation standards

Progress in combating fraud involving indirect taxation largely depends on the available administrative cooperation and mutual assistance tools being actually used. This means, in particular, Council Regulation (EEC) No 218/92 and Directive 77/799/EC. The Commission's second "Article 14" report,<sup>72</sup> which specifically deals with this issue, noted that several Member States do not make as much use of these tools as they might. In 1997 solid recommendations for strengthening cooperation were adopted by the senior civil servants responsible for indirect taxation. The Member States are currently working on stepping up cooperation in order to make the

best use of the existing arrangements for fighting fraud together.

#### 3.5.2.2. Simultaneous inspections to tighten up VAT operations

Inspections simultaneously carried out by several Member States in several Member States are set to play a major role in improving the fight against fraud.<sup>73</sup> The Commission oversaw four of these simultaneous exercises in 1997, involving 13 Member States. The main aim is to develop suitable methods for coordinating and conducting inspections of this type. The inspections were good practice for the Member States, making them better prepared to carry out similar ones in the future. The Commission also organised a special seminar on this subject in 1997, which should result in more inspections of this type being scheduled in the future. The Commission will be continuing with its policy of involving more officials in multilateral inspections to ensure that inspections of this type become part of an inspections strategy shared by all Member States.

#### 3.5.2.3. Analysing VAT fraud risk

Since 1996 SCAF has been conducting a study on VAT fraud in the Community to identify the most common types of fraud, how it is perpetrated and the factors that allow it to happen. The preliminary findings of the study were presented to the Member States in 1997 in the sub-committee to enable them to focus their resources on the most fraud-prone areas in order to detect and deal with fraud as early as possible.

SCAF's investigations, which covered nearly 500 fraud cases selected by the Member States, clearly showed that the intra-Community VAT system is particularly hard hit by fraud, although most types of transactions are now affected. The amounts involved are in the region of ECU 573 million and 30% of cases involve amounts in excess of ECU 1 million. And yet there are

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<sup>71</sup> System dealing specifically with indirect taxation using the SCENT network (see section 3.2).

<sup>72</sup> COM(96)681.

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<sup>73</sup> The investigation discussed in Chapter 2, section 2.3, clearly illustrates the operational difficulties encountered by the Member States in cases of this type.

good reasons to believe that this is only a fraction of the total fraud being committed. Fraud involving VAT on intra-Community and international transactions accounts for nearly half the total sums involved. SCAF's study should wake Member States to the seriousness of the situation and the need to step up cooperation to target cross-border transactions, since fraudsters are taking advantage of the absence of physical borders.

The study also showed that information was insufficiently centralised. This made it difficult to get an overview of the complete extent of the phenomenon and yet this is what the Member States needed to know in order to be able to devise an inspections strategy that took account of real priorities. Working in close cooperation with the Member States, the Commission is in the best position to receive, analyse and pass on information concerning fraud, so that it can be more effectively countered at international level.

### 3.5.3. *The Fiscalis programme*

The Commission proposals for the Fiscalis programme were adopted by the Council and the European Parliament on 13 May and 26 November.<sup>74</sup>

The programme runs from 1 January 1998 to 31 December 2002. It builds on the Union's current activities, where possible, and is based on using communication and information exchange tools to further cooperation on preventing fraud involving VAT and excise duties. To this end, Fiscalis also incorporates arrangements to bring national officials together to work on real cases and provide them with the necessary skills to do their job properly. The programme also involves the countries of Central and Eastern Europe and Cyprus and comprises three phases:

- preparing guides and manuals for the communication and information exchange systems, such as VIES;<sup>75</sup>
- exchanges, seminars and multilateral inspections;
- joint training for all national officials.

### 3.6. **Training**

As in 1996, the Commission focused on organising targeted training for specialist departments managing and checking Community funds handled by national authorities as well as for judicial authorities, such as judges, public prosecutors and the police, whose cooperation is vital for the success of anti-fraud activities in the field.<sup>76</sup>

To enhance its training support capacity, the Commission continued its policy of giving financial support to Member States who apply for it on the basis of a programme to upgrade the skills of national anti-fraud staff.

In 1997 the Commission organised the following events,<sup>77</sup> either alone or in conjunction with the Member States, mostly lasting 2 days:

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<sup>74</sup> COM(97)175 final, OJ C177, 11.6.1997; and COM(97)621 final, OJ C1, 3.1.1998.

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<sup>75</sup> VAT Information Exchange System.

<sup>76</sup> See section 3.5 on training concerning indirect taxation (points 3.5.2 and 3.5.3).

<sup>77</sup> The events involved nearly 1 500 national civil servants and other staff. The country name given refers to the country hosting the event, although the events were attended by officials from other Member States at the invitation of the organisers (Member State in question or the Commission).



| <b>COUNTRY</b>        | <b>AUTHORITIES AND AUDIENCE</b>   | <b>TOPICS</b>  |
|-----------------------|---|--|
| GERMANY               | The Saxony Public Prosecutor's Office<br>- German prosecutors, customs inspectors and police, with participants from Poland, Hungary and the Czech Republic | Community fraud and cooperation  |
|                       | <i>Zollkriminalamt</i> <sup>78</sup><br>- customs inspectors from seven Member States   | Fraud involving agricultural expenditure   |
|                       | <i>Zollkriminalamt</i><br>- customs inspectors from all the Member States   | Fraud involving imports of textile products  |
|                       | Federal Ministry of Finance and the agriculture authorities of the <i>Länder</i><br>- participants from four Member States                                  | Detecting fraud involving agricultural expenditure                                 |
|                       | <i>Landeskriminalamt</i> , <sup>79</sup><br>Sachsen-Anhalt  | Community fraud and cooperation  |
|                       | <i>Zollkriminalamt</i><br>- German prosecutors, with participants from Austria and Sweden   | Community fraud and cooperation  |
| BELGIUM<br>(Brussels) | Federal Ministry of Finance and <i>Told-og Skattevæsen</i> <sup>80</sup> (joint event)  | Cooperation and techniques for detecting fraud involving export refunds            |
|                       | Customs departments (all Member States)   | Extension of the EWS <sup>81</sup>   |
|                       | Customs departments and other experts (all Member States)   | Implementation of the AFIS <sup>82</sup>   |
|                       | <i>Fiscal General del Estado</i> <sup>83</sup><br>- prosecutors from Spain (and other Member States)  | Cooperation between investigators and judicial authorities                         |
| FINLAND               | Judicial and customs authorities from Hungary, Slovenia, Bulgaria and the Czech Republic  | Community fraud and cooperation  |
|                       | Customs inspectors (from other Member States too)<br><br>Finnish National Bureau of Investigation (central police)  | Fraud involving imports of textile products<br><br>Community fraud and cooperation |

<sup>78</sup> German central (federal) customs bureau.

<sup>79</sup> The central criminal investigation department.

<sup>80</sup> The Danish customs and tax authorities.

<sup>81</sup> Early Warning System.

<sup>82</sup> Anti-Fraud Information System - one-stop shop for Member States to exchange data electronically, incorporating the SCENT system.

<sup>83</sup> Spanish Public Prosecutor's Office.

|                |   |  |
|----------------|---|--|
|                | department)   |  |
|                | <i>Tullihallitus</i> <sup>84</sup> (with investigators from other Member States)                                | Cigarette smuggling  |
| FRANCE         | Criminal investigation police from France and other Member States   | Criminal law protection of industrial property                   |
|                | Customs authorities from France and twelve other Member States  | Technical assistance in detecting consignments of smuggled goods |
| ITALY          | Police Further Training College   | Community fraud  |
|                | The <i>Guardia di Finanza</i> Academy (Officer School)  | Protecting the Communities' financial interests                  |
|                | <i>Guardia di Finanza</i> (with investigators from other Member States)   | VAT fraud  |
|                | <i>Consiglio Superiore della Magistratura</i> <sup>85</sup><br>- prosecutors from Italy and other Member States | Judicial cooperation in prosecuting in fraud cases               |
|                | <i>Guardia di Finanza</i> (with investigators from all Member States)   | VAT fraud  |
| PORTUGAL       | <i>Inspecção Geral da Administração do Território</i> (IGAT) <sup>86</sup>                                      | Irregularities involving the ERDF and the Cohesion Fund          |
| UNITED KINGDOM | The Scottish Office <sup>87</sup>   | Fraud involving the Structural Funds                             |
|                | Intervention Board for Agriculture <sup>88</sup>  | Fraud involving agricultural expenditure                         |
|                | NAO <sup>89</sup>   | Fraud involving the Structural Funds                             |
| SWEDEN         | Ministry of Agriculture   | Fraud involving agricultural expenditure                         |
|                | <i>Riksrevisionsverket</i> (RRV) <sup>90</sup>  | Fraud involving the Structural Funds                             |

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84 Finnish national customs authorities.

85 The Supreme Law Council.

86 Inspectorate-General for Land-Use Planning.

87 Responsible for Structural Fund payments.

88 EAGGF-Guarantee paying agency.

89 National Audit Office.

90 Danish national audit office.

## 4. COOPERATION WITH NON-MEMBER COUNTRIES

### 4.1. Implementation of existing fraud prevention measures by applicant countries (preparation for enlargement)

On 15 July the Commission adopted "Agenda 2000",<sup>91</sup> a communication describing the broad outlook for the development of the Union and its policies on the eve of the next century, the issues posed by enlargement, and the future financial framework beyond the year 2000 in an enlarged Union.

The 1997/98 work programme for the fight against fraud made the link between protection of the Community's financial interests and the process of preparing the countries of central and eastern Europe for membership.<sup>92</sup>

This process is fleshed out in the Accession Partnerships drawn up by the Commission for each of the applicant countries, setting out the priorities to help them meet the political and economic criteria laid down by the Copenhagen European Council in June 1993. The Accession Partnerships also provide for pre-accession structural financial assistance from 2000 onwards, in addition to continued operations under the Phare programme.

This is the background against which the Commission's work programme for the protection of the Community's financial interests will be implemented. The work programme places the emphasis on extending customs cooperation to protect Community own resources. It recommends the adoption of existing Community rules, in particular on monitoring and preventing fraud. This includes not only Community regulations on controls, notification of cases of fraud and

irregularity, and administrative sanctions but also the Convention on the protection of the Community's financial interests and the accompanying protocols and the application of Article 209a EC (cooperation with the Commission and all competent authorities, principle of equivalence). To this end, the Commission has for several years been organising training courses.<sup>93</sup> However, to ensure that this approach is truly successful, it plans to set up a network of technical advisers in certain non-member countries, whose task will be to liaise directly between the authorities in those countries and departments in the institutions and to cooperate on the ground with local control bodies. The ultimate aim is to ensure, from day one of accession, a similar degree of protection for the Community's financial interests and policies in the enlarged Community as at present.

### 4.2. Mutual assistance agreements between the Community and non-member countries

Outside the pre-accession process, which only concerns 11 countries, the Community concluded a number of agreements in 1997 containing specific provisions on mutual customs assistance with 27 non-member countries, a third of them in central or eastern Europe. Nine countries have signed or initialled an agreement not yet in force, and negotiations are planned or in progress with a further 22.

These provisions provide a legal basis for the authorities responsible to request or provide administrative assistance when conducting investigations to ensure the proper application of the Community's or the partner country's customs regulations.

Agreements came into force in 1997 with 8 countries: the Faeroe Islands on 1 January; Kazakstan on 1 April; the Republic of Korea

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<sup>91</sup> COM(97) 2000 final. Programme covering the period 2000-2006.

<sup>92</sup> The applicant countries from central and eastern Europe are: Hungary, Poland, Estonia, the Czech Republic, Slovenia, Bulgaria, Latvia, Lithuania, Romania and Slovakia.

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<sup>93</sup> See in particular the annual reports on the fight against fraud for 1995 (Chapter 5, page 43) and 1996 (Chapter 4, page 38).

on 1 May; the Swiss Confederation on 1 July; the United States of America on 1 August; Georgia on 1 September; Armenia and the Russian Federation on 1 December.<sup>94</sup>

Community agreements with similar provisions were also signed with the following countries: Azerbaijan on 8 October (not yet in force); Jordan on 25 November (not yet in force); Canada on 4 December (entered into force on 1 January 1998).

By 31 December the Community had concluded agreements of this kind with 36 non-member countries (28 of which have already come into force), covering practically all its European neighbours and its main trading partners. Negotiations on global agreements (with mutual assistance protocols) or specific agreements (confined to customs matters, including mutual assistance) are under way or planned with around twenty other non-member countries, including Albania, South Africa, Egypt, Lebanon, Cyprus, Hong Kong, China, Chile, the Mercosur countries, and some ASEAN countries.<sup>95</sup>

The provisions on customs cooperation in the agreements with non-member countries also cover technical assistance in the customs field. With regard to enlargement, the essential aim of such assistance (provided under the Phare programme) is to help the countries concerned to apply Community legislation effectively when the time comes, including the rules on fraud prevention and on the protection of the Union's financial interests.<sup>96</sup>

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<sup>94</sup> As far as the Russian Federation is concerned, the entry into force of the Partnership and Cooperation Agreement, to which the Member States are also signatories, has no effect at Community level on the interim agreement, in force since 1 February 1996, and the accompanying protocol on mutual administrative assistance, which already covers all customs matters under Community jurisdiction.

<sup>95</sup> Association of South East Asian Nations.

<sup>96</sup> Cf. Section 4.1.

## **5. PENALTIES AND HORIZONTAL CRIMINAL-LAW LEGISLATION TO PROTECT THE COMMUNITY'S FINANCIAL INTERESTS**

This chapter reviews developments in 1997 regarding horizontal legislation concerning the protection of the Community's financial interests.

Section 1 examines the effective implementation of the Regulation concerning on-the-spot checks and inspections carried out by the Commission, while section 2 reviews significant developments regarding the implementation of the administrative penalties policy. The following section deals with criminal-law protection as it stands. The instruments adopted in 1995 and 1996 have been completed, but still have to be ratified by the Member States. Although some progress has been made in this field this year, this still hampers effective implementation. The chapter concludes with an appraisal of the relevant provisions of the Treaty of Amsterdam and the new opportunities it offers the Community to create a legal environment capable of meeting the challenge of protecting all the Community's interests.

### **5.1. The effective implementation of Council Regulation (Euratom, EC) No 2185/96 concerning on-the-spot checks and inspections carried out by the Commission**

1 January 1997 saw the entry into force of Council Regulation (Euratom, EC) No 2185/96 concerning on-the-spot checks and inspections carried out by the Commission in order to protect the European Communities' financial interests against fraud and other irregularities.

The on-the-spot checks Regulation was applied on eight occasions from the beginning of the second quarter. There were no serious disputes about the respective roles of Commission and national inspectors.

In 1997, the Commission firstly decided on a list of staff empowered to carry out the checks and inspections and the form of authorisation the inspectors need to carry with them under Article 6(1) of the

regulation. It also decided on the form of the inspection order, which indicates the subject-matter and purpose of the on-the-spot check or inspection.

In accordance with an undertaking given to the Council when the Regulation was adopted, the Commission has also produced a vade-mecum on the way staff are to apply the new Regulation.

The partnership with Member States, the basic principle underlying on-the-spot checks, has worked well, with the inspections being carried out jointly as allowed by Article 4 of the Regulation. There has been cooperation at the various stages of the inspections.

The spirit of partnership between the Commission and the Member States continued to prevail when it came to evaluating the results, with both working together to produce an initial inspection report. Under the Regulation, this task falls to the Commission, but the report may be countersigned by national inspectors when an inspection is conducted jointly.

The findings of on-the-spot inspections are recorded in a mission report prepared by the Commission, which is directly usable in national proceedings. This is a key element of the anti-fraud strategy, enabling evidence to be placed before the competent authorities and courts. The partnership will need to be equally constructive when it comes to monitoring administrative penalties and measures and the judicial action to be taken in cases where fraud is shown to have been committed.

In 1997, the Commission's powers of investigation under the Regulation were used in six Member States (Belgium, France, Germany, Greece, Spain and the United Kingdom) in the customs, agriculture and fisheries sectors.

In 1998 the Regulation is likely to be applied more frequently, involving all the Member

States and all the Community's fields of activity, demonstrating that it is a horizontal measure for investigating serious or transnational fraud in partnership with the Member States.

## **5.2. The implementation of penalties policy**

Council Regulation (EC, Euratom) No 2988/95 covers all Community penalties, including sectoral penalties already in existence when it came into force.<sup>97</sup>

Apart from penalties, the impact of a standard legal framework as set out by the Regulation must also be considered in relation to the obligation for Member States to notify the Commission of cases of fraud and other irregularities pursuant to sectoral regulations.<sup>98</sup> To fulfil their notification requirements in a homogenous and horizontal manner, Member States must base their activities on the definitions of the concepts of irregularity, abuse of law and economic operator.<sup>99</sup>

On the basis of the legal framework established by Council Regulation No 2988/95, the Commission is pursuing its policy of introducing administrative penalties into the fields of own resources and direct expenditure. As part of its 1997/8 anti-fraud work programme, it is drawing up a draft European Parliament and Council Regulation establishing administrative penalties in the customs sector and is in the process of conducting a study to establish the degree of reorganisation that will be needed for Community administrative penalties to be incorporated in direct expenditure schemes.

## **5.3. Protection of the Community against irregularities in financial management**

Considering the risk of internal corruption, asked the Commission to present a paper

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<sup>97</sup> OJ L 312, 23.12.1995.

<sup>98</sup> See Chapter 1, section 1.1.

<sup>99</sup> Regulation No 2988/95, Articles 1, 4(3) and 7. Discussions on these points will continue in COCOLAF.

with proposals for an independent UCLAF operating on the basis of an interinstitutional agreement.<sup>100</sup>

The Commission presented a communication on 19 November.<sup>101</sup> It offers avenues to be explored and concludes that the role of UCLAF should be reinforced in the Commission so that the Commission may have effective means of combating all forms of fraud and corruption internally.

## **5.4. Criminal-law protection of the financial interests of the Community**

### *5.4.1. The situation with regard to ratification of the instruments adopted*

The Amsterdam European Council gave a political undertaking to ratify the instruments adopted (Convention on the protection of the Communities' financial interests and the first and second Protocols, and the corruption convention) no later than the middle of 1998.<sup>102</sup>

The difficulties encountered, particularly with regard to ratification, a slow process, have had ramifications for the progress expected to result from the use of this type of instrument for the protection of financial interests.

The European Parliament, of course, is particularly attentive to the results of transposal into national law.

### *5.4.2. The second Protocol on the protection of the Communities' financial interests*

On 19 June the Council adopted the second Protocol on the criminal-law protection of

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<sup>100</sup> Resolution of the European Parliament of 22.10.1997 on the annual report for 1996 and the work programme for 1997/98 for the protection of financial interests and the fight against fraud: OJ C339, 10.11.1997.

<sup>101</sup> SEC(97)2198.

<sup>102</sup> First Protocol on corruption - cf. 1996 Report, p. 48, and section 5.4.3; second protocol, cf. section 5.4.2.

the Communities' financial interests<sup>103</sup> following negotiations conducted by the Italian, Irish (1996) and Netherlands (1997) Council Presidencies, on the basis of the Commission's draft Protocol.<sup>104</sup>

The Protocol to the Convention consists of additional provisions concerning the following:<sup>105</sup>

- *money-laundering related to the proceeds of fraud and corruption*<sup>106</sup>

The provisions making money-laundering a criminal offence will have to be accompanied by an amendment to Council Directive 91/308/EEC of 10 June 1991 on the prevention of the use of the financial system (credit and financial institutions) for the purposes of money laundering<sup>107</sup> to include the laundering of the proceeds of Community fraud in the identification and notification requirements.

- *the liability of legal persons*<sup>108</sup>

These provisions concern the responsibility of legal persons for fraud, corruption and money laundering, which constitute intentional acts, and for lack of supervision or control, which are forms of negligence. Legal persons may be held liable for fraud, corruption and money laundering committed on his own behalf by any person acting either individually or as a member of an organ of the legal person.

Member States must provide for effective, proportionate and dissuasive penalties, which must include criminal or non-criminal fines and possibly the other

penalties specified by the protocol in the event of liability for fraud.

- *confiscation and seizure of the proceeds of fraud*<sup>109</sup>

In the light of recommendations Nos 26 and 28 of the action plan to combat organised crime, adopted by the Council on 28 April, this provision will have to be replaced, as it must be implemented in line with the policy guidelines.

- *cooperation in relation to tax or customs duties offences*<sup>110</sup>

The second Protocol amplifies the Convention's legal framework with regard to extradition in relation to tax and customs duties offences.<sup>111</sup>

- *cooperation with the Commission in the fight against fraud, active and passive corruption and money-laundering*<sup>112</sup>

The second Protocol complements the Convention, which covers judicial cooperation in relation to fraud. It assigns to the Commission (UCLAF) a function in cooperation with the judicial authorities in the fight against fraud, corruption and money laundering. It confirms the Commission's power to contact judicial authorities direct for the protection of the Community's interests. In the area covered by Title VI, this protocol clarifies and amplifies the Commission's cooperation duties flowing from Articles 5 and 209a of the EC Treaty. It will allow an established practice to be developed in response to needs on the ground relating to prosecutions.<sup>113</sup>

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<sup>103</sup> OJ C 221, 19.7.1997.

<sup>104</sup> OJ C 83, 20.3.1996.

<sup>105</sup> Additional provisions provided for by the Council Act of 26 July 1995 establishing the abovementioned Convention.

<sup>106</sup> Articles 1 and 2.

<sup>107</sup> OJ L 166, 28.6.1991.

<sup>108</sup> Articles 3 and 4.

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<sup>109</sup> Article 5.

<sup>110</sup> Article 6.

<sup>111</sup> Article 5(3) of the Convention.

<sup>112</sup> Article 7.

<sup>113</sup> Cf. chapter 3, section 3.4.2.

### 5.4.3. *Public procurement policy and the fight against corruption*

The fight against corruption is gaining fresh momentum, primarily as a consequence of the publication in November 1996 of a Green Paper on public procurement in the European Union, with contributions from numerous key actors (Member States, institutions, economic operators). In 1997 the Commission analysed these contributions, and its findings will be reflected in a proposal, to be published in 1998, containing a range of measures to increase the transparency of award procedures in line with its communication on corruption.

The Green Paper highlighted the importance of adapting procedures for public procurement to render Union policy in the fight against corruption more effective.

#### 5.4.3.1. The Protocol and the Convention against corruption

In the Member States, corruption on the part of European Community officials or other foreign officials is not treated as a criminal offence. This creates a problem, particularly in relation to the Community budget. In 1995, the Spanish Council Presidency accordingly proposed what became the first Protocol to the Convention on the protection of the Communities' financial interests. The Protocol makes active or passive corruption on the part of a Community official or an official from any other Member State a criminal offence in all Member states if the Communities' financial interests are damaged.<sup>114</sup>

A Convention was then drafted, taking the first Protocol as a model, to make any form of active or passive corruption involving officials from the European institutions or Member States a criminal offence, even if their conduct had no bearing on the Union's financial interests. It was adopted on 26 May.<sup>115</sup> It enabled the Member States to

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<sup>114</sup> OJ C 313, 23.10.1996. Cf. page 18 of the 1995 report and Chapter 6 of the 1996 report, p. 48.

<sup>115</sup> OJ C 195, 25.6.1997.

adopt joint positions in Council of Europe and OECD (Organisation for Economic Cooperation and Development) discussions on the fight against corruption.<sup>116</sup>

#### 5.4.3.2. The Commission communication on corruption

In its communication of 21 May<sup>117</sup>, the Commission drew attention to the fact that corruption damages the financial interests of the Union. The communication advocates a coherent Union strategy to "squeeze out" opportunities for corruption. The areas include non-tax deductibility of bribes, public procurement, financial transactions, blacklisting, civil remedies, external assistance and co-operation.

Exclusion possibilities already exist under the Public Procurement Directives<sup>118</sup> and under the FEOGA guarantee scheme. An examination of the circumstances in which blacklisting could be introduced to cover all areas of Community spending has also begun.

Also important is the achievement of a fully co-ordinated anti-corruption strategy in relation to external aid and assistance. A recent Commission communication<sup>119</sup> sets down prevention measures and sanctions necessary for dealing effectively with fraud and corruption which harms the objective of "good governance".

The Action Plan on combating organised crime endorsed by the Amsterdam European Council last June called for a comprehensive policy against corruption. As a response the Commission will report on the implementation of the Communication.

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<sup>116</sup> Common positions of 6.10.1997 (OJ L 279, 13.10.1997) and 13.11.1997 (OJ L 320, 21.11.1997).

<sup>117</sup> COM(97) 192 final.

<sup>118</sup> Directives 92/50/EEC (OJ L 209, 24.7.1992), 93/36/EEC, 93/37/EEC and 93/38/EEC (OJ L 199, 9.8.1993).

<sup>119</sup> COM(98)146 final.



## 5.5. The Amsterdam Treaty

The Commission's efforts to create a legal basis for the criminal-law protection of the Communities' financial interests initially led to the adoption of Article 209a of the EC Treaty, which links the financial interests of the Community with national financial interests and the Member States' duty to cooperate with the Commission's duty to assist them. There is currently a major information-gathering exercise on the application of this Article and the Commission will report on the results in 1998.

In its opinion on the holding of an Intergovernmental Conference (IGC),<sup>120</sup> the objectives defined by the Commission were the fight against different forms of crime and fraud damaging to the Communities' financial interests and the development of effective cooperation between the national administrations concerned.

The Commission supported the proposal that Article 209a of the EC Treaty be amended to enlarge and align the legal bases available for the protection of the Communities' financial interests.

### 5.5.1. *The new Article 280 of the EC Treaty*

While Article 209a of the EC Treaty emphasised the special responsibility of the Member States' national authorities for the protection of the Communities' financial interests, the new Article 280 of the EC Treaty shares the responsibility between the Community and the Member States.<sup>121</sup>

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<sup>120</sup> Opinion given under Article N of the Union Treaty, COM(96) 90.

<sup>121</sup> Article 280 reads:

'1. The Community and the Member States shall counter fraud and any other illegal activities affecting the financial interests of the Community through measures to be taken in accordance with this Article, which shall act as a deterrent and be such as to afford effective protection in the Member States.

2. Member States shall take the same measures to counter fraud affecting the financial interests of the Community as they take to counter fraud affecting their own financial interests.

### 5.5.2. *Approaching deadlines*

Article 280 is now up for ratification by the Member States, with the rest of the Amsterdam Treaty. The Treaty will enter into force when ratification procedures have been completed.

If necessary the Commission will propose further legislative measures for the protection of the Communities' financial interests after ascertaining what needs emerge from the practical application of the Treaty.

## 5.6. Prospects for work under Title VI of the Union Treaty

In its Resolutions of 12 June and 22 October,<sup>122</sup> the European Parliament asked the Commission to conduct a feasibility study on the Corpus Juris, which contains criminal-law provisions for the protection of European Union's financial interests and is itself the result of a study carried out by researchers from European Associations of Lawyers at the behest of Parliament.<sup>123</sup>

The aims of the study to be carried out by the Commission are to measure the impact of the Corpus on the current national legal situation, with a view to achieving effective,

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3. Without prejudice to the other provisions of this Treaty, the Member States shall coordinate their action aimed at protecting the financial interests of the Community against fraud. To this end they shall organise, together with the Commission, close and regular cooperation between the competent authorities.

4. The Council, acting in accordance with the procedure referred to in Article 251, after consulting the Court of Auditors, shall adopt the necessary measures in the fields of the prevention of and fight against fraud affecting the financial interests of the Community with a view to affording effective and equivalent protection in the Member States. These measures shall not concern the application of national criminal law or the national administration of justice.

5. The Commission, in cooperation with Member States, shall each year submit to the European Parliament and to the Council a report on the measures taken for the implementation of this Article.'

<sup>122</sup> European Parliament Resolution of 12.6.1997 on the creation of a European legal and judicial area to protect the European Union's financial interests against international crime (OJ C 200, 30.6.1997) and Resolution of 22.10.1997 (*supra*).

<sup>123</sup> The associations of lawyers exist in every Member State. They were set up on the Commission's initiative.

proportionate and dissuasive protection of Community interests as required by the EC Treaty, taking account of the new possibilities offered by the Treaty of Amsterdam.

The analysis conducted during the preparation of the Corpus demonstrated that assimilation did not guarantee effectiveness. The same applies to the principle of cooperation and to harmonisation, which makes criminal-law protection so complex.

During the preparatory stage itself, before the judgment stage, the discrepancies seemed greatest and the obstacles most numerous.

This is why the Corpus proposes a set of rules covering criminal prosecutions to ensure simpler and more effective enforcement in a European law-enforcement area.<sup>124</sup>

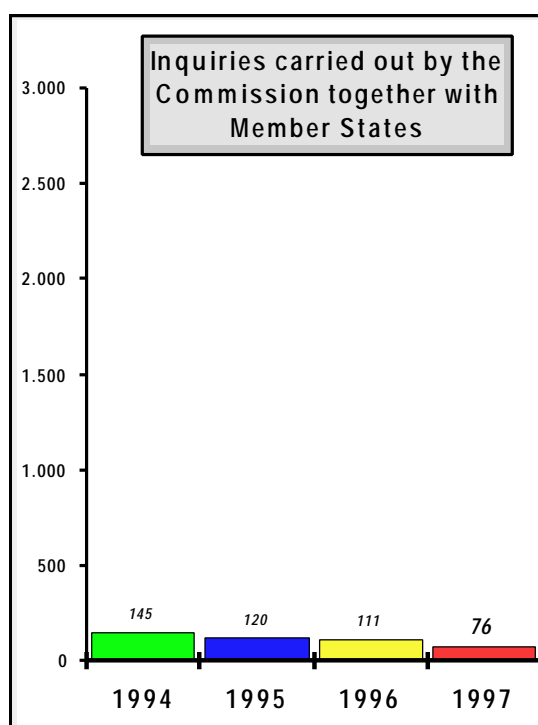
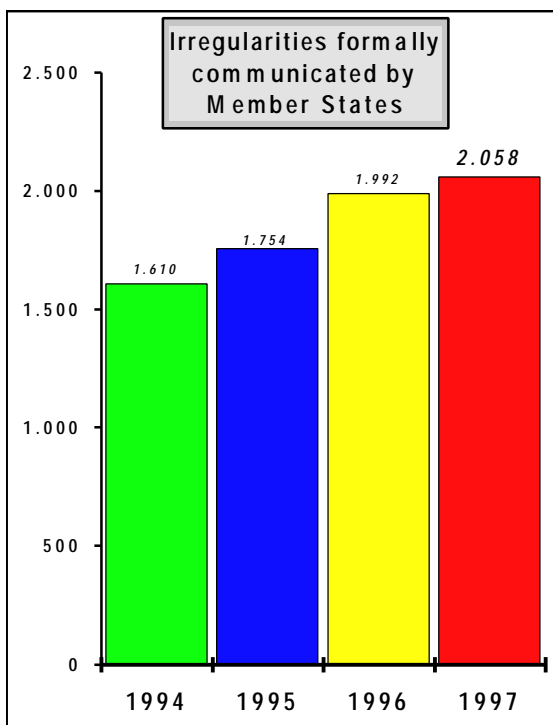
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<sup>124</sup> This is why the Corpus Juris calls for the establishment of a European Public Prosecutor's Office.

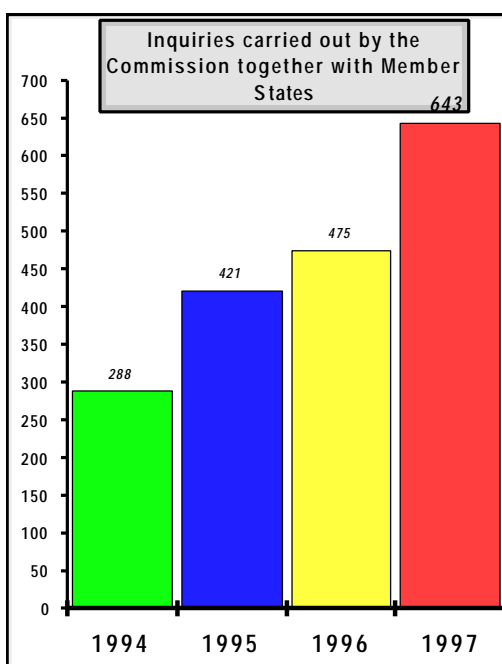
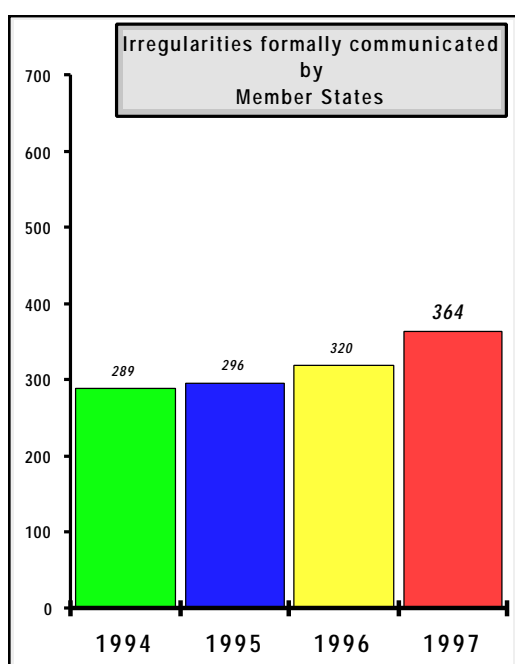
# TRADITIONAL OWN RESOURCES

1994 - 1997

## NUMBER OF CASES



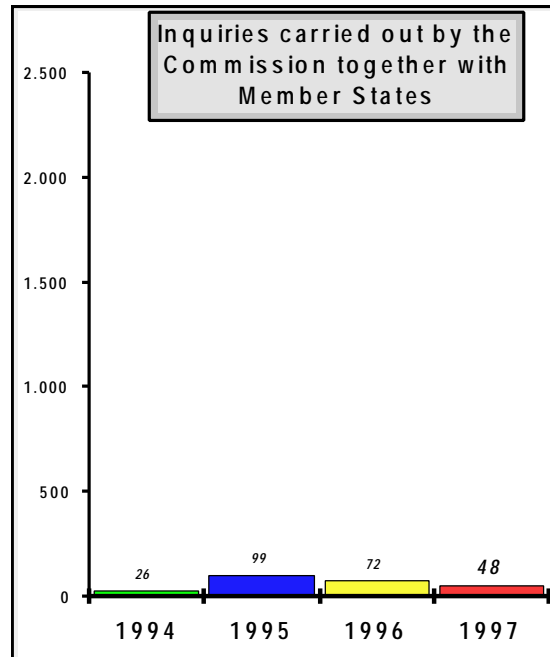
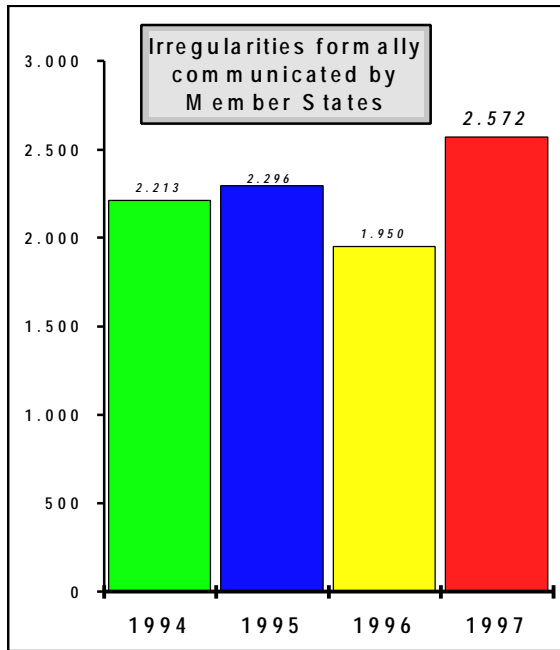
## AMOUNTS in MILLIONS of ECU



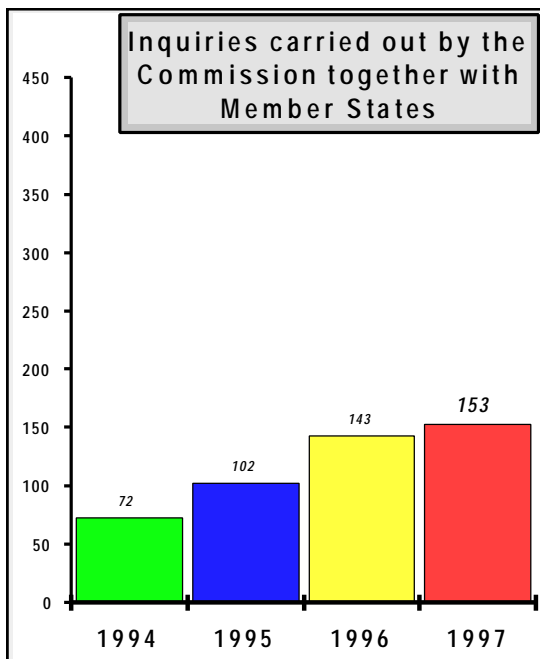
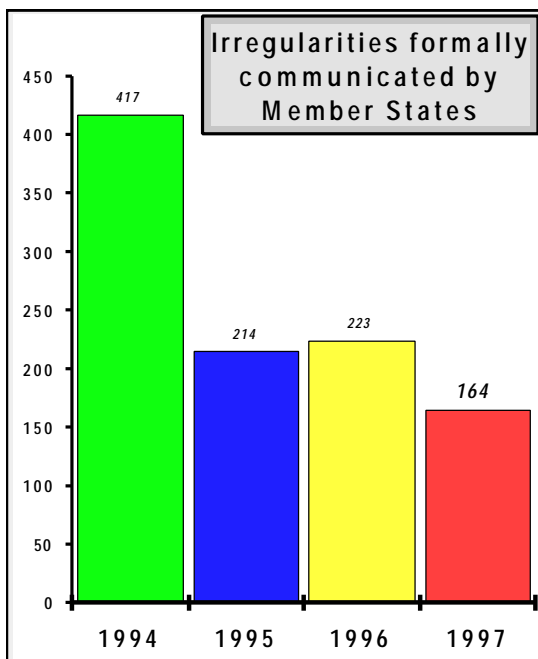
# EAGGF - GUARANTEE

1994 - 1997

## NUMBER OF CASES



## AMOUNTS in MILLIONS of ECU

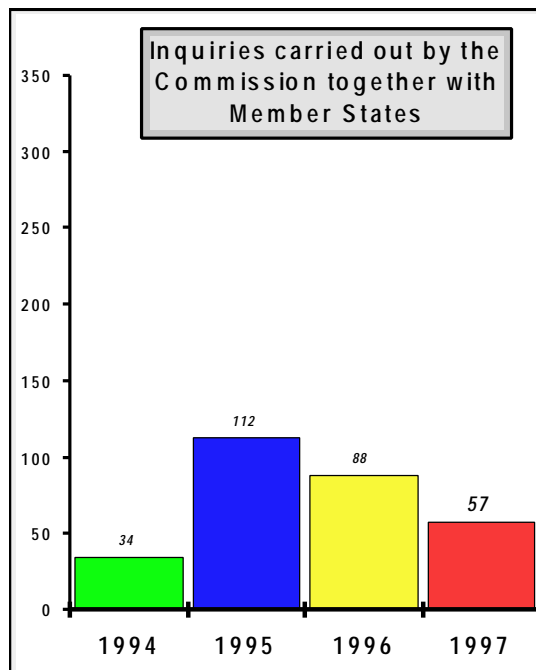
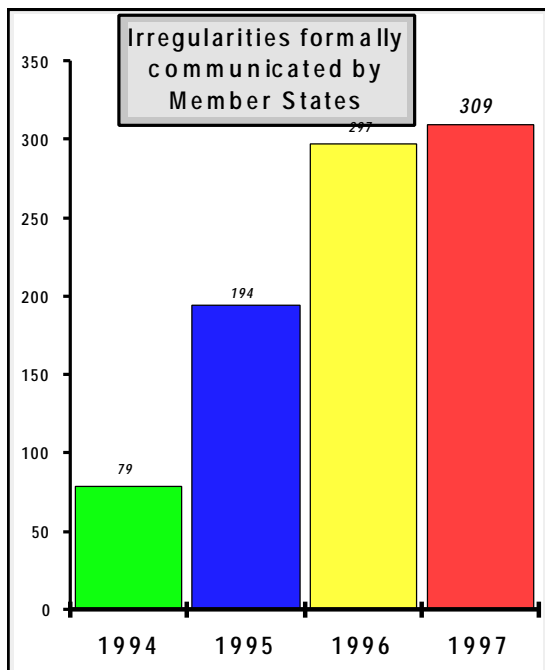


Communicated under Regulation (EEC) 595/91

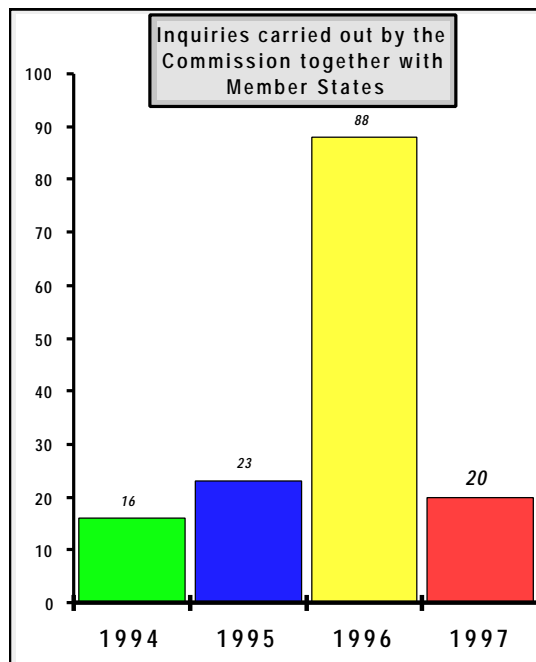
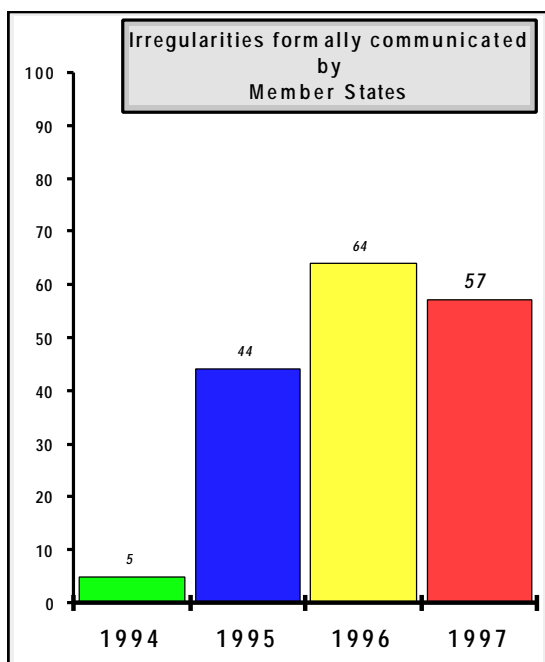
# STRUCTURAL ACTIONS

1994 - 1997

## NUMBER OF CASES



## AMOUNTS in MILLIONS of ECU



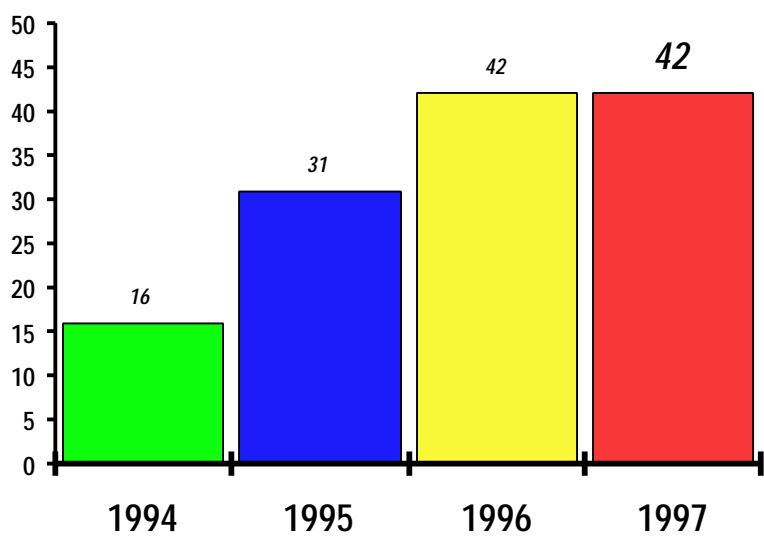
Communicated under Regulations (EEC) 1681/94 and 1831/94

# DIRECT EXPENDITURE

1994 - 1997

Inquiries carried out by the Commission with the assistance of Member States' services.

## NUMBER OF CASES



## AMOUNTS in MILLIONS of ECU

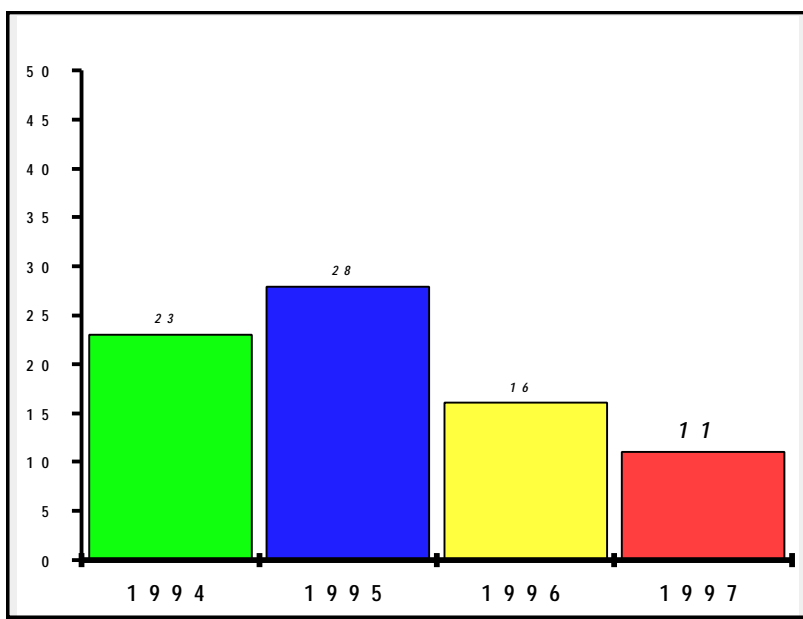


Table 1

# TRADITIONAL OWN RESOURCES

## IRREGULARITIES COMMUNICATED BY MEMBER STATES IN 1997 ON THE BASIS OF REGULATION (EEC) 1552/89

|                | NUMBER OF<br>CASES<br>NOTIFIED | AMOUNTS X 1.000 ECU (rate of December 1997) |                      |                  |    |
|----------------|--------------------------------|---|----------------------|------------------|----|
|                |                                | AMOUNTS<br>NOTIFIED                         | already<br>RECOVERED | BALANCE (1)      |    |
|                | a                              | b   | c                    | d = b - c        |    |
| BELGIOUE       | 405                            | 45.593                                      | 1.937                | 43.656           | BE |
| DANMARK        | 82                             | 8.244                                       | 5.359                | 2.885            | DK |
| DEUTSCHLAND    | 384                            | 28.624                                      | 5.473                | 23.151           | DE |
| ELLAS          | 5                              | 3.980                                       | 11                   | 3.970            | EL |
| ESPAÑA         | 75                             | 3.522                                       | 1.362                | 2.160            | ES |
| FRANCE         | 233                            | 32.332                                      | 8.722                | 23.610           | FR |
| IRELAND        | 54                             | 3.990                                       | 2.480                | 1.510            | IR |
| ITALIA         | 298                            | 88.398                                      | 155                  | 88.243           | IT |
| LUXEMBOURG     | 1                              | 12  | 12                   | 0                | LU |
| NEDERLAND (2)  | 453                            | 39.178                                      | ...                  | ...              | NL |
| ÖSTERREICH     | 73                             | 5.966                                       | 611                  | 5.355            | ÖS |
| PORTUGAL (2)   | 5                              | 6.037                                       | ...                  | ...              | PO |
| SUOMI          | 32                             | 1.678                                       | 1.561                | 117              | SU |
| SVERIGE        | 17                             | 576   | 401                  | 175              | SV |
| UNITED KINGDOM | 455                            | 95.380                                      | 23.240               | 72.140           | UK |
| <b>TOTAL</b>   | <b>2.572</b>                   | <b>363.511</b>                              | <b>51.324 #</b>      | <b>266.972 #</b> |    |

(1) The balance consists of a) amounts still to be recovered ; b) corrections to be made following Court decisions still to be awaited ;  
c) remissions/cancellations decided by national authorities and d) amounts which cannot be recovered and must subsequently be written off.

(2) The amounts recovered have not yet been communicated.

# = Total amount for 13 Member states only



Table 2

# EAGGF - GUARANTEE

## IRREGULARITIES COMMUNICATED BY MEMBER STATES IN 1997 ON THE BASIS OF REGULATION (EEC) 595/91

|                | NUMBER OF CASES            |  | AMOUNTS X 1.000 ECU ( rate of December 1997 ) |   |                                   |                      |                    |    |
|----------------|----------------------------|--|---|---|-----------------------------------|----------------------|--------------------|----|
|                | total<br>CASES<br>NOTIFIED | of which DETECTED<br>BEFORE<br>PAYMENT | TOTAL<br>AMOUNTS<br>NOTIFIED                  | of which WITHOUT<br>RECOVERY :<br>detected before payment | of which AMOUNTS NEEDING RECOVERY |                      |                    |    |
|                |                            |  |   |   | AMOUNTS<br>NOTIFIED               | already<br>RECOVERED | TO BE<br>RECOVERED |    |
|                | <i>a</i>                   | <i>b</i>                               | <i>c</i>                                      | <i>d</i>  | <i>e</i>                          | <i>f</i>             | <i>g = e - f</i>   |    |
| BELGIQUE       | 27                         | 0                                      | 1.672   | 379   | 1.294                             | 267                  | 1.026              | BE |
| DANMARK        | 24                         | 3                                      | 419   | 42  | 377                               | 343                  | 33                 | DK |
| DEUTSCHLAND    | 601                        | 95                                     | 26.865  | 2.204   | 24.662                            | 5.801                | 18.861             | DE |
| ELLAS          | 160                        | 66                                     | 36.931  | 3.793   | 33.138                            | 164                  | 32.975             | EL |
| ESPANA         | 261                        | 2                                      | 43.449  | 16.402  | 27.047                            | 1.568                | 25.479             | ES |
| FRANCE         | 91                         | 12                                     | 3.801   | 1.046   | 2.755                             | 828                  | 1.927              | FR |
| IRELAND        | 79                         | 63                                     | 693   | 472   | 221                               | 69                   | 152                | IR |
| ITALIA         | 249                        | 1                                      | 31.352  | 20  | 31.331                            | 606                  | 30.726             | IT |
| NEDERLAND      | 130                        | 58                                     | 7.666   | 4.542   | 3.124                             | 582                  | 2.542              | NL |
| ÖSTERREICH     | 36                         | 14                                     | 234   | 11  | 223                               | 204                  | 19                 | ÖS |
| PORTUGAL       | 81                         | 2                                      | 4.378   | 41  | 4.337                             | 287                  | 4.051              | PO |
| SUOMI          | 7                          | 6                                      | 75  | 43  | 32                                | 32                   | 0                  | SU |
| SVERIGE        | 66                         | 59                                     | 735   | 585   | 150                               | 104                  | 46                 | SV |
| UNITED KINGDOM | 246                        | 31                                     | 6.221   | 1.003   | 5.218                             | 1.166                | 4.052              | UK |
| <i>TOTAL</i>   | <i>2.058</i>               | <i>412</i>                             | <i>164.490</i>                                | <i>30.581</i>   | <i>133.909</i>                    | <i>12.021</i>        | <i>121.888</i>     |    |

Table 3

# STRUCTURAL ACTIONS

IRREGULARITIES COMMUNICATED BY MEMBER STATES IN 1997  
ON THE BASIS OF REGULATION (EEC) 1681/94 and 1831/94

AMOUNTS X 1.000 ECU (rate December 1997)

|                | EAGGF-GUIDANCE  |                  | ESF             |                  | ERDF            |                  | FISHERIES       |                  | COHESION FUND   |                  | TOTAL           |                  |    |
|----------------|-----------------|------------------|-----------------|------------------|-----------------|------------------|-----------------|------------------|-----------------|------------------|-----------------|------------------|----|
|                | number of cases | amounts notified | number of cases | amounts notified | number of cases | amounts notified | number of cases | amounts notified | number of cases | amounts notified | number of cases | amounts notified |    |
| BELGIQUE       | 5               | 271              | 2               | 27               | 5               | 247              | 0               | 0                | 0               | 0                | 12              | 545              | BE |
| DANMARK        | 0               | 0                | 0               | 0                | 0               | 0                | 0               | 0                | 0               | 0                | 0               | 0                | DK |
| DEUTSCHLAND    | 27              | 1.251            | 10              | 4.072            | 10              | 6.347            | 0               | 0                | 0               | 0                | 47              | 11.669           | DE |
| ELLAS          | 4               | 1.419            | 48              | 2.387            | 1               | 0                | 0               | 0                | 0               | 0                | 53              | 3.807            | EL |
| ESPANA         | 5               | 231              | 5               | 151              | 20              | 3.669            | 1               | 64               | 2               | 210              | 33              | 4.324            | ES |
| FRANCE         | 0               | 0                | 6               | 111              | 2               | 227              | 0               | 0                | 0               | 0                | 8               | 337              | FR |
| IRELAND        | 1               | 6                | 0               | 0                | 11              | 1.123            | 3               | 187              | 1               | 1.036            | 16              | 2.351            | IR |
| ITALIA         | 4               | 538              | 26              | 3.563            | 3               | 709              | 0               | 0                | 0               | 0                | 33              | 4.809            | IT |
| LUXEMBOURG     | 0               | 0                | 0               | 0                | 0               | 0                | 0               | 0                | 0               | 0                | 0               | 0                | LU |
| NEDERLAND      | 0               | 0                | 0               | 0                | 0               | 0                | 0               | 0                | 0               | 0                | 0               | 0                | NL |
| ÖSTERREICH     | 0               | 0                | 0               | 0                | 0               | 0                | 0               | 0                | 0               | 0                | 0               | 0                | ÖS |
| PORTUGAL       | 44              | 1.143            | 9               | 5.056            | 15              | 12.219           | 1               | 363              | 0               | 0                | 69              | 18.781           | PO |
| SUOMI          | 1               | 9                | 0               | 0                | 0               | 0                | 0               | 0                | 0               | 0                | 1               | 9                | SU |
| SVERIGE        | 6               | 19               | 10              | 482              | 1               | 63               | 0               | 0                | 0               | 0                | 17              | 564              | SV |
| UNITED KINGDOM | 3               | 751              | 7               | 5.388            | 10              | 3.734            | 0               | 0                | 0               | 0                | 20              | 9.873            | UK |
| <b>TOTAL</b>   | <b>100</b>      | <b>5.636</b>     | <b>123</b>      | <b>21.237</b>    | <b>78</b>       | <b>28.337</b>    | <b>5</b>        | <b>614</b>       | <b>3</b>        | <b>1.246</b>     | <b>309</b>      | <b>57.070</b>    |    |

Table 4

# EAGGF - GUARANTEE

RECOVERY SITUATION regarding IRREGULARITIES  
communicated BEFORE 1994 under Regulation (EEC) 595/91

|                | NUMBER of CASES |                        |                                     |                                |                              |                         |   |
|----------------|-----------------|------------------------|-------------------------------------|--------------------------------|------------------------------|-------------------------|---|
|                | total notified  | <i>total recovered</i> | <i>borne * by EAGGF - Guarantee</i> | <i>borne * by Member State</i> | <i>still to be recovered</i> | <i>whereof in COURT</i> | <i>request by M-S to declare as "irrecoverable"</i> |
|                | 1               | 2                      | 3                                   | 4                              | 5 = (1-2+4)                  | 6                       | 7   |
| BELGIQUE       | 176             | 130                    | 7                                   |                                | 39                           | 10                      | 10  |
| DANMARK        | 482             | 371                    | 89                                  | 1                              | 21                           | 8                       | 13  |
| DEUTSCHLAND    | 1.928           | 1.564                  | 94                                  | 5                              | 265                          | 112                     | 50  |
| ELLAS          | 303             | 249                    |                                     | 9                              | 45                           | 7                       | 1   |
| ESPANA         | 439             | 309                    |                                     |                                | 130                          | 16                      | 1   |
| FRANCE         | 1.002           | 851                    | 40                                  | 2                              | 109                          | 17                      | 18  |
| IRELAND        | 167             | 129                    | 1                                   | 4                              | 33                           | 3                       | 14  |
| ITALIA         | 1.180           | 292                    |                                     |                                | 888                          | 239                     | 1   |
| NEDERLAND      | 723             | 681                    | 2                                   | 1                              | 39                           | 2                       | 10  |
| PORTUGAL       | 218             | 105                    |                                     | 4                              | 109                          | 8                       |   |
| UNITED KINGDOM | 1.525           | 1.319                  | 72                                  | 17                             | 117                          | 10                      | 93  |
| <b>TOTAL</b>   | <b>8.144</b>    | <b>6.000</b>           | <b>305</b>                          | <b>43</b>                      | <b>1.795</b>                 | <b>432</b>              | <b>211</b>  |
|                |                 | <b>74%</b>             |                                     |                                | <b>22%</b>                   |                         |   |

|                | AMOUNTS x 1.000 ECU (rate of december 1997) |                        |                                     |                                |                              |                         |   |
|----------------|---|------------------------|-------------------------------------|--------------------------------|------------------------------|-------------------------|---|
|                | total notified                              | <i>total recovered</i> | <i>borne * by EAGGF - Guarantee</i> | <i>borne * by Member State</i> | <i>still to be recovered</i> | <i>whereof in COURT</i> | <i>request by M-S to declare as "irrecoverable"</i> |
|                | 1   | 2                      | 3                                   | 4                              | 5 = (1-2+4)                  | 6                       | 7   |
| BELGIQUE       | 23.385                                      | 9.587                  | 6.169                               | 0                              | 7.629                        | 1.593                   | 3.211   |
| DANMARK        | 28.586                                      | 13.872                 | 1.331                               | 2                              | 13.382                       | 10.815                  | 2.567   |
| DEUTSCHLAND    | 170.923                                     | 51.708                 | 52.233                              | 27.645                         | 39.337                       | 22.800                  | 11.566  |
| ELLAS          | 78.154                                      | 3.582                  | 0                                   | 53.981                         | 20.592                       | 15.279                  | 0   |
| ESPANA         | 9.355                                       | 3.274                  | 0                                   | 0                              | 6.081                        | 584                     | 0   |
| FRANCE         | 72.174                                      | 31.651                 | 1.102                               | 12                             | 39.408                       | 14.067                  | 2.483   |
| IRELAND        | 18.188                                      | 12.464                 | 17                                  | 23                             | 5.684                        | 2.609                   | 0   |
| ITALIA         | 577.638                                     | 48.360                 | 0                                   | 0                              | 529.278                      | 207.970                 | 0   |
| NEDERLAND      | 36.481                                      | 25.915                 | 36                                  | 218                            | 10.312                       | 1.433                   | 158   |
| PORTUGAL       | 9.189                                       | 2.009                  | 0                                   | 496                            | 6.684                        | 3.596                   | 0   |
| UNITED KINGDOM | 45.777                                      | 22.601                 | 3.357                               | 1.641                          | 18.178                       | 1.756                   | 7.008   |
| <b>TOTAL</b>   | <b>1.069.850</b>                            | <b>225.023</b>         | <b>64.245</b>                       | <b>84.018</b>                  | <b>696.563</b>               | <b>282.501</b>          | <b>26.993</b>                                       |
|                |   | <b>21%</b>             |                                     |                                | <b>65%</b>                   |                         |   |

\* irrecoverable : formal decision in the clearance of account procedure under regulation (EEC) 729/70

Table 5

**GLOBAL IMPACT of IRREGULARITIES**  
communicated / detected in 1996 en 1997 - in relation to  
the COMMUNITY BUDGET for 1996 and 1997

| <b>Traditional Own Resources<br/>collected by the Member States</b>                     | <b>1996</b>   |             | <b>1997</b>   |             |
|---|---------------|-------------|---------------|-------------|
|   | <i>MECU</i>   | <i>%</i>    | <i>MECU</i>   | <i>%</i>    |
| <b>BUDGET</b>   | <b>14.942</b> |             | <b>15.589</b> |             |
| Irregularities communicated by Member States  | <b>320</b>    | <b>2,14</b> | <b>364</b>    | <b>2,33</b> |
| Irregularities detected by the Commission services<br>in cooperation with Member States | <b>476</b>    | <b>3,19</b> | <b>643</b>    | <b>4,12</b> |
| <b>Global impact of irregularities</b>  | <b>796</b>    | <b>5,33</b> | <b>1.007</b>  | <b>6,45</b> |

| <b>Expenditures concerning<br/>Structural Actions</b>                                   | <b>1996</b>   |             | <b>1997</b>   |             |
|---|---------------|-------------|---------------|-------------|
|   | <i>MECU</i>   | <i>%</i>    | <i>MECU</i>   | <i>%</i>    |
| <b>BUDGET</b>   | <b>24.320</b> |             | <b>26.048</b> |             |
| Irregularities communicated by Member States  | <b>64</b>     | <b>0,26</b> | <b>57</b>     | <b>0,23</b> |
| Irregularities detected by the Commission services<br>in cooperation with Member States | <b>88</b>     | <b>0,36</b> | <b>20</b>     | <b>0,08</b> |
| <b>Global impact of irregularities</b>  | <b>152</b>    | <b>0,62</b> | <b>77</b>     | <b>0,31</b> |

| <b>Agricultural Expenditure concerning<br/>EAGGF-Guarantee measures.</b>                | <b>1996</b>   |             | <b>1997</b>   |             |
|---|---------------|-------------|---------------|-------------|
|   | <i>MECU</i>   | <i>%</i>    | <i>MECU</i>   | <i>%</i>    |
| <b>BUDGET</b>   | <b>42.799</b> |             | <b>40.423</b> |             |
| Irregularities communicated by Member States  | <b>223</b>    | <b>0,52</b> | <b>164</b>    | <b>0,41</b> |
| Irregularities detected by the Commission services<br>in cooperation with Member States | <b>142</b>    | <b>0,33</b> | <b>153</b>    | <b>0,38</b> |
| <b>Global impact of irregularities</b>  | <b>365</b>    | <b>0,85</b> | <b>317</b>    | <b>0,79</b> |

*MECU* = amounts in MILLION ECU : rate of December 1997

General remark : the irregularities detected / communicated in 1997 often relate to previous budgetary years.

## GLOSSARY

### Definition of the concept of irregularity

The Council regulation (EC) No 2988/95 on the protection of the European Communities financial interests (OJ No L 312 of 23.12.95) defines very broadly the concept of irregularity. This concept covers both simple omission due to error or negligence which is likely to have a harmful effect on the Communities' budget and intentional and deliberate acts which corresponds for their part to the more restrictive concept of fraud as defined in the penal convention.

Council Regulation (EC, Euratom) No 2988/95 of 18 December 1995 on the protection of the European Communities financial interests (OJ No L 312 of 23.12.95).

Article 1, § 2 :

“ ‘Irregularity’ shall mean any infringement of a provision of Community law resulting from an act or omission by an economic operator, which has, or would have, the effect of prejudicing the general budget of the Communities or budgets managed by them, either by reducing or losing revenue accruing from own resources collected directly on behalf of the Communities, or by an unjustified item of expenditure”.

Council Act of 26 July on drawing up the Convention on the protection of the European Communities' financial interests (OJ No C 316 of 27.11.95).

Article 1 § 1 :

“For the purposes of this Convention, fraud affecting the European Communities' financial interests shall consist of :

- (a) in respect of expenditure, any intentional act or omission relating to :
  - the use or presentation of false, incorrect or incomplete statements or documents, which has as its effect the disappropriation or wrongful retention of funds from the general budget of the European Communities or budgets managed by , or on behalf of, the European Communities,
  - non-disclosure of information in violation of a specific obligation, with the same effect,
  - the misapplication of such funds for purposes other than those for which they are originally granted;
- (b) in respect of revenue, any intentional act on omission relating to :
  - the use or presentation of false, incorrect or incomplete statements or documents, which has as its effect the illegal diminution of the resources of the general budget of the European Communities or budgets managed by, or on behalf of, the European Communities,
  - non-disclosure of information in violation of a specific obligation, with the same effect,
  - misapplication of a legally obtained benefit, with the same effect.

The Member States notify the Commission of irregularities where a mutual administrative report has been made. The Commission, for its part, carries out, in cooperation with the specialist national services, investigations into cases of irregularity which have not been the subject of such a report by the Member States but where there is, according to diverse information sources, a strong presumption of fraud.

### Organised crime

The Council report on organised crime in the European Union offers a number of criteria for defining organised crime:

- more than one participant;
- specific functions exercised by each participant, with a degree of discipline and control;
- international activity;
- use of violence or other forms of coercion;
- money-laundering;
- use of business or businesslike structures;
- profit motive;
- influence over political and business circles, public administration, the media and the judiciary.

|              |  |
|--------------|--|
| Agenda 2000: | Commission Communication on enlargement – horizon 2000   |
| ASEAN:       | Association of South-East Asian Nations  |
| CAP:         | Common Agricultural Policy   |
| CIS:         | Customs Information System   |
| COCOLAF:     | French acronym for Advisory Committee for the Coordination of Fraud Prevention   |
| CPCA:        | French acronym for Standing Committee for Administrative Cooperation (indirect taxation). Chaired by the Commission, Directorate-General for Customs and Indirect Taxation (DG XXI). Deals with implementation of the transitional intra-Community VAT system. |
| EAGGF:       | European Agricultural Guidance and Guarantee Fund (Guarantee Section: EAGGF - Guarantee, Guidance Section: EAGGF - Guidance)   |
| EC:          | European Community (name used since entry into force of the Treaty on European Union)  |
| EDF:         | European Development Fund  |
| EDF:         | European Development Fund  |
| EFTA:        | European Free Trade Area (Iceland, Liechtenstein, Norway, Switzerland)   |
| EMU:         | Economic and Monetary Union  |
| ERDF:        | European Regional Development Fund   |
| ESF:         | European Social Fund   |
| EWS:         | Early Warning System   |
| FIFG:        | Financial Instrument for Fisheries Guidance  |
| GSP:         | Generalised System of Preferences  |
| IRENE:       | French acronym for database managed by UCLAF - Irregularities, Inquiries,  |
| OECD:        | Organisation for Economic Cooperation and Development  |
| OJ:          | Official Journal of the European Communities (OJ L: L series, OJ C: C series)  |
| PHARE:       | Programme of Community aid for central and eastern European countries  |
| RTD:         | Research and technological development   |
| SCAF:        | French acronym for Anti-fraud Sub-committee of the CPCA, dealing with indirect taxation.   |
| SCENT:       | System for a Customs Enforcement Network   |
| SEM 2000:    | Sound and Efficient Management - Commission programme for improving the management of Community finances by the year 2000  |
| TACIS:       | Programme of technical assistance to the Independent States of the former Soviet Union and Mongolia  |
| TIR:         | Transport International Routier  |
| TUE:         | Treaty on European Union   |
| UCLAF:       | Unit for the Coordination of Fraud Prevention (Directorate within the Commission's Secretariat-General)  |
| VAT:         | Value Added tax  |
| VIIES:       | VAT Information Exchange System  |