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

**Ninth report from the Commission on the operation of the inspection arrangements for
traditional own resources (2016–2018) Article 6(3) of Council Regulation (EC, Euratom)
No 608/2014 of 26 May 2014**

1. INTRODUCTION

The Commission reports every three years¹ to the European Parliament and to the Council on the functioning of the inspection arrangements for traditional own resources (TOR)².

From 2016 to 2018, more than EUR 60 billion was made available (net) with a yearly average of more than EUR 20 billion. This represents an increase of 20% compared with the period 2013-2015.

The TOR inspections are based on Council Decision 2014/335/EU, Euratom of 26 May 2014³, Council Regulation (EU, Euratom) No 608/2014 of 26 May 2014⁴ and Council Regulation (EU, Euratom) No 609/2014 of 26 May 2014⁵.

This document describes and analyses the operation of the inspection system for TOR for the period from 2016 to 2018⁶. It reports on the inspections carried out by the European Commission on traditional own resources over this period and includes other activities performed to protect the financial interests of the EU:

- the on-the-spot inspections carried out by the Commission in Member States and their follow-up;
- the follow-up of the European Court of Auditors' preliminary findings letters;
- the examination of irrecoverable entitlements that have been written off (WOMIS);
- the treatment of Member States' errors leading to a loss of traditional own resources;
- the management of the database relating to fraud and irregularities (OWNRES);
- the second pilot project on audit of A and B accounts by Member States;
- the assistance to the candidate countries.

2. TOR INSPECTIONS' FRAMEWORK AND METHODOLOGY

2.1. TOR regulatory and operational framework

The collection of TOR is delegated to the Member States by law. They must make the duties collected available⁷ to the EU budget and retain a 20% flat rate of all amounts of TOR made available to the Commission⁸ as compensation for collection costs, independently of the costs

¹ Article 6(3) of Regulation No 608/2014

² Customs duties on products imported from third countries, plus sugar levies.

³ OJ L 168, 07.6.2014, p. 105

⁴ OJ L 168, 07.6.2014, p. 29

⁵ OJ L 168, 07.6.2014, p. 39, as amended by Council Regulation No 804/2016 of 17 May 2016 (OJ L 132, 21.05.2016, p. 85)

⁶ The report focuses on the checks made by the EU institutions (the Commission and the Court of Auditors). It does not cover the checks made by the Member States, the detailed results of which are set out in the annual report drawn up under Article 325 of the Treaty on the Functioning of the European Union.

⁷ With this term, the legislation refers to the payments made by the Member States to the EU budget.

⁸ Over the years, this percentage has changed from 10% for amounts made available before 28 February 2001 to 25% for amounts made available from 1 March 2001 to 28 February 2014. For amounts made available after 1 March 2014 the percentage to be applied is 20%.

actually incurred. The Member States are required to carry out checks themselves and to report to the Commission.

Nevertheless, the Commission retains important inspection powers in this field. In this context, the on-the-spot inspections are important tools to supervise the system for the collection of TOR by performing several types of checks⁹ on Member States' regulations and documents.

The Commission is also required to respond to the observations made by the Court of Auditors in its Annual Report, special reports or preliminary findings letters and to the observations and recommendations made by the European Parliament during the discharge procedure in respect of the implementation of the budget. The Commission ensures that the Member States apply the EU rules correctly and reports to the budgetary authority.

The Commission's inspection activities have three main objectives:

- To maintain a level playing field between Member States and economic operators, regardless of where the goods are cleared through customs in the EU to prevent distortions of competition;
- To improve the recovery of TOR. The Commission must reassure itself that the Member States comply with their responsibilities when it comes to collecting and making available TOR. The Commission inspects the actions taken by the Member States concerning the recovery of TOR including the timely notification of the customs debt and the enforcement procedures deemed necessary;
- To inform the budgetary authority. From the inspection findings the Commission is able to judge the effectiveness and diligence of the Member States with regard to the collection and making available of TOR, to take the measures necessary to remedy any shortcomings and ultimately to report to the budgetary authority.

Furthermore, the inspections contribute to ensuring the effective functioning of the Customs Union and the uniform application of EU rules to avoid loopholes where fraudsters can take advantage or circumvent the duties to be paid.

From 1 May 2016, a new customs legislation became applicable and a new own resources legislative framework for the period 2014 - 2020 is retroactively applied from 1 January 2014. In addition, the continuous development of trade facilitation and simplifications complicate the TOR controls carried out by the Commission and the Member States.

⁹ **On regulations:** checks on Member States' provisions concerning the system for collecting TOR. **On documents:** analysis of accounting statements and all kind of accounting documents and files from Member States, including Member States' reports on irrecoverable entitlements. **On-the-spot inspections:** check on the conformity with EU legislation of national systems and underlying documents from both the accounting and customs perspective. These inspections are carried out autonomously or jointly with the Member States concerned.

2.2. Objectives and methodology of TOR on-the-spot inspections

The main objective of the inspections on traditional own resources is to gain assurance that the procedures in place in the Member States comply with the relevant EU legislation and that the EU's financial interests are appropriately and homogeneously protected wherever the goods are cleared. Each year, the inspections focus on various customs and accounting topics. The final effect is the harmonisation and the enhancement of the procedures in place in the Member States in order to protect efficiently and effectively the financial interests of EU in a consistent manner.

The Commission's on-the-spot inspections are based on a precise methodology and are planned as part of an annual inspection programme based on risk analysis and containing a number of topics to be inspected in one or more Member States.

All the inspections are carried out using standardised procedures and involve the use of tailor-made audit tools to ensure that the inspections are carried out and that the reports are drafted in a consistent manner.

In addition, an audit pilot was launched in 2014 and in 2016 on the audit of A and B accounts management to be carried out by the Member States themselves. Even if the results were generally positive, the Commission services decided to discontinue this joint work because the expected synergies and efficiencies were not realised.

3. TOR INSPECTIONS CARRIED OUT BY THE COMMISSION OVER THE PERIOD 2016-2018

During the period 2016-2018 the Commission carried out **68 inspections** giving rise to 233 findings under Article 2 of Regulation No 608/2014. Four of these inspections were carried out under the Joint Audit approach¹⁰.

Of the 233 findings noted, so far 134 had a direct financial impact (57.5%) and 60 a regulatory impact (25.8%).

Accounting and the customs matters are both assessed during the inspections.

3.1. Accounting matters

The management of the A account and the B account¹¹ is inspected in all Member States visited together with the main customs topic. The inspections carried out over the period 2016

¹⁰ Inspections in Denmark and Austria

¹¹ The Member States enter TOR in one of two accounts:

- the **normal account** (A) for amounts recovered or guaranteed (these amounts are paid into the EU budget);
- the **separate account** (B) for amounts which have not been recovered or guaranteed amounts that have been contested. TOR corresponding to **irrecoverable** customs duties are to be withdrawn from the separate account after a defined period of time. Such TOR amounts must simultaneously be made available (paid) to the Commission unless they cannot be recovered for reasons of force majeure, for other reasons which cannot be attributed to the Member State or due to the

- 2018 on this topic confirmed that most errors were one-off and that systematic errors were exceptional. The Member States assumed the financial consequences resulting from the findings noted.

The overall situation improved due to the consideration given by the Commission's inspections to this topic and to the use in most Member States of electronic accounting systems that reduce the risk of errors related to manual intervention. However, Member States must further enhance their effort to ensure the diligent management of the B account and the corrections of the A account and provide all the information required by law to ensure that the statements are clear and transparent.

A series of inspections was also carried out in 5 Member States on the **reliability of the A and the B account and related statements**. The general conclusion was that the procedures in place to establish these statements complied with the EU provisions and ensured the protection of the EU's financial interests. The findings communicated following these inspections concern some inconsistency between the two accounts and late removals from the B account with a limited financial impact.

3.2. Customs matters 2016 - 2018

During this three-year period the inspections focused on:

2016

- the management of tariff suspensions and quotas;
- the management of preferential tariff measures;
- the reliability of A&B accounts;
- the control strategy in the field of customs value (pilot).

2017

- the management of tariff suspension and quotas;
- the external EU transit and the TIR procedures;
- the control strategy of large business units.

2018

- the control strategy in the field of customs value;
- the control strategy for imports of solar panels.

The customs topics with the highest risk for the financial interests of the Union are selected for the inspections.

deferral of the entry in the accounts or the notification of the customs debt in order not to prejudice a criminal investigation affecting the financial interests of the Union.

In this context, the undervaluation of goods has been identified as a significant risk for the finance of the Member States and for the EU budget resulting in significant losses of traditional own resources and VAT that are not collected by Member States, as shown by the TOR inspections and the recent investigations of OLAF¹². In fact, the EU suffered a major case of customs fraud whose consequences were felt all over the EU. International organised criminal groups scouted ports in the EU with the weakest controls in order to get away with declaring falsely low values for textiles and footwear imported from China.

However, while many Member States started to implement targeted measures to reduce this type of fraud, the volume of such trade continued to increase in the UK due to its lack of customs controls. By 2016, the UK accounted for almost 80% of the EU-wide imports of textiles and footwear from China suspected to be fraudulently undervalued. The TOR inspections confirmed that the UK did not implement any effective measures to address this fraud until October 2017 and refused to make available the amounts of TOR lost to the EU budget due to its inaction, estimated at EUR 2.1 billion (net) for 2011-2017. Consequently, the Commission opened infringement proceedings against the UK in March 2018 and submitted its Application to the European Court of Justice in March 2019.

In 2016 and 2017, **the management of tariff suspensions and quotas** was inspected in 11 Member States.

The majority of the Member States were found to be compliant with the EU legislation ensuring an adequate protection of the EU's financial interest. Shortcomings were nevertheless identified concerning the management of tariff quotas, the checks performed and the making available of TOR amounts in case of partial allocation or denial of a quota. The Commission requested the Member States concerned to quickly remedy the situation from a regulatory point of view and to pay the amount of TOR losses due to administrative errors.

In addition, in 2016 **the management of preferential tariff measures** was examined in two Member States, focussing on the procedures and conditions for granting the preferential treatment, the monitoring of incomplete declarations and missing proofs of origin, the checks and the risk analysis and the subsequent requests of verification of origin. Even if an adequate protection of the EU's financial interests is ensured considering the overall situation in Member States, in some cases additional information concerning national measures to be implemented has been requested to ensure that the procedures are correctly applied.

In 2017 **the EU external transit** was examined in 18 Member States to gain assurance that procedures concerning guaranteeing, authorising, and controlling transit movements and following-up any operations not discharged comply with the relevant regulations and that traditional own resources have been properly calculated, established and accounted for. The findings of the inspections were mainly related to regulatory issues for which Member States were requested to take prompt action.

¹² See the OLAF Reports 2017 and 2018.

In 2018, **the control strategy for solar panels** was checked in nine Member States. The general objective of the inspection on the control strategy for solar panels was to evaluate the effectiveness and the efficiency of the systems and procedures in place in the Member States as regards preventing the evasion of ADD and CVD¹³ due for solar panels.

The inspections revealed that several Member States misinterpreted the legal provisions of the ADD and the CVD Regulations of solar panels concerning the term *consigned from* and the elements defining the origin of the goods, thereby artificially limiting the scope of these Regulations which aims to protect the EU industry. This error led to financial consequences for the Member States concerned.

In 2018, the second topic assessed in 13 Member States was **the control strategy in the field of customs value**.

The inspections covered the assessment of the control strategy on customs value in place in the Member States in order to address the risk of import of undervalued goods, especially textile and footwear imported from China, and to ensure that the declared value is the correct one.

The inspections unveiled serious shortcomings in the implementation of proper risk profiles (e.g. based on ratio value/weight covering all traders and risky goods) to efficiently target undervalued imports before the release for free circulation. In fact, although OLAF and the Commission Joint Research Centre (JRC) developed the *Clean Average Prices* (CAP) providing a benchmark to target possible undervalued consignments of textiles and footwear from China¹⁴, several Member States did not use them in practice. The non-homogenous approach in creating risk profiles has prevented Member States from targeting potentially undervalued goods for control and has led to a diversion of import flows towards Member States considered less effective in tackling undervaluation.

The results of the inspections confirmed that a unique ‘customs shield’ is required to pursue and protect the financial interests of the Union. Following the inspections and the findings related to this inspection topic, risk analysis and checks on goods improved in Member States.

One general conclusion drawn by the Commission from its inspections in Member States in recent years is that their control strategies are increasingly shifting from customs controls at the time of release of goods to post-release customs controls. However, the customs controls before or at the time of release of goods remain indispensable for addressing undervaluation and for the detection of new types or patterns of fraud or irregularities.

¹³ ADD (anti-dumping duties), CVD (countervailing duties).

¹⁴ The methodology is supported by the judgement of the ECJ (C-291/15).

4. FOLLOW-UP TO THE COMMISSION INSPECTIONS

4.1. Regulatory aspects

The Member States are requested to take measures whenever flaws or loopholes are detected in national regulations or administrative provisions in the course of the inspections, to bring them into line with EU requirements. These amendments, deemed necessary to harmonise the establishment and the collection of TOR among all 28 Member States, are a great achievement of Commission's inspections. The findings identified are also an essential source of information on the problems encountered by the Member States in applying customs regulations and their impact on TOR.

4.2. Outcome of disputes

The interpretation of legal provisions and the procedures in place in some Member States are not always in line with the requirements of the Commission. Therefore, if an amicable solution cannot be found, the only option is to start an infringement procedure (Article 258 of the Treaty on the Functioning of the European Union).

During the period 2016-2018, eight infringements procedures were either launched or closed (see annex for the details). The most prominent of them is the case opened against the UK in relation to the undervaluation of textile and footwear that resulted in an enormous loss of own resources which the UK refused to make available.

4.3. Financial aspects

For the period 2016 - 2018 additional entitlements totalling more than **EUR 105 million** (+75% compared with the three-year period 2013 - 2015) were paid to the Commission following observations made in the inspection reports, other inspection activities and as a result of the follow-up of Court of Auditors' findings and Court of Justice's decisions on TOR infringement procedures.

The interest for late payment paid by the Member States totalled more than **EUR 110 million**.

5. MEASURES TO IMPROVE THE RECOVERY OF TRADITIONAL OWN RESOURCES

Apart from its on-the-spot inspections in the Member States, the Commission has several other means of monitoring the recovery of TOR.

5.1. Examination of irrecoverable entitlements that have been written off

Member States must take all the requisite measures to make TOR available, except where recovery proves impossible pursuant to Article 13(2) of Regulation No 609/2014:

- for reasons of *force majeure*;

- for other reasons which cannot be attributed to them; or
- due to the deferral of the entry in the accounts or the notification of the customs debt in order not to prejudice a criminal investigation affecting the financial interests of the Union.

In accordance with EU legislative provisions, Member States must report to the Commission irrecoverable amounts of TOR exceeding EUR 100,000 (write-off reports¹⁵) for which they consider themselves not to be responsible. Subsequently, the Commission provides its comments on each report. For amounts below the above threshold, the Commission routinely assesses samples of cases during the on-the-spot inspections since there is no separate reporting requirement.

In order to support the Member States in evaluating their potential financial responsibility for irrecoverable TOR amounts, the Commission issued a working document – the *Compendium* – with the criteria that have been used to assess write-off reports. The working document was communicated to all Member States for the first time in the framework of the Advisory Committee meeting on Own Resources (ACOR) of 6 December 2012. Its latest revised version of 8 March 2018 taking into account changes in the EU legislation and the relevant case law on traditional own resources was communicated to all Member States in their respective official language on 1 June 2018.

Member States must draft for each relevant case a structured report and forward it to the Commission using a multilingual database called WOMIS (Write-Off Management and Information System). WOMIS, regularly updated, allows for an efficient and secure management of the Member States' reports.

The competent Commission services assess the report and provide comments to the Member State within a legal deadline of six months. These comments concern the justification the Member State can invoke for not making the TOR corresponding to the irrecoverable customs duties available to the Commission.

Over the period 2016-2018, 214 write-off reports were communicated to the Commission, involving a total amount of EUR 124,633,046.19. In the same period¹⁶, the Commission considered for 91 reports involving EUR 30,435,940.72 that the loss of traditional own resources could not be attributed to the Member States. In 159 cases - involving **EUR 77,289,805.76** - the Commission was of the opinion that amounts proved irrecoverable

¹⁵ **Write-off report:** Procedure under article 13 of Regulation No 609/2014 for monitoring Member States' potential financial responsibility for irrecoverable amounts of TOR over EUR 100,000. Under the procedure, the Commission issues its opinion on whether the TOR became irrecoverable for reasons not attributable to the Member States. The purpose of the Commission's examination of the write-off reports is to assess the degree of diligence shown by the Member States in carrying out their efforts to establish and recover from the economic operators the customs duties representing TOR. The threshold for reporting irrecoverable amounts has been raised from EUR 50,000 to EUR 100,000 by Council Regulation No 609/2014 as of 1 October 2016.

¹⁶ The following figures also include reports finally assessed that were initially communicated prior to 2016.

for reasons at least partially attributable to the Member State concerned. In 5 cases, reporting to the Commission was considered incorrect or premature (EUR 3,253,457.74).

In order to assess whether the loss of TOR can be attributed to the Member State, a thorough analysis of the elements of the report is needed. Due to this sometimes lengthy process, at the time of drafting the report up to 330 write-off reports (EUR 167,590,097.16) relating to the years 2009 to 2019 were still under examination.

5.2. Treatment of errors of establishment leading to a loss of traditional own resources

The Commission followed up the administrative errors committed by the Member States to the detriment of the EU's financial interests during the period 2016-2018 (cases found during on-the-spot inspections, national repayment or remission decisions due to administrative errors, voluntary making available of payments by Member States due to administrative errors for which they assume the financial responsibility for the TOR losses, rejected written-off irrecoverable amounts below EUR 100,000 etc.). As a result, the Member States made available **EUR 52.9 million** over the period 2016-2018. In addition, **EUR 43.2 million** were paid as interest for late payment.

5.3. OWNRES database

Pursuant to Article 5(1) of Regulation No 608/2014, Member States must send the Commission information on cases of fraud and irregularities involving entitlements of more than EUR 10,000. This information is reported via the OWNRES database, which is managed and maintained by the Commission.

OWNRES provides the Commission with information necessary to monitor recovery and prepare its on-the-spot inspections. It is also used by the Anti-Fraud Office (OLAF) for various analyses and the data reported is assessed in detail in the annual report from the Commission to the European Parliament and the Council on the protection of the European Union's financial interests — Fight against fraud.

At the beginning of 2019, the OWNRES database contained **106,361** cases of fraud or irregularity (either 'open' or 'closed') compared to **90,204** cases at the beginning of 2016. This is an increase of around **17.91%** or **16,157** new cases reported in the three-year period 2016 – 2018.

During the ACOR meeting held in Brussels on 6 July 2017, the Commission services presented the upgrade of the OWNRES application and the working document on how to report in this database the results of financial recovery actions for OLAF investigations.

5.4. Monitoring measures for the acceding countries

The Commission provides technical assistance to the candidate countries so that they develop the administrative capacity and put in place the systems necessary to implement the *acquis* with respect to TOR upon accession. It also assesses the preparedness of the candidate countries to that effect.

In this domain, the Commission conducted a monitoring mission in 2016 in the framework of the accession negotiations concerning Montenegro. This fact-finding mission showed that Montenegro clearly needs more time to adapt its administrative procedures and to mobilise the various actors involved in the Own Resources system.

Further to the Accession Conference with Serbia on 25 June 2018, *acquis* chapter 33 (Financial and Budgetary Provisions) was formally opened for accession negotiations. As a first step the Serbian authorities were requested to complete a comprehensive questionnaire on the own resources system to identify and plan future measures of information and technical assistance in this area.

6. CONCLUSION

The results recorded from 2016 to 2018 show that the Commission's inspections of TOR and the systematic follow-up of the shortcomings observed continue to be indispensable and efficient means to improve recovery of TOR and provide reassurance that the financial interests of the EU are properly protected.

The inspections continue to be a key tool to harmonise and enhance compliance with the EU rules. Their financial impact is significant, as illustrated by the additional net amount made available to the EU budget of **around EUR 388 million during 2016-2018**. This results in significant incentives for Member States for timely and complete making available of TOR to the EU budget. On top of this, the inspections contribute to ensure the correct application of the customs and accounting rules and thus protecting of the EU's financial interests by providing a powerful mechanism to fight and prevent damaging distortions of competition.

The Commission has to face a number of challenges in the field of TOR. Brexit in particular represents a major issue for the Customs Union and already required the Commission and Member States to dedicate a significant amount of resources to prepare for the various potential scenarios and take all measures to protect the Union's financial interests as regards revenues to the EU budget.

The evolution of international trade and trends like e-commerce also represent threats and opportunities, calling for new tools and continued close collaboration between the Commission and Member States to enhance risk-based customs controls and ensure effective customs duties collection.

In that context, the Commission services in charge of TOR have strengthened their cooperation in recent years to address more effectively the challenges looming ahead. They will continue taking initiatives to improve the functioning of the Customs Union.