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REPORT FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT AND THE COUNCIL

32nd Annual Report on the protection of the European Union's financial interests - Fight against fraud - 2020

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REPORT FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT AND THE COUNCIL

32nd Annual Report on the protection of the European Union's financial interests - Fight against fraud - 2020

TABLE OF CONTENTS

LIST OF ABBREVIATIONS	2
EXECUTIVE SUMMARY	3
1. INTRODUCTION.....	4
2. THE EU'S FINANCIAL INTERESTS IN 2020	4
3. THE PLAYERS PROTECTING THE EU'S FINANCIAL INTERESTS AND MAIN DEVELOPMENTS IN 2020.....	7
3.1. The EU legislative framework.....	7
3.2. The control framework for the EU's financial interests.....	10
3.2.1. The EU level.....	10
3.2.2. Member States' level.....	14
4. COOPERATION TO FIGHT FRAUD	18
4.1. Inter-institutional cooperation at EU level	18
4.1.1. Cooperation between the Commission (OLAF), the European Parliament and the Council	18
4.1.2. Cooperation between OLAF and the European Court of Auditors	18
4.1.3. Working arrangements between OLAF and EPPO	18
4.1.4. Cooperation between OLAF and Europol	19
4.2. Cooperation between EU and Member States authorities.....	19
4.2.1. Activities of the Advisory Committee for fraud prevention (COCOLAF).....	19
4.2.2. Customs cooperation	19
4.2.3. Joint customs operations.....	20
4.3. Cooperation between EU Member States.....	21
4.4. Cooperation with non-EU countries.....	21
5. FOCUS ON INITIATIVES ADOPTED, IMPLEMENTED OR ONGOING IN 2020.....	22
5.1. The Commission Anti-Fraud Strategy.....	22

5.2.	Hercule programme: support to EU Member States' anti-fraud activities.....	22
5.3.	Revenue: EU level	23
5.3.1.	The VAT e-commerce package	23
5.3.2.	Fight against fraud in customs duties	24
5.3.3.	Fight against illicit trade in tobacco products.....	24
5.4.	Revenue: EU Member State level	25
5.5.	Expenditure: EU level	25
5.5.1.	Rule of Law - conditionality.....	25
5.5.2.	The 2021-2027 EU budget	26
5.5.3.	The Recovery and Resilience Facility	26
5.5.4.	Technical support through the Structural Reform Support programme.....	27
5.6.	Expenditure: EU Member State level.....	28
6.	IRREGULARITIES, FRAUD AND RISKS	29
6.1.	From detection to risk.....	29
6.1.1.	VAT fraud – “Study and Reports on the VAT Gap in the EU-28 Member States” (published in 2020).....	31
6.1.2.	Irregularities and fraud in revenue.....	31
6.1.3.	Irregularities and fraud in expenditure	32
6.2.	Additional risks of irregularities and fraud for 2021 and beyond	36
6.2.1.	COVID-19 risks in revenue	36
6.2.2.	COVID-related risks in expenditure.....	37
6.2.3.	Risks related to the Recovery and Resilience Facility	38
7.	TOOLS TO STRENGTHEN THE FIGHT AGAINST FRAUD	40
7.1.	ARACHNE.....	40
7.2.	The Early Detection and Exclusion System (EDES)	40
7.3.	GetI project	41
7.4.	National IT tools to protect the EU's financial interests	42
8.	CONCLUSIONS AND RECOMMENDATIONS	42

LIST OF ABBREVIATIONS

AFCOS	Anti-Fraud Coordination Service
CAFS	Commission Anti-Fraud Strategy
EAFRD	European Agricultural Fund for Rural Development
ECA	European Court of Auditors
EDES	Early Detection and Exclusion System
EPPO	European Public Prosecutor's Office
ERDF	European Regional Development Fund
ESF	European Social Fund
ESIF	European Structural and Investment Funds
EU	European Union
IMS	Irregularity Management System
MFF	Multiannual Financial Framework
NGEU	Next Generation EU
OLAF	European Anti-Fraud Office
PIF	Protection of financial interests
RRF	Recovery and Resilience Facility
TFEU	Treaty on the Functioning of the European Union
TOR	Traditional Own Resources
VAT	Value Added Tax

EXECUTIVE SUMMARY

The responsibility of protecting the EU's financial interests is shared between the EU and its Member States. To exit the crisis caused by the COVID-19 pandemic and support the transition towards a more modern and sustainable Europe, EU Member States have approved a financial package consisting of the 2021-2027 multiannual financial framework ('EU budget') of EUR 1.074 trillion, and of a temporary recovery instrument, the Next Generation EU of EUR 750 billion, which will be invested in a green, digital and resilient Europe with new sources of EU revenue. In total, this package amounts to more than EUR 1.8 trillion.

A revamped EU anti-fraud architecture has been set up over the last years to protect EU taxpayers' money, relying on: a reformed European Anti-Fraud Office (OLAF), the investigative and prosecutorial powers of the European Public Prosecutor's Office (EPPO), the coordinating role of Eurojust, the analytical capacity of Europol, and close cooperation with and between national authorities.

Throughout 2020, this cooperation has been further developed by establishing working arrangements, setting up joint initiatives and operations, and exchanging good practice and training.

In 2020 and in the first half of 2021, several key events and measures have further equipped the EU and national authorities to better protect the EU's financial interests. Among these are:

- The EPPO started its operations;
- A revised regulation made OLAF ready to cooperate with the EPPO and strengthened its investigative powers;
- A general regime of 'conditionality' to protect the EU budget was introduced against breaches of the principles of the rule of law that affect the protection of the EU's financial interests;
- Good progress on implementing the Commission's Anti-Fraud Strategy was achieved with two thirds of the planned actions implemented and the remaining third ongoing.

The number of fraud and irregularities reported by the competent EU and national authorities dropped in 2020 compared with previous years. While certain cyclical effects explain the drop in fraudulent irregularities, the drop in the detection and reporting rate of non-fraudulent irregularities in certain areas of spending cannot easily be explained and are therefore of concern. In addition to known risks, new challenges are emerging. They are linked to new ways of managing and spending EU funds, linked to performance and achieving specific targets, areas of reinforced spending, linked for example to the green and digital transition and to the health sector.

Coping effectively with these risks will require new approaches and tools, a renewed and joint European vision for fighting fraud, corruption and other illegal activities affecting the EU's financial interests. This vision will build on the achievements of recent years, and include a more efficient collection and use of data, improved transparency, better coordinated, coherent anti-fraud efforts by Member States through national anti-fraud strategies, reinforced cooperation within national authorities, between EU Member States and with the EU.

1. INTRODUCTION

The EU and its Member States share responsibility for protecting the EU's financial interests and fighting fraud. EU Member State authorities manage the largest share of EU expenditure and collect traditional own resources (TOR). The Commission oversees both these areas, sets standards and checks compliance. In line with Article 325(5) of the Treaty on the Functioning of the European Union (TFEU), the Commission, in cooperation with EU Member States, submits an annual report to the European Parliament and the Council on measures taken to counter fraud and other illegal activities affecting the EU's financial interests (the 'PIF report'). For 2020, this report and its accompanying documents¹ meet this obligation.

The year 2020 was marked by the COVID-19 pandemic and its impact. The EU institutions have reacted with unprecedented financial and economic policy decisions. They have finalised the negotiations and approved the EU budget for 2021 to 2027 as well as those for Next Generation EU (NGEU) and its flagship programme, the Recovery and Resilience Facility (RRF). The EUR 1.8 trillion budget will help rebuild Europe to make it greener, more digital, more resilient and better fit for the current and future challenges. Protecting the EU's financial interests will be key in achieving the ambitious objectives of this historic budget agreement.

The 2020 PIF report presents:

- i) an overview of the EU's financial interests, following the strategic decisions taken in 2020;
- ii) the main players, at EU and national level;
- iii) the cooperation among these players;
- iv) the most significant initiatives taken;
- v) the risks to which the EU's financial interests are and will be exposed, based on the irregularities and fraud detected by EU bodies and national authorities;
- vi) the tools developed to fight fraud.

2. THE EU'S FINANCIAL INTERESTS IN 2020

The EU's financial interests include revenues, expenditures and assets covered by the EU budget and those covered by the budgets of the EU institutions, bodies, offices and agencies and the budgets managed and monitored by them.

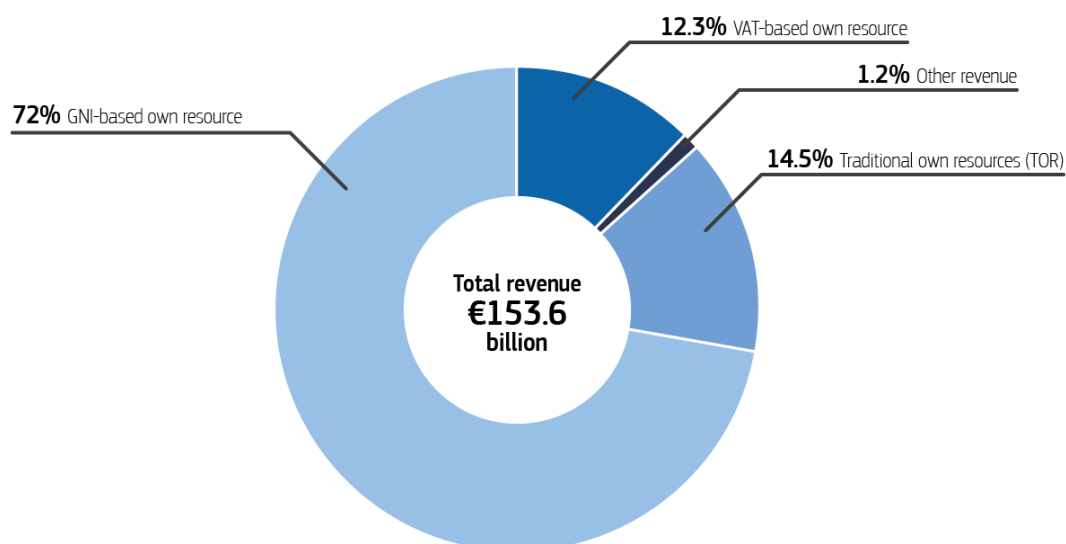
¹ Also known as the PIF report, from the French acronym for *Protection des Intérêts Financiers*, this report is accompanied by six Commission Staff Working Documents concerning:

- a) Statistical evaluation of irregularities reported for own resources, natural resources, cohesion policy and pre-accession assistance and direct expenditure in 2020;
- b) Measures adopted by Member States to protect the EU's financial interests in 2020;
- c) Follow-up on recommendations to the Commission report on the protection of the EU's financial interests – fight against fraud 2019;
- d) HERCULE III –2020 implementation;
- e) Early Detection and Exclusion System (EDES) — Panel referred to in Article 143 of the Financial Regulation;
- f) Commission Anti-Fraud Strategy (CAFS) implementation in 2020.

The revenue side of the budget is made up of customs duties, Value Added Tax and a share of the gross national income of EU Member States.

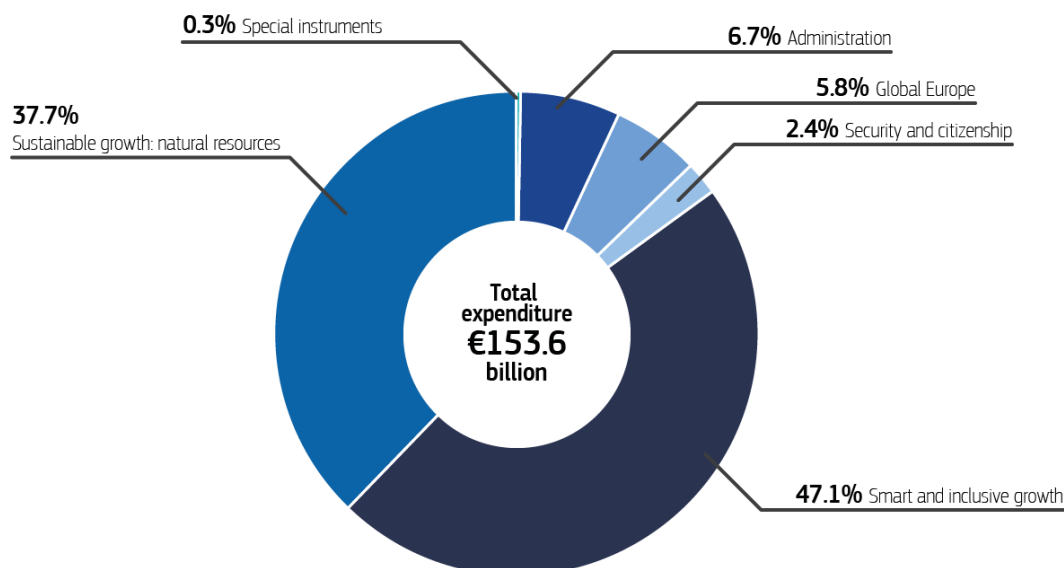
Figure 1 shows the resources available to the EU in 2020.

Figure 1 - EU revenue in 2020²



The EU finances its policies through these resources (see **Figure 2**).

Figure 2 - EU expenditure in 2020³



² Source: OJ L57, 27.2.2020, p14.

³ Source: OJ L57, 27.2.2020, p13.

Although the budget follows a yearly implementation⁴, it is part of the Union's long-term budget, the Multiannual Financial Framework (MFF), which provides the limits for spending for seven years. While 2020 was the last year of the 2014-2020 MFF⁵, it was also the year in which the legal framework for the next long-term budget was defined.

The EU budget is spent through three different management modes (see **Figure 3**).

Figure 3 – EU budget management modes

EU Budget		
Direct management: by the European Commission	Indirect management: by other bodies inside or outside the EU such as third countries and international organisations	Shared Management: jointly by the European Commission and national authorities

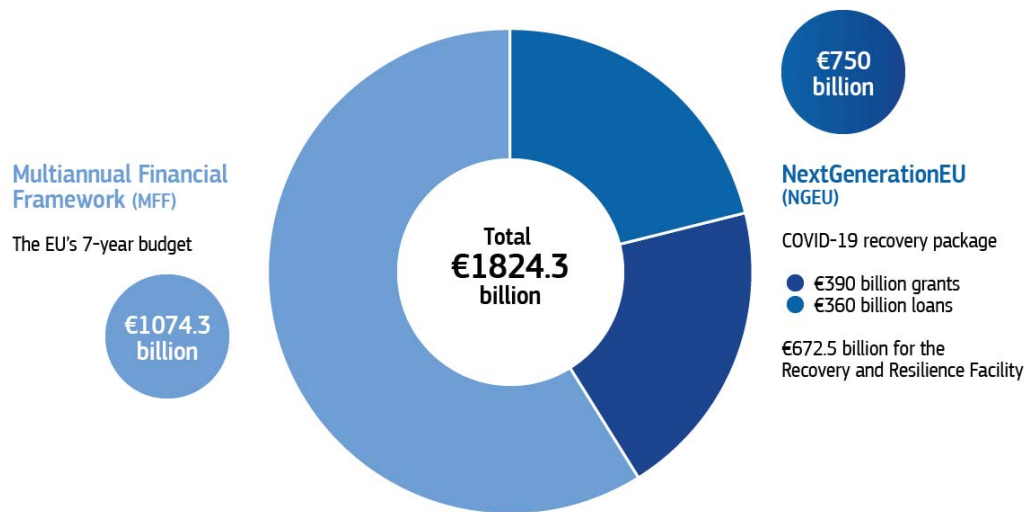
To exit the crisis caused by the COVID-19 pandemic and support the transition towards a more modern and sustainable Europe, EU Member States have approved the long-term 2021-2027 EU budget⁶, of EUR 1.074 trillion, and a temporary recovery instrument, the Next Generation EU of EUR 750 billion. In total, this package amounts to more than EUR 1.8 trillion (see **Figure 4**).

⁴ For the yearly adoption procedure, please consult https://ec.europa.eu/info/sites/default/files/about_the_european_commission/eu_budget/budgetary-procedure.pdf

⁵ [Council Regulation \(EU, Euratom\) No 1311/2013](#) of 2 December 2013 laying down the multiannual financial framework for the years 2014-2020.

⁶ [Council Regulation \(EU, Euratom\) 2020/2093](#) of 17 December 2020 laying down the multiannual financial framework for the years 2021 to 2027.

Figure 4 – EU expenditure 2021-2027



The Recovery and Resilience Facility (RRF)⁷ is at the heart of NGEU with EUR 672.5 billion in loans and non-repayable financial support available between 2021 and 2026⁸.

3. THE PLAYERS PROTECTING THE EU'S FINANCIAL INTERESTS AND MAIN DEVELOPMENTS IN 2020

Many players look after the EU's financial interests and work continuously to improve its protection; both by shaping the required legislative framework and by implementing the underlying policies.

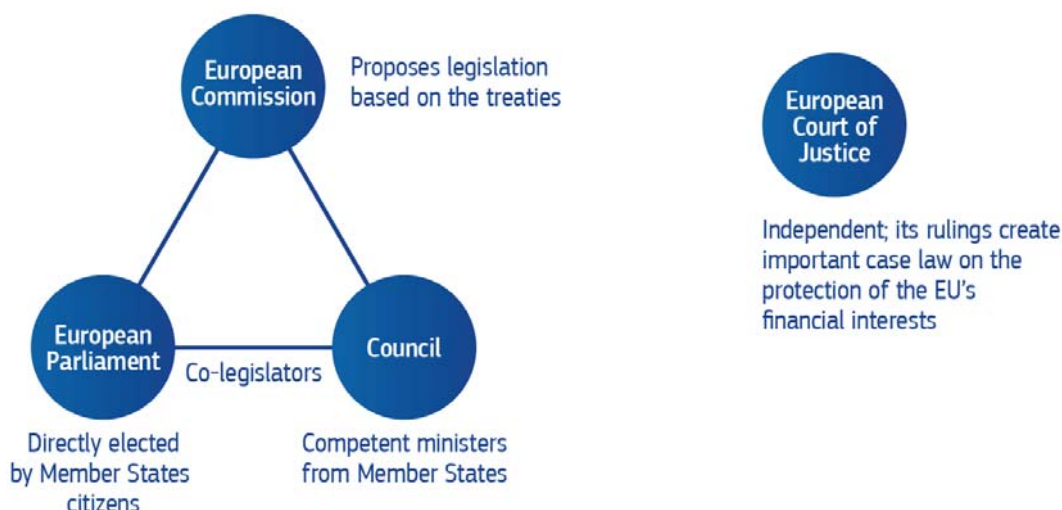
3.1. The EU legislative framework

The **Commission** proposes anti-fraud legislation, which is then decided on by the **European Parliament** and the **Council** (the 'co-legislators').

⁷ [Regulation \(EU\) 2021/241](#) of the European Parliament and of the Council of 12 February 2021 establishing the Recovery and Resilience Facility.

⁸ The funds also cover measures started from 1 February 2020.

Figure 5 – The EU institutions’ roles in the legislative process



Error! Reference source not found. shows the key legislative acts adopted in 2020 and early 2021.

Table 1 - Key acts adopted

Title	Description of the protection of the EU's financial interests mechanism
Council Regulation (EU, Euratom) 2020/2093 of 17 December 2020 laying down the multiannual financial framework for the years 2021 to 2027⁹.	The 'MFF Regulation.' Harmonised anti-fraud provisions have been agreed for all MFF sectoral acts ¹⁰ .
Regulation (EU, Euratom) 2020/2092 of the European Parliament and of the Council of 16 December 2020 on a general regime of conditionality for the protection of the Union budget¹¹.	The 'Conditionality Regulation.' The objective of the conditionality mechanism is to protect the EU's budget against breaches of the principles of the rule of law by EU Member States that affect or seriously risk affecting the sound financial management of the budget or the EU's financial interests in a sufficiently direct way ¹² .
Regulation (EU, Euratom) 2020/2223 of the European Parliament and of the Council of 23 December 2020 amending Regulation (EU, Euratom) No 883/2013, as regards cooperation with the European Public Prosecutor's Office and the effectiveness of the European Anti-Fraud Office investigations¹³.	The 'OLAF Regulation.' The amended Regulation defines OLAF's relations with the European Public Prosecutor's Office (EPPO) to ensure full complementarity between the two bodies, and reinforces OLAF's investigative capacity ¹⁴ .

⁹ OJ L 433I, 22.12.2020, p. 11.

¹⁰ See Section 5.5.2.

¹¹ OJ L 433I, 22.12.2020, p. 1.

¹² See Section 5.5.1.

¹³ OJ L 437, 28.12.2020, p. 49.

Regulation (EU) 2021/241 of the European Parliament and of the Council of 12 February 2021 establishing the Recovery and Resilience Facility¹⁵	The ‘RRF Regulation.’ Article 22 of that Regulation contains provisions on the protection of the EU’s financial interests ¹⁶ .
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The **Court of Justice of the European Union** (‘the Court’) ensures the uniform application and interpretation of EU law. In 2020, the Court delivered three decisions in the field of protecting the EU’s financial interests.

Case number and description
<p>C-603/19¹⁷, Úrad špeciálnej prokuratúry.</p> <p>In this case, the Court confirmed that Article 325 TFEU does not preclude national law preventing the state from claiming compensation in criminal proceedings for damage caused to it by fraudulent conduct on the part of the accused person resulting in the misappropriation of funds from the EU budget, and under which the state does not have, in those proceedings, any other type of action available to it by which it may assert its right as against the accused. The Court clarified that although Article 325 TFEU obliges EU Member States to take effective measures to recover sums wrongly paid to the beneficiary of an EU subsidy, it does not impose any constraint as regards the recovery procedure. The national court only has to take account of whether an effective legal remedy for acts affecting EU’s financial interests exists in administrative, civil or criminal law.</p>
<p>C-743/18¹⁸, Elme Messer Metalurgs.</p> <p>In this case, the Court had the opportunity to interpret Article 2(7) of Regulation (EC) No 1083/2006, laying down general provisions on the European Regional Development Fund, the European Social Fund and the Cohesion Fund, which defines the concept of ‘irregularity’. The Court interpreted the provision to include within this concept the situation in which the beneficiary of European Regional Development Fund funding fails to achieve, during the relevant period, the level of turnover expected as part of the project eligible for financing because the activities of its sole business partner have been suspended or because that partner has become insolvent. In its judgment, the Court underlined that a demonstration of the existence of a specific financial impact on the EU budget is not required and that it is sufficient that the possibility of such an impact is not excluded.</p>
<p>C-496/18 and C-497/18¹⁹, HUNGEOD and others.</p> <p>The EU public procurement directives authorise EU Member States to adopt national legislation that allows a monitoring authority to initiate of its own motion, on grounds of protection of EU financial interests, a review procedure in order to monitor infringements of public procurement rules. In that regard, the Court stated that, where provision is made for such a procedure, it comes within the scope of EU law since the public contracts, which are the subject of such a procedure come within the material scope of the public procurement directives. Accordingly, the Court held that those review procedures must comply with the general principles of EU law and, in particular, the general principle of legal certainty.</p>

¹⁴ See **Snapshot 4**.

¹⁵ OJ L 57, 18.2.2021, p. 17. Even if adopted in the beginning of 2021, this act is the result of intense negotiations conducted in 2020, following the agreement in the European Council of July, on the new MFF and NGEU.

¹⁶ See Section 5.5.3.

¹⁷ Judgment of 1 October 2020, EU:C:2020:774.

¹⁸ Judgment of 1 October 2020, EU:C:2020:767.

¹⁹ Judgment of 26 March 2020, EU:C:2020:240.

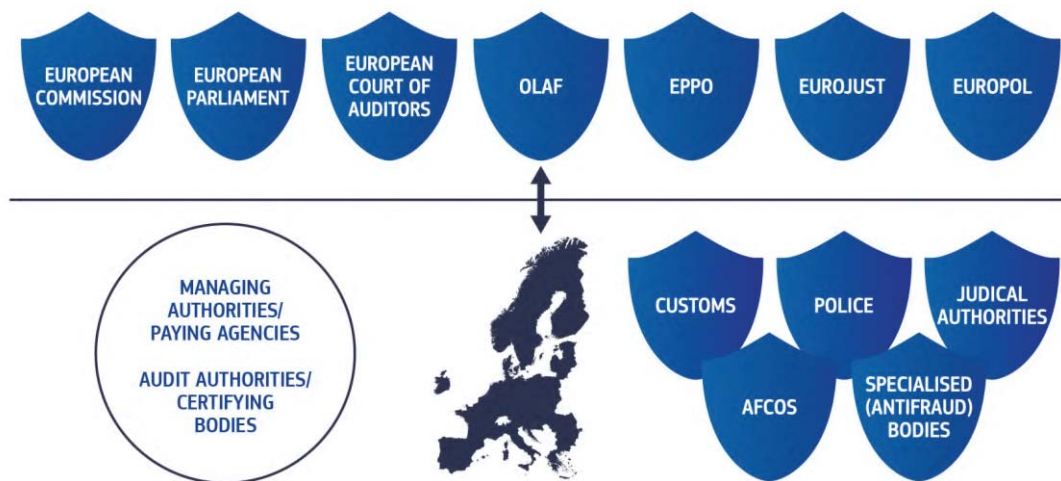
Snapshot 1: Update on the undervaluation case

The 2019 PIF report²⁰ referred to the Court's ongoing proceedings against the United Kingdom²¹ for alleged undervaluation fraud concerning textile and shoes imported from China via the UK, based on the investigations carried out by OLAF as well as by the Commission's own resources management. On 8 December 2020, the oral hearing was held in Luxembourg, the opinion of the Advocate General is scheduled for 9 September 2021 and the Court's ruling in early 2022.

3.2. The control framework for the EU's financial interests

Figure 6 shows the complexity of the EU control framework with a multitude of players at European and national level.

Figure 6 – The control framework: an overview



3.2.1. The EU level

EU institutions and bodies handle both EU revenue and expenditure.

The **Commission** defines the strategies and translates into policies and initiatives the overall political goals developed collectively by the EU institutions. The Commission's departments manage specific policies and the related spending programmes which support them. The management of financial resources can follow any of the modes shown in **Figure 3**. The Commission is responsible for implementing the EU budget.

The **European Parliament** exercises democratic oversight to ensure that the Commission and the other institutions deal properly with EU funds. The European Parliament, acting on a recommendation from the Council, decides whether to grant the discharge, *i.e.* the final approval on the budget for a specific year. The European Parliament decides after careful examination by its **Committee on Budgetary Control (CONT)** of the Commission's financial accounts.

²⁰ http://ec.europa.eu/anti-fraud/sites/default/files/pif_report_2019_en.pdf, Section 3.3.1.

²¹ C-213/19.

Snapshot 2 – The European Parliament’s resolution on the protection of the EU’s financial interests

The European Parliament’s resolution on the 2018 PIF report was adopted in the plenary session of 10 July 2020, after having received a favourable vote by CONT on 7 May 2020²².

The European Parliament’s resolution is a key political document addressing several issues linked to protecting the EU’s financial interests and highlighting areas for improvements²³. The European Parliament, for instance, encouraged the Commission and the EU Member States to enhance the use of new technologies in managing the funds, strengthen their analytical capacity to improve fraud risk assessment and management, improve the reporting of comparable data and the use of analytical IT tools, and present a legislative proposal for mutual administrative assistance in EU expenditure.

The **European Court of Auditors** assesses the economy, effectiveness, efficiency, legality and regularity of EU action to improve accountability, transparency and financial management.

Snapshot 3 – The European Court of Auditors’ annual report

Every year the European Court of Auditors audits the revenue and expenditure of the EU budget and provides its opinion on the extent to which the annual accounts are reliable, and income and spending comply with the applicable rules and regulations. The annual report for the financial year 2019 was published on 10 November 2020²⁴.

The European Court of Auditors concluded that the accounts were not affected by material misstatements. As for the regularity of transactions, it concluded that revenue was free from material error. On expenditure, the audit results showed an increased estimated level of error compared to 2018. High-risk (mainly reimbursement-based) expenditure, which is often subject to complex rules, was affected by a material level of error.

The **European Anti-Fraud Office** (OLAF) carries out independent investigations into fraud and corruption involving EU funds and develops EU anti-fraud policy to fight fraud, corruption and any other illegal activity affecting the EU’s financial interests.

Snapshot 4: What’s new in 2020 for OLAF?

Both OLAF and the European Public Prosecutor’s Office (EPPO) protect the EU budget. While they do so within their respective mandates, the OLAF and EPPO regulations ensure close cooperation between both bodies. This cooperation rests on three strands:

i) the EPPO can rely on OLAF’s support and expertise; ii) OLAF can launch investigations that are complementary to EPPO’s, on the request of or in agreement with the latter, to facilitate recovery or adopt administrative precautionary measures; iii) the

²² Procedure file [2019/2128\(INI\)](#), Protection of the European Union's financial interests - combating fraud – 2018 annual report.

²³ The Commission commented in detail on the resolution in its formal reply.

²⁴ <https://www.eca.europa.eu/en/Pages/DocItem.aspx?did=53898>

offices will exchange information before and during investigations, through mutual reporting mechanisms²⁵.

The revised OLAF regulation also equips OLAF with sharper tools to investigate fraud against the EU budget. For instance, the conduct of on-the-spot checks by OLAF is subject to clearer rules and it benefits from enhanced two-way cooperation with national authorities. OLAF will also be able to access bank account information under the same conditions as those for national competent authorities. These tools now coexist with stronger procedural guarantees for persons concerned by OLAF investigations, and with control mechanisms for their enforcement, such as the Controller of Procedural Guarantees.

OLAF's 2020 operational results are described in its annual report²⁶.

OLAF underwent a **reorganisation** in June 2020 to strengthen its investigative capacity, internal controls and financial management, and maximise the potential of the broad range of skills and experience of its staff.

The **European Public Prosecutor's Office** (EPPO) has powers to investigate and prosecute crimes affecting the EU's financial interests in the 22 participating EU Member States²⁷. It started its operations on 1 June 2021.

Snapshot 5: What's new for the EPPO in 2020?

The EPPO was established by Council Regulation (EU) 2017/1939²⁸, which entered into force on 20 November 2017. Following the appointment of the European Chief Prosecutor, Ms Laura Codruța Kövesi in 2019, the College of European Prosecutors was constituted in September 2020. It adopted a set of internal rules needed for it to function effectively, including: the internal rules of procedure, the conditions of employment of the European Delegated Prosecutors, and the rules on data protection and Permanent Chambers.

On the decentralised level, which consists of the European Delegated Prosecutors located in the EU Member States that participate in the EPPO, nominations by the Member States have been advancing and the formal appointments by the College are ongoing.

EPPO's Central Office moved into its premises in Luxembourg at the beginning of 2021. The Case Management System, a key tool for EPPO's operations, has been rolled out.

During the set up process, the participating EU Member States were consulted on crucial issues, such as the changes needed to integrate the EPPO into the national systems.

Croatia, Czechia and France indicated the adoption in 2020 of organisational measures and legislative amendments to complete national preparations so that EPPO's operations can begin. Sweden appointed a Commission of Inquiry to analyse and propose necessary

²⁵ In 2020, OLAF and the EPPO started negotiations on their working arrangements. See Section 4.1.3.

²⁶ http://ec.europa.eu/anti-fraud/sites/default/files/olaf_report_2020_en.pdf

²⁷ Denmark, Ireland, Hungary, Poland and Sweden do not participate in the EPPO.

²⁸ OJ L 283, 31.10.2017, p. 1.

legislative amendments and other measures needed for Sweden to participate in the EPPO²⁹.

Eurojust, the European Union Agency for Criminal Justice Cooperation, coordinates the work of national authorities – from the EU Member States as well as non-EU countries – in investigating and prosecuting cross-border crime.

Snapshot 6 –Eurojust’s highlights in 2020

In 2020, Eurojust continued its operational work on fighting fraud against the EU budget and other PIF crimes, in close cooperation with OLAF. Eurojust and OLAF were involved in a number of joint investigation teams and OLAF participated in coordination meetings organised by Eurojust. A training course was also organised by Eurojust to showcase the added-value it can bring to OLAF’s administrative investigations. Eurojust published a “*Note to introduce to practitioners the new Regulation on the Mutual Recognition of Freezing and Confiscation Orders*”³⁰, which has considerably strengthened the EU legal framework in asset recovery. Eurojust also prepared the ground for the entry into operations of the EPPO by negotiating a working arrangement establishing the practical details of their cooperation with it.

Europol, the European Union Agency for Law Enforcement Cooperation serves as a support centre for law enforcement operations, hub for information on criminal activities, and centre for law enforcement expertise.

Snapshot 7 – What’s new for Europol in 2020?

In June 2020 Europol launched the European Financial and Economic Crime Centre (EFECC) to improve the operational support provided to EU Member States and EU bodies in financial and economic crime, including those covered by Directive (EU) 2017/1371³¹ (‘PIF Directive’).

The EFECC also promotes the systematic use of financial investigations and the development of alliances with public and private entities to trace, seize and confiscate criminal assets in the EU and beyond.

In 2020 the Commission also presented a legislative proposal on strengthening Europol’s mandate. On the protection of EU financial interests, the proposal aims at strengthening Europol’s cooperation and exchange of information with the EPPO and OLAF. Europol has negotiated a working arrangement with the EPPO to define their future cooperation.

²⁹ See Sections 5 and 6 of ‘Measures adopted by the Member States to protect the EU’s financial interests in 2020’, accompanying this report.

³⁰ [Note on Regulation \(EU\) 2018/1805 on the mutual recognition of freezing orders and confiscation orders | Eurojust | European Union Agency for Criminal Justice Cooperation \(europa.eu\)](#)

³¹ Directive (EU) 2017/1371 of the European Parliament and of the Council of 5 July 2017 on the fight against fraud to the Union’s financial interests by means of criminal law, OJ L 198, 28.7.2017, p. 29.

3.2.2. Member States' level

On **revenue**, EU Member States are responsible for implementing customs legislation, for carrying out customs controls and for collecting customs duties, excise duties and VAT due at import.

Member States' customs authorities pursue several other objectives such as the application of non-fiscal measures aimed at improving internal EU security, protecting the EU from unfair and illegal trade and the environment.

Member States' customs authorities play a key role in balancing the need to facilitate trade, with faster and seamless import procedures, and the need to apply customs controls, with the support of the EU.

Snapshot 8 – Commission's and EU Member States' response to the COVID-19 crisis

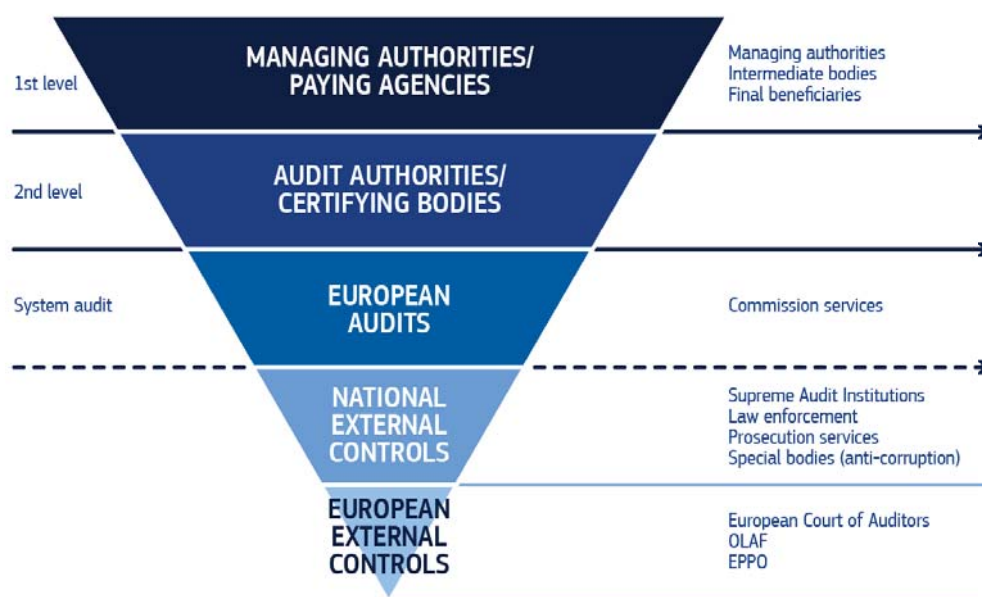
The Commission reacted swiftly to the COVID-19 crisis by adopting legislation, issuing guidelines and actively supporting EU Member States and businesses to ensure flexibility for customs debt obligations, to facilitate fast and swift clearance of medical/protective equipment and to prevent counterfeit or unsafe equipment from entering the EU. Member States also made a significant contribution to the EU's pandemic response in 2020: customs authorities adjusted their customs controls strategies; anti-fraud services in several EU Member States effectively countered fraud in the context of the COVID-19 crisis. This allowed the overall protection of the EU financial interests in 2020 to be maintained at a similar level as in previous years, while ensuring smooth and frictionless trade flows for the EU citizens and businesses.

EU Member States also manage about three quarters of the EU budget **expenditure**, through a number of bodies (managing authorities, paying agencies, audit authorities, certifying bodies), whose number may vary depending on the size of the country, the amount of EU funds to be managed and their degree of decentralisation. *Supreme audit institutions* play a significant role in supervising the legality and regularity of the activities of national public bodies. As fraud and corruption are criminal acts, *national law enforcement, prosecution and judicial services* play a fundamental role in the protection of the EU's financial interests, alongside *specialised bodies*, such as anti-fraud or anti-corruption offices.

This complex system³² provides for several layers of control (see **Figure 7**).

³² The number of bodies and authorities involved in the management of EU funds is due to increase with the implementation of the RRF as of 2021.

Figure 7 – Framework to protect EU funds spent under shared management



Anti-Fraud Coordination Services (AFCOS): set up based on Regulation (EU, EURATOM) No 883/2013 ('OLAF Regulation'), AFCOS facilitate effective cooperation and exchange of information, including information of an operational nature, with OLAF. In several EU Member States they effectively play a coordinating and steering role in relation to the fight against fraud affecting the EU's financial interests.

Snapshot 9 – What's new in the EU Member States in 2020?

France and Greece reorganised their AFCOS³³.

Given the complexity of the national framework protecting the EU's financial interests, the Commission has promoted over the past years the voluntary adoption by the Member States of **national anti-fraud strategies**.

By the end of 2020, 14 Member States³⁴ reported having adopted such strategies. These strategies, however, can vary in scope and depth and some need to be updated. Among those EU Member States which replied as not having a national anti-fraud strategies in place³⁵, five³⁶ indicated that they have launched a procedure to adopt one (see **Figure 8**).

³³ See Footnote 29.

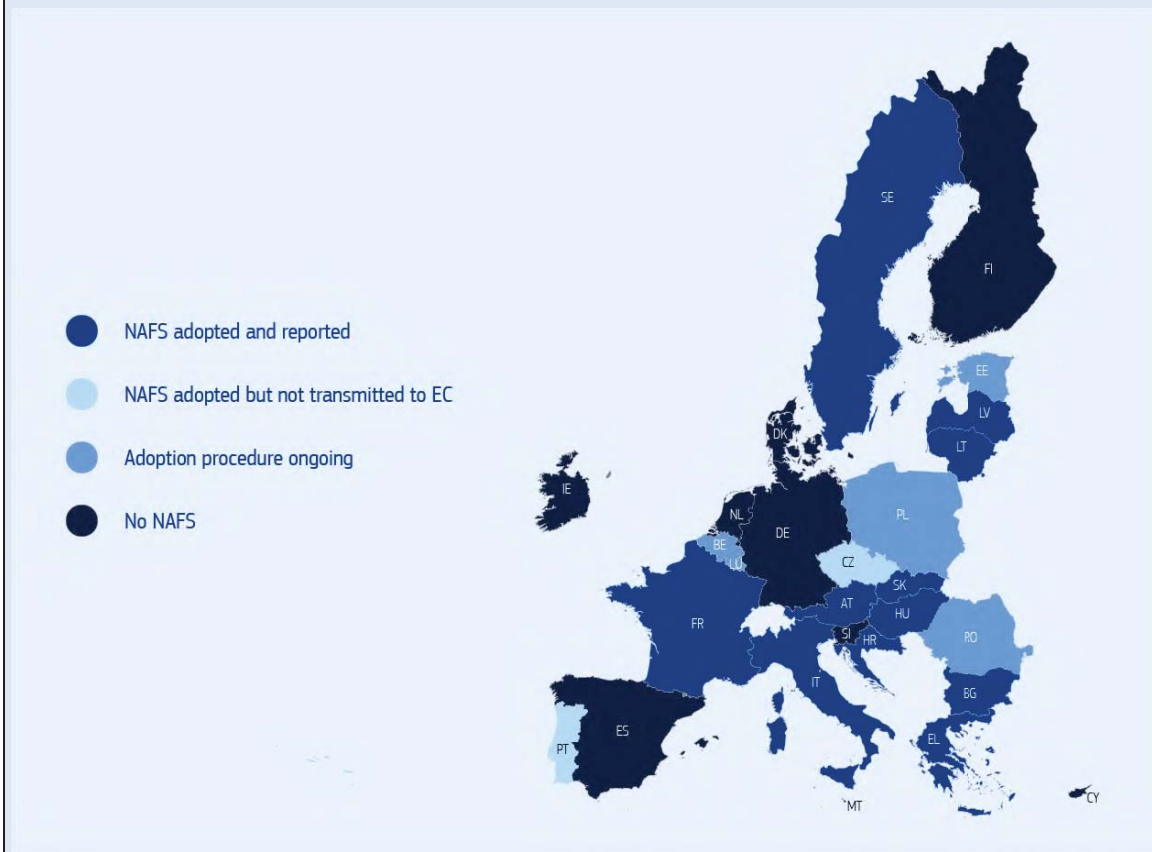
³⁴ Austria, Bulgaria, Croatia, Czechia, France, Greece, Hungary, Italy, Latvia, Lithuania, Malta, Portugal, Slovakia, Sweden. Out of these, Czechia informed the Commission of having updated its strategy, but has not yet transmitted the new document; Portugal has indicated having adopted a strategy, but has never formally transmitted it to the Commission.

³⁵ Belgium, Cyprus, Denmark, Estonia, Finland, Germany, Ireland, Luxembourg, Netherlands, Poland, Romania, Slovenia, Spain.

³⁶ Belgium, Estonia, Luxembourg, Poland, Romania.

The situation has improved compared with 2019, when 10 EU Member States indicated having adopted a strategy³⁷. The implementation of the national Recovery and Resilience plans would represent the opportunity for all other EU Member States to follow and establish anti-fraud strategies based on the Commission's guidelines prepared in collaboration with EU Member States experts. For EU Member States that have such a strategy already in place, a step forward would be to do an update, taking into account the risks linked to the implementation of the RRF and the COVID-19 crisis³⁸.

Figure 8 – National anti-fraud strategies: state of play



Among the measures adopted in 2020 to protect the EU's financial interests, Greece, Italy and Romania named the national legislative acts that turned the PIF Directive into national law. Ireland did so in 2021. Romania stated that several other EU directives had also been turned into national law³⁹.

³⁷ For more information about some of the strategies adopted or updated, see the document accompanying this report 'Measures adopted by the Member States to protect the EU's financial interests in 2020', the information provided by Bulgaria, Malta and Sweden.

³⁸ See Sections 6.2 and 6.3.

³⁹ See Section 5 of 'Measures adopted by the Member States to protect the EU's financial interests in 2020', accompanying this report.

Snapshot 10 – What’s the EU Member States’ follow-up to the 2019 PIF report recommendations?

In the 2019 PIF report on the protection of the European Union's financial interests, the Commission made a set of recommendations to EU Member States on emergency spending and reporting of irregularities⁴⁰. On emergency spending, it recommended:

- Keeping checks and monitoring measures to a high level: 22 Member States⁴¹ replied that they had fully implemented this point. Malta and Slovakia reported partial implementation, while Austria and Denmark considered their systems already aligned.
- Carefully assessing the use of emergency procurement: 23 Member States⁴² reported full implementation. Slovakia reported partial implementation, and Austria and Denmark considered their systems already aligned.
- Completing the transition to e-procurement processes: 18 Member States⁴³ reported full implementation of the transition to e-procurement processes. Six⁴⁴ reported partial implementation. Austria has not implemented it, while Ireland did not reply to this question.
- Considering the possibility of further strengthening transparency in the use of EU funds, particularly for emergency procurement, 17 Member States⁴⁵ replied that they had done so and 8⁴⁶ reported that they had not. Denmark stated that the question was not relevant to them.

On the recommendation to report irregularities and to carefully monitor them, 22 Member States⁴⁷ reported full implementation and 4⁴⁸ reported partial implementation.

⁴⁰ For a complete analysis of the replies provided by the Member States see ‘Follow-up on recommendations to the Commission report on the protection of the EU’s financial interests – fight against fraud 2019’ accompanying this report.’

⁴¹ Belgium, Bulgaria, Czech Republic, Germany, Estonia, Ireland, Greece, Spain, France, Croatia, Italy, Latvia, Lithuania, Luxembourg, Hungary, the Netherlands, Poland, Portugal, Romania, Slovenia, Finland and Sweden.

⁴² Belgium, Bulgaria Czech Republic, Germany, Estonia, Ireland, Greece, Spain, France, Croatia, Italy, Latvia, Lithuania, Luxembourg, Hungary, Malta, the Netherlands, Poland Portugal, Romania, Slovenia, Finland and Sweden.

⁴³ Belgium, Bulgaria, Czech Republic, Denmark, Germany, Estonia, Greece, Croatia, Italy, Latvia, Luxembourg, Hungary, Malta, Portugal, Romania, Slovenia, Finland and Sweden.

⁴⁴ Spain, France, Lithuania, the Netherlands, Poland and Slovakia.

⁴⁵ Bulgaria, Germany, Estonia, Ireland, Greece, Spain, Croatia, Italy, Latvia, Lithuania, Luxembourg, Hungary, Poland, Portugal, Romania, Slovenia and Sweden.

⁴⁶ Belgium, Czech Republic, France, Malta, the Netherlands, Austria, Slovakia and Finland.

⁴⁷ Belgium, Bulgaria, Czech Republic, Denmark, Germany, Estonia, Spain, France, Croatia, Italy, Latvia, Lithuania, Luxembourg, Hungary, Malta, Austria, Poland, Portugal, Romania, Slovakia, Sweden and Finland.

⁴⁸ Ireland, Greece, the Netherlands and Slovenia.

4. COOPERATION TO FIGHT FRAUD

The complex anti-fraud architecture in place requires close cooperation between the various players.

4.1. Inter-institutional cooperation at EU level

4.1.1. *Cooperation between the Commission (OLAF), the European Parliament and the Council*

In 2020, several meetings of the Committee on Budgetary Control of the European Parliament focused on OLAF's activities and the Office could present its results. OLAF represented the Commission in several Council working groups and notably in the Working Party on Combating Fraud.

On 1 December 2020, OLAF participated with the Commission, the European Parliament, the Council, the European Chief Prosecutor and the OLAF Supervisory Committee in the inter-institutional exchange of views on OLAF, and discussed the new EU anti-fraud architecture, including OLAF's reorganisation and the cooperation with EPPO. This was a high-level event characterised by focused and positive discussions which paved the way for improved cooperation between OLAF, EPPO, Eurojust and Europol.

4.1.2. *Cooperation between OLAF and the European Court of Auditors*

While the European Court of Auditors (ECA) and OLAF have different mandates, they have a shared mission to protect the EU's financial interests and ensure sound financial management of the EU budget. The ECA informs OLAF of any suspicion of fraud or other illegal activity that it detects in its audit work or that is reported to it. In 2020 OLAF received six such notifications from ECA, which all led to the opening of investigations.

Following the Administrative Arrangement concluded in May 2019, OLAF and the ECA have improved their cooperation by organising a joint annual workshop, sharing their training programmes, know-how and risk analysis. The 2020 annual workshop had to be postponed to 2021 due to the COVID-19 pandemic.

4.1.3. *Working arrangements between OLAF and EPPO*

The legal framework governing EPPO and OLAF provides for working arrangements between the two bodies to lay down the practical aspects of their relationship. The working arrangements were agreed in November 2020 and signed on 5 July 2021.

Overall, the arrangements set out the necessary mechanisms to ensure efficient reporting, non-duplication and complementarity of the investigative activities of the two offices. They provide for close cooperation by establishing practical ways to exchange information and the technical aspects for mutual indirect access to their case management systems.

4.1.4. Cooperation between OLAF and Europol

In autumn 2020 OLAF and Europol signed working arrangements, which resulted in the establishment of a secured channel of communication (SIENA) and in the appointment of an OLAF Liaison Officer at Europol.

4.2. Cooperation between EU and Member States authorities

4.2.1. Activities of the Advisory Committee for fraud prevention (COCOLAF)

The Advisory Committee for Coordination of Fraud Prevention ('COCOLAF') brings together the Commission (represented by OLAF) and Member State experts. It provides a forum for discussing the main developments in the fight against fraud and the preparation of this report. Its work is structured around four working groups and a plenary session. In 2020, meetings were held virtually on the following topics:

- OLAF investigations in the EU Member States;
- fraud risks and mitigating measures in the context of the COVID-19 crisis;
- possible uses of the Early Detection and Exclusion System (EDES) to protect the EU's financial interests in shared management;
- capacity-building actions to identify and prevent fraud and corruption in the European Structural and Investment Funds;
- main fraud and irregularity trends and patterns;
- the new anti-fraud triangle: AFCOS, OLAF and EPPO.

4.2.2. Customs cooperation

Given the cross-border nature of customs fraud, it is essential that EU Member States' customs authorities cooperate to prevent, investigate and prosecute breaches of customs and agricultural legislation. Exchanges of information can take place at EU level between EU Member States or among them and the Commission, or at international level with non-EU countries. Exchanges of information at EU level are made under either the Mutual Assistance Regulation⁴⁹ or the customs risk management system for risk-related information⁵⁰, while those with non-EU countries are based on specific agreements (see Section 4.4).

⁴⁹ Council Regulation (EC) No 515/97 of 13 March 1997 on 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, OJ L 82, 22.3.1997, p. 1.

⁵⁰ Article 46(3) of Regulation (EU) 952/2013 of the European Parliament and of the Council of 9 October 2013 laying down the Customs Code, OJ L 269, 10.10.2013, p. 1.

Snapshot 11 – Evaluation of Regulation 515/97

An evaluation of Regulation 515/97 started in 2019 and is now nearly finalised. Relevant stakeholders in EU Member States, Commission departments and agencies and other organisations gave their views on the implementation of the Regulation and its relevance in combating customs and agricultural fraud. Stakeholders, in particular EU Member States, are generally satisfied with the Regulation as it currently stands, and consider that it meets its objectives and remains a good instrument to tackle the new challenges arising in the fight against fraud.

Customs authorities can also cooperate with each other and exchange information and best practice through joint actions, seminars, training courses, project groups, working visits, and cross-border operations financed by the EU action programmes: Customs 2020 and Hercule III⁵¹.

4.2.3. Joint customs operations

Joint customs operations ('JCOs') are targeted actions limited in time that aim to combat fraud and the smuggling of sensitive goods in specific areas at risk and/or on identified trade routes.

In addition to its investigations on cases of revenue fraud and counterfeiting, OLAF coordinates large-scale JCOs involving EU and international operational partners. OLAF's support is tailored to each JCO and may include the use of permanent technical infrastructure, IT and communications tools, in particular the Virtual Operations Coordination Unit (VOCU) for the secure exchange of information, as well as dedicated strategic analysis, administrative and financial support. **Table 2** shows JCOs in which OLAF was involved in 2020.

Table 2 - Joint customs operations in 2020

Operation	Description
SILVER AXE V	Coordinated by Europol and targeting illicit imports of prohibited pesticides, one of the most profitable businesses for international fraudsters (estimated to represent up to 13.8% of all pesticides sold in the EU). Operation Silver Axe is now in its fifth year, and has so far led to seizures of 2 568 tonnes of illegal pesticides.
OPSON IX	Worldwide operation led by Europol and Interpol targeting counterfeit/substandard food and beverages, food frauds and economically motivated adulteration. OLAF led an action specifically targeting trafficking in counterfeit wine and alcoholic beverages. 1 158 199 litres of wine seized, mostly champagne and 109 267 litres of various alcoholic beverages, that infringe intellectual property rights.
SHIELD	Organised by Europol and focused on counterfeit and substandard oncological medicines and hormonal substances, including a targeted action on counterfeit/illegal/misused medicines, doping substances, food supplements and all medical supplies used in the fight against COVID-19. Coordinated by OLAF with the participation of 13 EU Member States. Detection of 58 cases of various irregularities with illicit and substandard oncological medicines, hormonal substances and food supplements.
DEMETER VI	Global operation (73 participating countries) to monitor and control illicit cross-border movements of waste and illegal trade in ozone depleting substances (ODS) and refrigerant gases (HFCs); coordinated by the World Customs Organization (WCO). OLAF contributed with risk-based information and intelligence to the identification

⁵¹ See Section 6.1.

	and monitoring of suspicious shipments destined to the EU. 98 682.95 tonnes of ODS and 41.97 tonnes of HFCs were detected and intercepted.
STOP	Coordinated by the WCO, it mobilised 99 customs administrations all over the world with OLAF's support. It targeted the traffic of illicit products related to the COVID-19 pandemic. 307 215 524 units of illicit medicine and 47 891 628 units of medical supplies (masks, gloves, test kits, thermometers) as well as 2 762 386 litres of sanitiser gel were seized.
ARKTOS	Coordinated by FRONTEX together with the Finnish and Latvian national Authorities, targeting excise fraud, particularly tobacco smuggling, document fraud and illegal immigration at selected border crossing points on the EU eastern land borders. OLAF, Interpol, Eurojust, Europol, Poland, Estonia, Lithuania and Slovakia participated. 37 million illegal cigarettes and over 1.8 tonnes of tobacco were seized.
LUDUS	Coordinated by OLAF under the Joint Customs Police Operation led by Europol and the Spanish Guardia Civil, National Police and Customs. The action targeted counterfeit and hazardous toys for the European market. The evaluation of the results is ongoing.

4.3. Cooperation between EU Member States

Member States cooperate in the fight against fraud, sometimes financed by the Hercule programme (see Section 5.2). Some of these projects are briefly described in **Table 3**.

Table 3 – Cooperation projects financed by the Hercule programme finalised in 2020

Organising country	Project name	Other participating countries	reference ⁵²
Bulgaria	Enhancing the cooperation and the control models in preventing fraud, linked to customs regimes 4200 and 4000, affecting the EU system of own resources.	Romania, Greece, Turkey	p. 14
Slovakia	Training for customs officers on X-ray scanner image interpretation and customs control process.	Bulgaria, Croatia, Estonia, Finland, Greece, Hungary, Latvia, Lithuania, Poland, Romania	p. 15
Latvia	Advanced X-ray image interpretation training.	Estonia, Lithuania	p. 23

4.4. Cooperation with non-EU countries

Cooperation with non-EU countries to prevent, detect and combat breaches of customs legislation is based on agreements on mutual administrative assistance (MAA). Currently, there are agreements in force with more than 80 countries, including major EU trade partners, such as the United States, China and Japan. In 2020, negotiations with the United Kingdom and Uzbekistan were finalised, and were ongoing with Australia, Indonesia and eastern and southern Africa (ESA5).

Free-trade agreements usually contain an anti-fraud clause, which allows for a temporary withdrawal of tariff preference for a product in cases of serious customs fraud and persistent lack of sufficient cooperation to combat it. In 2020, negotiations were concluded with the United Kingdom; and were ongoing with Australia, Chile, New Zealand and Indonesia.

⁵² It refers to the page number in the document 'HERCULE III – 2020 implementation' accompanying this report.

5. FOCUS ON INITIATIVES ADOPTED, IMPLEMENTED OR ONGOING IN 2020

5.1. The Commission Anti-Fraud Strategy

The Commission's Anti-Fraud Strategy ('CAFS'), adopted in April 2019, and its action plan including 63 actions, play a significant role in preventing the possible misuse of EU money. Good progress in implementing the actions was achieved in 2020. By June 2021, two thirds of the actions had been implemented, while for the remaining third implementation was ongoing⁵³.

The strategy has two priority objectives: (i) to improve data collection and analysis and (ii) to improve coordination, cooperation and processes.

In line with the first objective, OLAF intensified its analytical work, for example, on a COVID-19 related fraud risk assessment (see Section 6.2.2), shared with Commission departments, and on irregularities and fraud in the EU funding of health infrastructure (see *Snapshot 18*).

In line with the second objective of the CAFS, good progress was made on a number of actions aimed to increase coordination and cooperation between Commission departments and to equip the Commission with a more effective system of anti-fraud oversight. Most notably, contacts and cooperation between Commission departments have been intensified, in particular through the setting up of groups composed of Commission representatives within the Fraud Prevention and Detection network (FPDNet) led by OLAF. These groups are set up by management mode or by theme, such as the group on internal cases and on fraud risk management, both launched in spring 2021.

In the CAFS, the Commission has also committed to improve monitoring of the follow-up given to OLAF recommendations, which are essential for bringing the money back to the EU budget and fraudsters to justice. Therefore, in 2020, the Commission and OLAF dedicated considerable efforts to make such monitoring as efficient as possible, taking stock of about 1 400 financial recommendations issued between January 2012 and June 2019. In total, the sum of recommended amounts for recoveries for 2012-2020 is equivalent to more than EUR 6 billion with more than a half linked to customs cases.

5.2. Hercule programme: support to EU Member States' anti-fraud activities

The 2014-2020 Hercule III programme⁵⁴ promoted actions to counter fraud, corruption and any other illegal activities affecting the EU's financial interests. In 2020⁵⁵, the last year of its implementation, a budget of EUR 16.44 million was made available for:

⁵³ A stocktaking exercise was finalised in June 2021. See 'Commission Anti-Fraud Strategy (CAFS) Action Plan State-of-Play June 2021' accompanying this report.

⁵⁴ Regulation (EU) No 250/2014 of the European Parliament and of the Council of 26 February 2014 establishing a programme to promote activities in the field of the protection of the financial interests of the European Union (Hercule III programme) and repealing Decision No 804/2004/EC (OJ L 84, 20.3.2014, p. 6).

⁵⁵ Commission Decision C(2020) 28 final of 16 January 2020.

- Actions to strengthen the operational and technical capacity of national and regional authorities in the Member States, and IT support (74% of the programme's budget);
- Training activities, conferences, seminars and staff exchanges mainly addressed to staff employed by law enforcement agencies in the EU Member States and partner countries, as well as comparative research studies and scientific publication activities (26% of the budget).

The COVID-19 pandemic had a major impact on the general implementation of the programme. Most of the training activities planned for 2020 were either postponed to 2021 or delivered virtually where possible. Most grant contracts were extended in duration, allowing the beneficiaries to continue implementing their projects.

Beneficiaries of Hercule III grants awarded in 2017-2019 reported substantial successes achieved with the help of equipment and training funded under the programme⁵⁶.

5.3. Revenue: EU level

5.3.1. The VAT e-commerce package

Due to the COVID-19 crisis, Member States and businesses were facing difficulties in progressing with the IT developments needed to implement the VAT e-commerce rules by 1 January 2021. Therefore, the entry into force of the VAT e-commerce package was postponed by six months. The customs rules applicable to e-commerce were also adapted to enable the smooth implementation of the VAT e-commerce rules.

The Commission also adopted in September 2020 the Customs action plan⁵⁷, proposing actions to tackle the challenges of e-commerce and step up the fight against VAT and customs fraud, such as undervaluation, mis-description of goods and false declarations of origin.

On 18 February 2020, the Council adopted a legislative package⁵⁸ to request payment service providers to send information on cross-border payments originating from EU Member States and on the beneficiary ('the payee') of these cross-border payments. Under this package, payment service providers offering payment services in the EU will have to monitor the payees of cross-border payments and send information on those who receive more than 25 cross-border payments per quarter to EU Member States' authorities.

This information will then be centralised in a European database, the Central Electronic System of Payment Information (CESOP) and will then be made available to anti-fraud experts in EU Member States via the Eurofisc network. The objective of this new measure is to give EU Member States tax authorities the right instruments to detect

⁵⁶ See 'HERCULE III – 2020 implementation', accompanying this report.

⁵⁷ COM(2020) 581 final.

⁵⁸ Council Directive (EU) 2020/284 of 18 February 2020 amending Directive 2006/112/EC as regards introducing certain requirements for payment service providers (OJ L 62, 2.3.2020, p. 7) and Council Regulation (EU) 2020/283 of 18 February 2020 amending Regulation (EU) No 904/2010 as regards measures to strengthen administrative cooperation in order to combat VAT fraud (OJ L 62, 2.3.2020, p. 1–6).

possible e-commerce VAT fraud carried out by sellers established in another Member State or in a non-EU country.

The sending of data must start on 1 January 2024.

5.3.2. Fight against fraud in customs duties

The COVID-19 pandemic has strongly impacted customs, which had to fulfil its core tasks despite the difficult situation. At the start of February 2020, the Commission opened a crisis alert in the customs risk management system, to streamline and centralise the exchange of risk-related information linked to COVID-19. EU Member States have been very responsive and information sharing has reached exceptional levels.

In May 2020, the Commission adopted the guidelines on prioritising risks for customs controls, which provide for temporary measures to support EU Member States. They describe the main risks that have to be addressed as a priority, depending on the impact of the crisis on those countries.

The Commission carries out, on-the-spot or remotely, monitoring and control visits to ensure the correct application of the customs and TOR legislation. Where cooperation and progress made in tackling outstanding issues are considered insufficient, corrective measures are applied.

As stated in the 2019 PIF report, such corrective measures have already been applied by the Commission against the United Kingdom in relation to undervalued textiles and footwear from China (see **Snapshot 1**). The Commission took further steps in 2020 to quantify similar TOR losses occurred in all EU Member States and sent them preliminary calculations of potential TOR losses related to imports of possibly undervalued textiles and footwear from China that took place on their territory. In addition, the Commission quantified potential TOR losses with regard to the evasion of anti-dumping duties for solar panels and informed the EU Member States concerned.

5.3.3. Fight against illicit trade in tobacco products

The fight against the illicit tobacco trade is an important component of the EU policy for protecting the EU's financial interests. Throughout 2020, the Commission continued implementing the second action plan to combat illegal tobacco trade. Most key actions were either underway or completed by the end of the year. Within the EU, the Commission assisted EU Member States in rolling out the new tobacco traceability system launched in 2019. Considerable progress has been made in analysis and intelligence. For instance, the independent tobacco laboratory handled more than 150 requests in 2020. A study to identify a methodology to measure the illicit tobacco market was completed in 2020 and published in early 2021.

Since the entry into force of the FCTC Protocol to Eliminate Illicit Trade in Tobacco Products (FCTC Protocol) in 2018, OLAF, in close cooperation with Commission departments and EU Member States, is an active player on the multilateral stage. International cooperation focused on securing the supply chain of tobacco products. OLAF, in view of the second meeting of the parties scheduled for November 2021, is acting as a 'Key Facilitator' for the working group on tracking and tracing. OLAF also provides its expertise as an active member of the working group on assistance and cooperation.

5.4. Revenue: EU Member State level

To better protect EU revenue, some EU Member States adopted specific measures⁵⁹, as shown in **Table 4**.

Table 4 - Measures adopted by EU Member States in relation to revenue in 2020

Member State	Description	Revenue area
Belgium	National Operational plan 2020	Customs and tax fraud
Croatia	Enhanced controls in the port of Rijeka	Customs
	Implementation of the General Audit Support (GAS) System at the Croatian Tax Administration	Tax fraud
Czechia	Accelerating the process of establishing a customs debt	Customs
Estonia	Fight against fuel fraud	Customs
Greece	Measures that aim at reducing smuggling	Customs and tax fraud
Hungary	2021 plan for post-release checks	Customs and tax fraud
Italy	Implementation of control arrangements in application of Decision 491/2020	Customs
Latvia	Registration of websites or mobile applications in commercial passenger transport	Tax fraud
	Check lottery	Tax fraud
	Segmentation of taxpayers	Customs and tax fraud
Lithuania	Joint Operation JAD HANSA	Customs and tax fraud
The Netherlands	Prevention by customs of fraud relating to COVID-19	Customs
Portugal	Implementation of common financial risk criteria and standards (FRC)	Customs
	Interconnection between the Automatic Selection System and the Low Value Merchandise Import System (e-commerce)	Customs
Slovenia	Update of the Slovenian risk analysis	Customs and tax fraud

5.5. Expenditure: EU level

The adoption of the spending package for the 2021-2027 EU budget and NGEU is accompanied by the necessary provisions to ensure that the EU's financial interests are sufficiently protected.

5.5.1. Rule of Law - conditionality

Regulation (EU, Euratom) 2020/2092 of the European Parliament and of the Council introduces a general regime of conditionality to protect the EU budget.

It aims at protecting the EU budget against breaches of the principles of the rule of law that affect (or seriously risk affecting) its sound financial management or the EU's financial interests in a sufficiently direct way. It is therefore linked to the EU budget. Based on this regulation, the Commission may propose to the Council appropriate measures to protect the EU budget or the EU's financial interests, such as suspension and termination of payments, as well as prohibition of new legal commitments and financial corrections. The regulation complements other procedures established by EU legislation

⁵⁹ See Sections 5 and 6 of 'Implementation of Article 325 TFEU by the Member States', accompanying this report.

to protect the EU budget, including OLAF and EPPO's investigations. The Commission will continue using all the instruments available to effectively protect the EU budget, including e.g. the Early Detection and Exclusion System, checks and audits or financial corrections. The Commission will apply the conditionality mechanism from 2021 onwards, when it considers that other instruments are not more effective to protect the EU budget.

In July 2021 the Commission published the second annual Rule of Law report⁶⁰, which presents a synthesis of both the rule of law situation in the EU and an assessment of the situation in each EU Member State. The Rule of Law report monitors significant developments, both positive and negative, relating to the rule of law in EU Member States. The report covers four pillars: (i) the justice system, (ii) the anti-corruption framework, (iii) media pluralism and (iv) freedom, and other institutional issues related to checks and balances. It is a separate instrument from the Regulation on a general regime of conditionality for the protection of the Union budget and represents an important source of information for the Commission.

5.5.2. *The 2021-2027 EU budget*

The legislative framework which is being developed in relation to the 2021-2027 EU budget will bring some significant changes and simplification in the management of EU funds, in particular in ESI Funds observing an increased:

- share of payments based on performance rather than costs;
- use of simplified cost options and lump sums.

The approval of the 2021-2027 EU budget also requires the definition of the specific regulations for each spending programme. Dedicated anti-fraud provisions have been agreed to ensure that the necessary rights and access required are granted for the authorising officer responsible, OLAF and the Court of Auditors to comprehensively exercise their respective competences and ensure that any third parties involved in the implementation of EU funds grant equivalent rights. In the case of OLAF, such rights must include the right to carry out investigations, including on-the-spot checks and inspections, as provided for in Regulation (EU, Euratom) No 883/2013.

These provisions would also apply to non-EU countries participating in EU programmes.

5.5.3. *The Recovery and Resilience Facility*

Following the Commission's proposal for a Regulation establishing the RRF of May 2020, the Commission published in September 2020 guidance to EU Member States for preparing the national recovery and resilience plans, which was updated following the political agreement between the Parliament and the Council in December 2020⁶¹.

⁶⁰ COM(2021) 700 final. https://ec.europa.eu/info/policies/justice-and-fundamental-rights/upholding-rule-law/rule-law/rule-law-mechanism/2021-rule-law-report/2021-rule-law-report-communication-and-country-chapters_en

⁶¹ SWD(2020)205 published on 17.9.2020 and updated following the agreement between Council and Parliament on the RRF Regulation by SWD(2021)12 final of 22.1.2021. These and other relevant information and documents are available at https://ec.europa.eu/info/business-economy-euro/recovery-coronavirus/recovery-and-resilience-facility_en

The European Council in July⁶² and December 2020 underlined the importance of sound financial management and the protection of the EU's financial interests for this new instrument.

In line with the RRF Regulation, in the assessment of the national recovery and resilience plans, the Commission is checking that EU Member States put in place internal control systems to manage the facility ensuring that the funding received is used in compliance with EU and national law, and allow, in particular, to prevent, detect and correct conflict of interest, fraud, corruption and double-funding.

During the implementation of the RRF, EU Member States must ensure sound financial management of these funds and recover amounts unduly spent. In particular, EU Member States must collect standardised categories of data in respect of final recipients of funds, contractors, sub-contractors and beneficial owners for audit and control and ensure access to these data for the Commission, OLAF, ECA and EPPO (where applicable).

The Commission will make available to the EU Member States an information and monitoring system including a single data mining and risk-scoring tool to access and analyse the relevant data.

With the requests for payment under RRF, EU Member States must include a management declaration, a summary of audits carried out, including weaknesses identified and any corrective actions taken.

Following payment, the Commission will carry out risk-based controls.

All in all, a comprehensive set of measures has been included to strengthen the protection of the EU's financial interests and in the first months of 2021 EU Member States have been working closely together with the Commission to reflect this in their recovery and resilience plans, submitted in the second quarter of 2021. The Commission will closely monitor the implementation of these plans.

5.5.4. Technical support through the Structural Reform Support programme

In 2020 technical support was provided through the Structural Reform Support programme for a number of actions in the fight against corruption and fraud. Projects have been started with authorities from a number of EU Member States to:

- raise awareness and standards in fighting bribery in international business transactions;
- develop risk assessment and behavioural insights framework for better managing corruption risks;
- strengthen coordination on corruption prevention and detection;
- improve fraud risk detection related to grants; and
- increase the effectiveness of implementing and monitoring anti-corruption actions.

⁶² Council of 17-21 July 2020 concl.22-24.

5.6. Expenditure: EU Member State level

In 2020, several EU Member States adopted measures to better protect the resources coming from the EU budget and spent under shared management. These cover a wide range of initiatives, such as sectoral strategies, reinforcing the cooperation among the bodies concerned, strengthening the fight against corruption or preventing conflict of interest⁶³. A selection of these initiatives are shown in **Table 5**, while further measures on anti-fraud IT tools are described in Section 6.5.

Table 5 – Measures adopted by EU Member States in relation to expenditure in 2020

Member State	Measure	Budgetary sector
Austria	Audit strategy	Agriculture, Fisheries, Cohesion policy and Fund for the most deprived
	Preventing irregularities through a high density of checks	Cohesion policy
Belgium	Measures to reinforce checks	Cohesion policy
	Measures to reinforce integrity and counter conflicts of interest	Agriculture, Fisheries and Cohesion policy
Bulgaria	Ordinance for defining irregularities, which justify the imposing of financial corrections and the corresponding percentage of corrections pursuant to the Management of the resources from the ESIF Act	All expenditure areas
Croatia	Implementation of anti-fraud policy for operational programmes	Cohesion policy
Czechia	Update of procedures for checking ownership structures and conflicts of interest	Cohesion policy
Denmark	Action plan on the common agricultural policy (CAP)	Agriculture
	Anti-fraud strategy of the Danish Fisheries Agency	Fisheries
Finland	Anti-fraud cooperation between national authorities under the ESIF	All expenditure areas
Germany	Anti-fraud measures (North Rhine-Westphalia ERDF programme)	Cohesion policy
Hungary	Anti-corruption package	All expenditure
Luxembourg	Administrative measure to fight against fraud	Cohesion policy
Poland	Strengthening control mechanisms and means of monitoring public contracts financed by EU funds by amending the rules governing public procurement control	All expenditure areas
	Anti-corruption policy at the Agency for Restructuring and Modernisation of Agriculture	Agriculture
Portugal	Audit of anti-fraud measures adopted by operational programmes for the programming period 2014-2020	Cohesion policy
Slovakia	Establishment of an anti-corruption department at the level of the Ministry of Agriculture and Rural Development	Agriculture
	ISO 37001 Certificate - Anti-Corruption Management System and Code of Conduct	Cohesion policy
Slovenia	Cooperation in proceedings before national courts	Cohesion policy
	Measures taken by the Agency for Agricultural Markets and Rural Development	Agriculture
Spain	Cooperation Agreement between the Spanish AFCOS and Guardia Civil	All expenditure areas
	Consolidation of the cooperation among the national, regional and local anti-fraud authorities	All expenditure areas

⁶³ See Sections 5 and 6 of 'Measures adopted by the Member States to protect the EU's financial interests in 2020', accompanying this report.

6. IRREGULARITIES, FRAUD AND RISKS

6.1. From detection to risk

The EU's financial interests can be adversely impacted by:

- A **diminution of the resources** of the EU budget, adversely affecting the possibility to finance its policies;
- An **increase in the costs** associated to an item of expenditure;
- A **waste of the resources** financing projects of low quality or not delivering the expected results;
- A **misapplication of such funds** for purposes other than those for which they were originally intended (beneficiary or project not entitled to the financial support).

When the adverse impact on the EU budget is the result of a breach of rules, it is defined as '**irregularity**'⁶⁴. In case of intentional behaviour, such as any act or omission relating to the use or presentation of false, incorrect or incomplete statements or documents or to non-disclosure of information in violation of a specific obligation, such behaviour amounts to '**fraud**'⁶⁵. Therefore, an irregularity may be the result of an incorrect interpretation of a rule, while fraud is the result of a deliberate breach of a rule.

Other illegal behaviours may affect the EU's financial interests, such as, active or passive **corruption**⁶⁶ and **misappropriation** of EU funds or assets by a public official directly or indirectly entrusted with their management⁶⁷.

Fraud against the EU budget can also be made for committing other crimes in the context of **predicate offences**. Even if not directly linked to the protection of the EU budget, the EU legal framework on anti-money laundering and counter-terrorist financing is relevant in this context⁶⁸.

⁶⁴ As defined in Article 1 of [Council Regulation \(EC, EURATOM\) No 2988/95](#) of 18 December 1995 on the protection of the European Communities financial interests. OJ L312 of 23.12.1995, p. 1.

⁶⁵ As defined in Article 3 of the PIF Directive. In respect of revenue arising from VAT own resources, the PIF Directive requires the Member States to criminalise offences against the common VAT system when they are connected with the territory of two or more Member States of the Union and involve a total damage of at least EUR 10 million (Article 2(2) of the PIF Directive).

⁶⁶ Article 4(2) of the PIF Directive.

⁶⁷ Article 4(3) of the PIF Directive.

⁶⁸ https://ec.europa.eu/info/business-economy-euro/banking-and-finance/financial-supervision-and-risk-management/anti-money-laundering-and-counter-terrorist-financing_en#eu. At the moment of the preparation of this report Austria, Belgium, Bulgaria, Croatia, Czechia, Denmark, Estonia, France, Germany, Greece, Hungary, Italy, Latvia, Lithuania, Luxembourg, Finland, Malta, Portugal, Romania, Slovakia, Slovenia, Spain and Sweden reported full transposition of the fifth anti-money laundering directive (EU Directive 2018/843) on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing, whilst Ireland, Netherlands and Poland indicated a partial transposition.

Snapshot 12 – Organised crime and corruption

Organised crime⁶⁹ is a significant threat to European citizens, business and state institutions, as well as to the economy as a whole. Organised crime groups are present across all EU Member States⁷⁰ and use their large illegal profits to infiltrate the licit economy and public institutions, including via corruption, eroding the rule of law and fundamental rights, and undermining people's right to safety as well as their trust in public authorities. Fraud is becoming increasingly appealing for organised crime⁷¹.

Corruption is a central part of the modus operandi of organised crime groups. Under the current EU anti-corruption rules, EU Member States are required to criminalise both active and passive corruption of public officials, establish adequate sanctions and ensure that persons corrupting officials are held criminally liable. In 2019, the EU introduced new legislation protecting whistle-blowers and requiring the creation of safe channels for reporting corrupt practices. The annual Rule of Law report examines the situation of EU Member States also in relation to anti-corruption policies⁷².

The control framework put in place at European and national level (see Section 3.2) aims at preventing, detecting and correcting these risks. Member States have a frontline responsibility for managing about 80% of the expenditure budget and for collecting almost all the revenue. EU Member States should report to the Commission cases of irregularities (including potential cases of fraud⁷³) that they have detected⁷⁴. Based on these notifications ('reported fraud' or 'reported irregularities'), the Commission can identify the most recurrent fraud risks and patterns.

The following sections briefly outline the main trends in past detection of irregularities and fraud, as reported by the EU Member States. These trends point to risks that may be relevant for future action. Past detections can be seen as indicators of inherent risks and vulnerabilities in the management systems that have been exploited by fraudsters. Without significant improvements in prevention, there are risks that similar irregularities and fraud will take place also in the future.

⁶⁹ In the sense of [Council Framework Decision 2008/841/JHA](#) of 24 October 2008 on the fight against organised crime. OJ L300 of 11.11.08, p. 42.

⁷⁰ See Europol report '2021 European Union Serious and Organised Crime Threat Assessment (EU SOCTA), 12 April 2021', <https://www.europol.europa.eu/activities-services/main-reports/european-union-serious-and-organised-crime-threat-assessment>. The EU SOCTA is a comprehensive organised crime threat analysis identifying high priority crime areas produced every four years by Europol, on the basis of Member States' contributions.

⁷¹ See 'Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions on the EU Strategy to tackle Organised Crime 2021-2025'. [COM\(2021\) 170 final](#).

⁷² *Idem*, p. 25.

⁷³ The final decision on whether an irregularity actually constitutes fraud is the responsibility of the relevant authorities of the Member State involved. As criminal procedures can take a few years, unless specifically described as 'established fraud', any reference to detected fraud throughout this document should be interpreted as referring to cases of 'suspected fraud'.

⁷⁴ Certain derogations apply to this rule and are specified in the regulations detailing the reporting obligations. See Section 8 of the '[Handbook on irregularities reporting](#)'.

Snapshot 13 – Detecting fraud

Detecting fraud is far more difficult than detecting a ‘simple’ irregularity, where no deliberate attempt to defraud is made. While the latter usually may stem from a vulnerability in the first layer of control, the former, even when exploiting existing weaknesses, is the result of a specific action committed by individuals and/or organisations, with malevolent intent and methods varying from the simplest to the most complex schemes.

The detection and reporting of fraud proves that the overall control system put in place at national and EU level works.

6.1.1. VAT fraud – “Study and Reports on the VAT Gap in the EU-28 Member States” (published in 2020)

EU Member States are losing billions of euros in VAT revenues because of tax fraud and inadequate tax collection systems. The ‘VAT Gap’ (difference between expected VAT revenues and VAT actually collected) impacts the EU’s financial interests.

The overall VAT Gap in EU Member States was approximately EUR 140 billion in 2018. Based on the Commission’s projections, the VAT Gap has probably declined in 2019 and could fall below EUR 130 billion or 10% of the total VAT liability.

Individual performances of EU Member States still vary significantly from the 2018 median of 9.2%. The VAT Gap declined for 21 Member States, most significantly in Hungary (-5.1%), Latvia (-4.4%), and Poland (-4.3%). The biggest increase was seen in Luxembourg (+2.5%), followed by marginal increases in Lithuania (+0.8%) and Austria (+0.5%).

6.1.2. Irregularities and fraud in revenue

The number of reported cases compared with the five-year average declined for both fraudulent and non-fraudulent irregularities related to EU revenue. The related amount increased for fraudulent irregularities but decreased for non-fraudulent irregularities⁷⁵.

⁷⁵ For comparability reasons with previous years, the analysis for the year 2020 is carried out based on the figures obtained for the EU of 27 Member States plus the UK. The UK left the EU on 31 January 2020 and is no longer a member of the EU while the UK is still part of the internal market and customs union until 31 December 2020 as agreed in the UK–EU Withdrawal Agreement. In 2020, the UK detected and reported 2 cases as fraudulent (EUR 34 292) and 637 cases (EUR 70 788 223) as non-fraudulent.

Table 6 - Revenue: irregularities detected by national authorities - Traditional Own Resources

Budgetary sector	Fraudulent irregularities		Non-fraudulent irregularities		FDR ⁷⁶	IDR ⁷⁷
	N	EUR (million)	N	EUR (million)	%	%
Traditional Own Resources	451	108	4 003	382	0.43%	1.54%

The overall situation in 2020 appears to be less affected by the COVID-19 pandemic than could be expected. The variation of the number of cases reported as fraudulent or non-fraudulent and of the related amounts is rather within the usual range of the annual fluctuation (see box on the right). However, some EU Member States have been impacted harder than others (see Section 5.3.1).

Inspections by anti-fraud services was the most successful method of detecting fraudulent cases and related amounts in 2020. Post-release controls and release controls have been almost equally important for detecting organised duty evasion crime and new fraud patterns.

TOR: variation 2020 data compared to the five-year average 2016-2020

- 9%** number of fraudulent and non-fraudulent irregularities
- +6%** financial amounts linked to fraudulent irregularities
- 8%** financial amounts linked to non-fraudulent irregularities

Non-fraudulent irregularities were primarily detected by means of post-release controls. In monetary terms, around 43 % of total estimated and established amounts were discovered during a post-release control and 29 % were related to a tax audit, the latter gaining importance in 2020 as a method of detection.

Snapshot 14 – Most frequently recurring irregularities and types of goods concerned

Most cases reported in 2020 as fraudulent or non-fraudulent affecting EU revenue relate to **undervaluation, incorrect classification/mis-description of goods** or **smuggling**. Footwear, textiles, vehicles, electrical machinery and equipment were the types of goods most affected by fraud and irregularities in number of cases and in monetary terms.

6.1.3. Irregularities and fraud in expenditure

Over the last five years, the number of reported irregularities (fraudulent and non-fraudulent) related to EU expenditure for the programming period 2007-2013 decreased, while those linked to the 2014-2020 EU budget⁷⁸ have been increasing, consistently with

⁷⁶ FDR – Fraud Detection Rate: Ratio of financial amounts related to fraudulent irregularities on the total payments made.

⁷⁷ IDR – Irregularity Detection Rate: Ratio of financial amounts related to non-fraudulent irregularities on the total payments made.

⁷⁸ Spending areas linked to programming periods concern rural development, cohesion, fisheries policies and internal policies.

the implementation cycles. Reported irregularities related to annual spending (direct aid to farmers and market support measures) remained stable.

Table 7 - Expenditure: irregularities detected by the budgetary sector in 2020

Budgetary sector	Fraudulent irregularities		Non-fraudulent irregularities		FDR ⁷⁹	IDR ⁸⁰
	N	EUR (million)	N	EUR (million)	%	%
Agriculture	255	28.4	3 016	162.4	0.02%	0.11%
<i>Rural development</i>	127	19.2	2 086	96.9	0.14%	0.70%
<i>Support to agriculture</i>	117	6.5	903	62.1	0.02%	0.15%
<i>Both/Unclear</i>	11	2.7	27	3.4	-	-
ESI Funds	281	225.1	2 297	490.2	0.40%	0.88%
<i>Cohesion and regional</i>	221	213.7	1 685	432.1	0.52%	1.05%
<i>Social policy</i>	56	8.7	554	51.8	0.07%	0.40%
<i>Fisheries</i>	4	2.7	54	6.2	0.36%	0.82%
<i>Other</i>	0	0	4	0.2	0.00%	0.02%
Pre-accession	28	3.4	98	4.8	0.18%	0.25%
<i>IPA I</i>	17	2.9	49	3.7	n.a.	n.a.
<i>IPA II</i>	11	0.5	49	1.1	0.03%	0.06%
Direct expenditure	41	9.1	1 285	53.2	0.03%	0.28%
TOTAL	605	266.0	6 696	710.6	0.19%	0.51%

Agriculture - During the past five years (see box below), reporting of fraudulent irregularities related to rural development for 2014-2020 has had a slow start - which might indicate **insufficient detection efforts** in EU Member States - and decreased for the programming period 2007-2013 - as expected. Reporting of fraud was rather stable for support to agriculture (including direct aid to farmers and market measures).

In proportion to payments received by the EU Member States, **rural development** seems to be more affected by fraud than **direct aid to farmers**. The latter is entitlement-based and systems in place support prevention.

Market measures absorb less financial resources, but the incidence of reported fraud in proportion to payments is even higher than for rural development (see **Figure 14**). Reported fraud concerns, in particular, national support programmes for the wine sector (investment measures, promotion, especially in non-EU markets, and restructuring and conversion of vineyards), the fruits and vegetables sector (aid for producer groups for preliminary

Agriculture: variation 2020 data compared to the five-year average 2016-2020

+5% number of fraudulent and non-fraudulent irregularities

-37% financial amounts linked to fraudulent irregularities

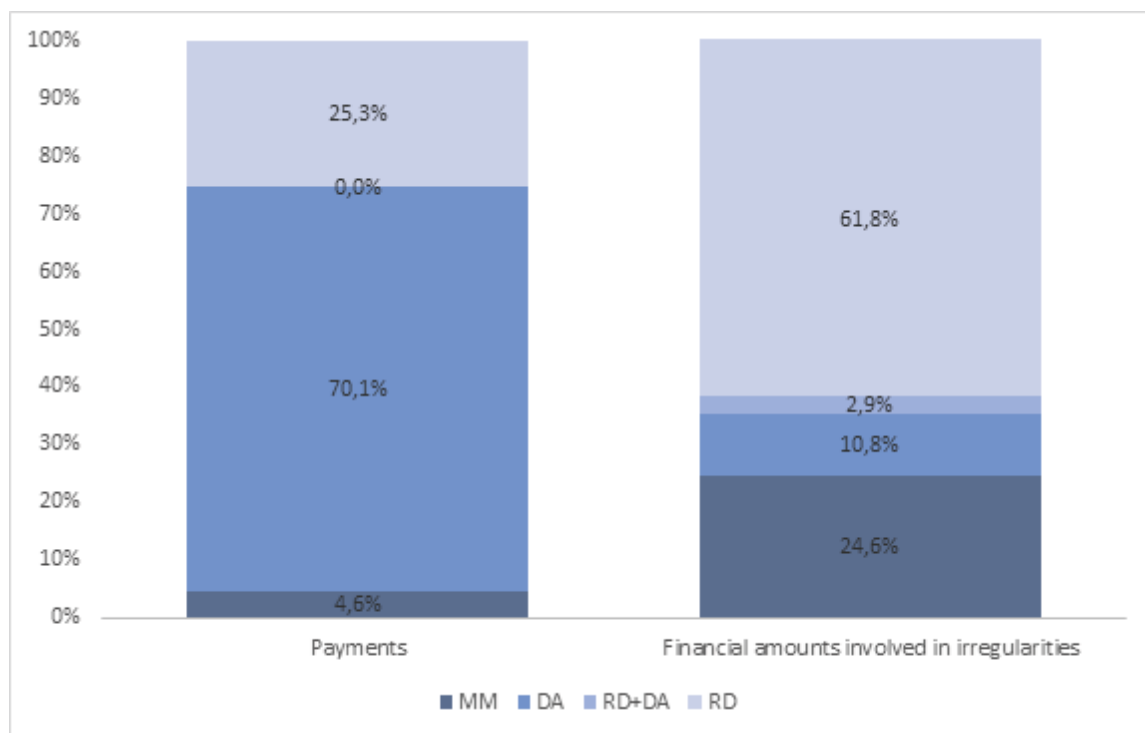
-5% financial amounts linked to non-fraudulent irregularities

⁷⁹ FDR – Fraud Detection Rate: Ratio of financial amounts related to fraudulent irregularities on the total payments made.

⁸⁰ IDR – Irregularity Detection Rate: Ratio of financial amounts related to non-fraudulent irregularities on the total payments made.

recognition, especially investment measures). Also the 'Promotion' sector seem to have a higher incidence of fraud, both on EU markets and on non-EU markets.

Figure 14 - Share of the different components of common agricultural policy (CAP) in payments and in financial amounts involved in irregularities (EU-27 - 2020)



Snapshot 15 – Agriculture: irregularities most frequently detected

In agricultural spending, as in many other areas of spending, there is a risk of **falsification of documents**. For rural development, falsification may concern, for example, invoices, declarations of equipment as new while it is second-hand, offers in the context of procurement, information about compliance with conditions for receiving the aid. For the other forms of support to agriculture, falsification may relate, for example, to invoices or lease agreements, or to requests for aid, which may include false information about the eligible area at disposal, compliance with other conditions for aid, etc. There is also the risk of the **creation of artificial conditions**. For example, beneficiaries may artificially split agricultural holdings and request aid through several linked companies, to avoid degressive aid rates or limits in terms of area or animals. For rural development, a significant number of fraudulent irregularities concern **incomplete implementation of the action**, pointing to significant risks in this sector. On market measures, high financial amounts were recorded in several cases of **conflict of interest** combined with other breaches linked to promotion and investigated by OLAF.

Cohesion and fisheries policies - During the past five years, the number of detected and reported fraudulent and non-fraudulent irregularities for the programming period 2007-13 for the European Structural and Investment Funds (ESIF, i.e. the Cohesion Fund, European Regional Development Fund, European Social Fund and Fisheries Funds) dropped in line with the

Cohesion policy: variation 2020 data compared to the five-year average 2016-2020

- 34%** number of fraudulent and non-fraudulent irregularities
- 37%** financial amounts linked to fraudulent irregularities
- 42%** financial amounts linked to non-fraudulent irregularities

implementation cycle (see box on the right). The number of irregularities reported for 2014-2020 has been rising. However, for non-fraudulent irregularities this increase was limited, highlighting an exceptional drop in the number of detected irregularities (and related financial amounts) in comparison to the previous programming period. The gap is significant for all funds, but in particular for the European Regional Development Fund.

Snapshot 16 – Cohesion and fisheries policies: irregularities most frequently detected and thematic areas concerned

ESIF projects on **research and technological development, innovation and entrepreneurship** are the most frequently affected by the reported fraudulent as well as non-fraudulent irregularities. EU Member States are reporting an increasing number of fraudulent irregularities related to **measures to improve employability**. Also fraudulent irregularities concerning infrastructure intended to provide basic services to Europeans (such as **energy, environment, transport and ICT**) and **social, health and education infrastructure** are increasingly reported. The highest financial amounts related to non-fraudulent irregularities are associated with infrastructure projects, in particular **TEN-T motorways and roads** (core network).

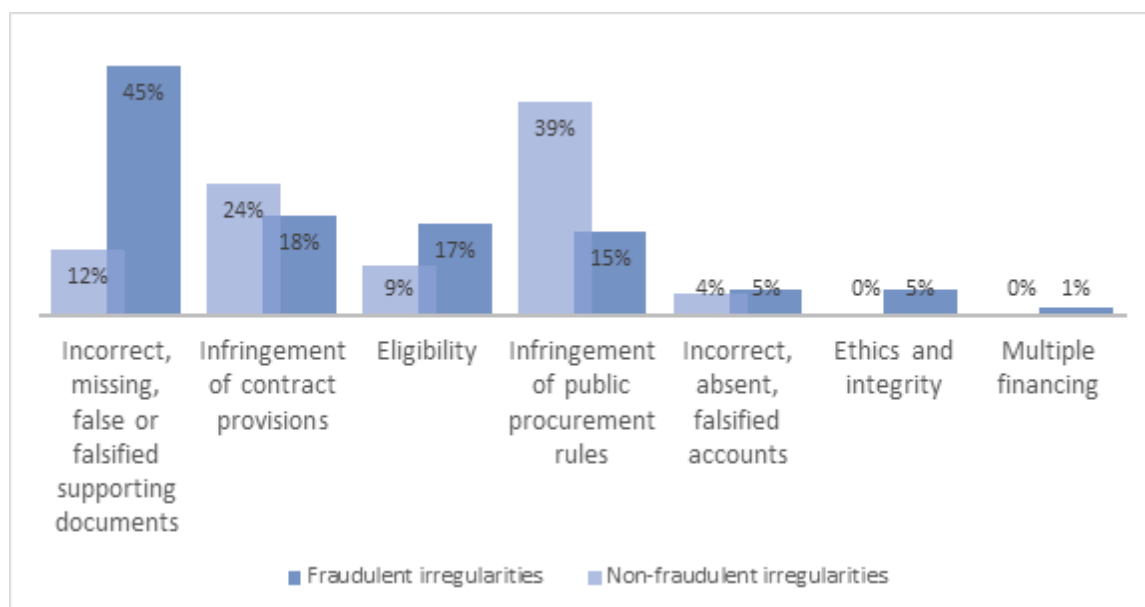
In proportion to payments, the **fisheries policy** seem to be an area highly affected by fraud and irregularities. Measures for **productive investments in aquaculture** and **investments in processing and marketing** appear among the riskiest operations. **Technical assistance** and the **development of new markets and promotional campaigns** also seem vulnerable.

Figure 15 shows the most frequently detected types of irregularities in relation to fraudulent irregularities for projects financed under the programming period 2014-2020. They were: **incorrect, missing, false or falsified supporting documents, infringement of contract provisions, eligibility and infringement of public procurement rules**. Breaches in relation to **ethics and integrity**⁸¹ and **double-funding** appeared in 5% and 1% of the detected cases, respectively. With the increasing use of simplified cost options, risks move further to the actual and correct implementation of the action. This must be considered in control strategies.

In relation to non-fraudulent irregularities, **infringements of public procurement rules** represent the most significant share (see *Snapshot 18* for risks linked to public procurement).

⁸¹ This category includes issues related to 'conflict of interest' and 'corruption.'

Figure 15 – Types of irregularities detected in fraudulent and non-fraudulent cases - programming period 2014-2020



Direct expenditure – Detected fraudulent irregularities related to direct expenditure by the Commission have fallen since 2016 and remained rather stable over the last three years. In relation to non-fraudulent irregularities, 2020 was the year in which the lowest figure was recorded for both number of cases and amounts concerned.

Snapshot 17 – Direct expenditure: irregularities most frequently detected and policy areas concerned

The most recurrent types of irregularities concern the **eligibility of expenditure** and **under-performance/non-performance**. Specifically in relation to fraudulent irregularities, issues linked to the **supporting documentation** is the second most recurrent type after ‘eligibility.’

In 2020, the policy areas most concerned by the irregularities were **research and innovation, communication networks, content and technology** and **international cooperation and development**.

6.2. Additional risks of irregularities and fraud for 2021 and beyond

In recent history, the year 2020 has been unprecedented due to the COVID-19 pandemic. In this context, the Recovery and Resilience Facility also changes the situation in terms of risks. New objectives and significant changes in the environment must swiftly trigger actions by EU Member States and the Commission to identify and assess additional risks of irregularities and fraud.

6.2.1. COVID-19 risks in revenue

The year 2020 was marked by the COVID-19 pandemic and by the sharp drop in import flows. Trade within the EU-27⁸² was hit hard. A significant fall in imports (-11.6 %) was

⁸² The UK left the EU on 31 January 2020 and is no longer a member of the EU while the UK is still part of the single market until 31 December 2020 in line with the UK–EU Withdrawal Agreement.

observed compared with 2019⁸³. The **drop in import volume** and a significant **shift towards e-commerce** caused by the COVID-19 pandemic has led not only to changes in the number of customs declarations to be cleared but also to a shift in customs workload and work patterns. The reaction of national authorities to those **challenges** and the speed with which the customs authorities were able to adapt to new circumstances are only partially comparable, as the changing rules of lockdowns have changed greatly over the course of the year among EU Member States and within specific regions in some EU Member States.

Based on the overall figures, it seems however that the variation of the total number of reported irregularities (fraudulent and non-fraudulent) and of the related amounts is rather within the usual range of the annual fluctuation⁸⁴ and therefore, probably less affected by the COVID-19 pandemic. However, customs fraud appear to have affected EU Member States to differing degrees during the COVID-19 pandemic. Whereas the detection rates⁸⁵ of Belgium, Bulgaria, Germany, Croatia, Hungary, Poland, Slovenia and Sweden were the highest in 2020 compared to the previous five years, the detection rates in Italy, the Netherlands, Austria, Portugal and Slovakia were the lowest⁸⁶.

For COVID-19 related goods, a slight increase in the amounts reported as irregular was observed in 2020, in particular for goods such as protective garments. However, analysis shows that the impact of irregularities affecting COVID-19 related goods appear to have remained relatively low in 2020 (6% of the total number of irregularities reported in 2020 and 3% of the related amounts).

6.2.2. COVID-related risks in expenditure

The COVID-19 pandemic has pushed the EU institutions and the EU Member States to enable the EU budget to support the response to the crisis, adding the necessary resources and flexibility. The EU has strict rules to protect its budget from fraud. However, fraudsters are swift in adapting their operations. A number of key potential risks related to the COVID-19 outbreak may bring new opportunities to them.

First, there are risks related to **managing the emergency**, which requires simplified procedures. The *abuse of simplified procedures* may lead to less competitive public procurement and direct award, which increase the risk of conflict of interest and corruption and make controls more difficult. Emergency procedures may lead to *lower quality of tender specifications*, making it easier for fraudsters to inflate costs or reduce quality during implementation. Urgent operations may receive EU funding after they have been completed outside the management and control framework for EU funds (*retroactive financing*). While the services of consulting companies can be of great assistance, increased reliance on them may present fraud risks. Increased demand and

⁸³ Source: EUROSTAT, EU trade in goods strongly impacted by the COVID-19 pandemic in 2020, <https://ec.europa.eu/eurostat/product?code=DDN-20210325-1>

⁸⁴ Taking into account that new reporting rules for fraudulent and non-fraudulent cases detected during post-clearance controls were introduced in September 2019, with a potential effect that post-clearance detection are not artificially split anymore based on the CN headings.

⁸⁵ Individual bigger cases detected in a specific year may affect annual rates significantly. The detection rates can also be affected by the way a Member State's customs control strategy is set up to target risky imports and to detect TOR-related fraud and irregularities.

⁸⁶ No conclusion can be drawn for Cyprus, Luxembourg and Malta due to very few cases reported in 2016-2020.

disruption of supply chains during emergencies may lead to *contractual relationships with unreliable counterparts*.

Other risks are due to **pressure** on the authorities in charge of managing EU funds. Delays in the current operational programmes due to the COVID-19 pandemic, new needs related to emergency spending, and the start of the next programming period can be *stress factors* benefiting fraudsters using networks of (shell) companies offering the same services in multiple projects in different operational programmes (risks of conflict of interest, double-funding, etc.), or inflating costs through fake intra-network transactions. Such pressure may add to the challenge of assessing applicants' declarations, which increases the risk of inflated costs and of funding to companies with no financial and operational capacity. It may also lead to a reduction in the use of guarantees, or a decrease in the quantity or quality of controls, also hampered by travel restrictions.

Another risk may be related to beneficiaries unduly invoking 'force majeure' to justify non-compliance with contractual obligations in the implementation of programmes. This may even facilitate fraudulent bankruptcies, falsely pretending the crisis caused them.

These risks may apply to 2020, requiring adaptation of the control strategies related to the operations implemented during the peak of the sanitary emergency, and to 2021 and beyond, requiring prevention through specific mitigating measures and targeted action to detect future irregularities and fraud.

6.2.3. Risks related to the Recovery and Resilience Facility

In relation to the Recovery and Resilience Facility, Regulation (EU) 2021/241 singles out, in particular, four specific risks against which EU Member States must take appropriate measures: i) fraud, ii) corruption, iii) conflicts of interest, and iv) double-funding.

These risks are defined as '**serious irregularities**' in the regulation.

The RRF will bring a large amount of money to some EU Member States that already have a **weak absorption capacity** of European Structural and Investment Funds. This will add **pressure on the management and control system**.

Most EU Member States need to develop new IT tools to collect and manage the information to implement the RRF. Interoperability between different national systems may not be ensured.

In implementing the RRF, EU Member States will need to ensure an effective and efficient **internal control system** and to develop a reliable IT infrastructure to collect:

- a) information about the achievement of milestones and targets; and
- b) standardised categories of data (on final recipients, contractors, sub-contractors and beneficial owners).

The Commission will make available an information and monitoring system, including a single data mining and risk-scoring tool, to access and analyse this data and information for generalised application by the EU Member States.

The Commission, OLAF, the Court of Auditors and, where applicable the EPPO can use the information and monitoring system within the scope of their mandates.

Snapshot 18 – Focus on the healthcare sector

Following the COVID-19 outbreak, EU funding to strengthen national healthcare systems increased and will increase further in the next programming period, including national plans related to the RRF. Therefore, the impact of risks materialising is higher, vulnerabilities must be identified and risks mitigated.

Projects to improve the healthcare infrastructure are complex, requiring the procurement of services, works and supplies of medical and ordinary equipment. Broadly speaking, risks of irregularities and fraud are related to the (i) **restrictions to competition** (by limiting information, excluding or discouraging potential tenderers, non-transparent selection or evaluation, collusion); (ii) **changes to contracts after award**; (iii) **implementation shortcomings**; (iv) **inflation of costs**.

On **restrictions to competition**, the openness of the procedure may be undermined by irregularities related to the ‘how,’ ‘what’ or ‘timing’ of the publication of the contract notice, which is meant to inform all potential bidders. This may be the result of undervaluation of the estimated value of the contract or the artificial splitting of contracts. The number of potential bidders may be unduly reduced through excessive or discriminatory requirements concerning the tenderer. Furthermore, contracting authorities may unduly group in the same contract, works, supplies or services that are usually offered by different economic operators (artificial grouping). Other possible malpractices concern technical specifications, which are too narrow or even referring to a specific brand. Unclear or changing terms and conditions may make participation more difficult. Insufficient documentation of the evaluation process and vague or irregular award criteria may make the evaluation non-transparent. Contracts may be awarded to operators that do not meet the criteria. On the other hand, the exclusion of certain operators may be unjustified. Competition may be defeated by collusion, including cooperation among bidders or between bidders and contracting authority.

Contracts may be changed after the award. The contract can be different from the tender specifications already at the first signature or it may be changed during implementation. If such changes had already been part of the tender specifications, other operators could have made better offers and could have won. Furthermore, these changes can generate extra-profits for the economic operator, because of cheaper/less materials or less works, for the same price or because of additional supplies or works, for a higher price. Existing contracts may be amended or additional contracts may be unduly awarded to the current contractor, directly or after a negotiated procedure without publication.

Shortcomings in implementation may take various forms. This can have serious consequences in healthcare facilities. They may be accompanied by documents that do not match with actual implementation on the ground. Irregularities may also be due to expenditure that does not lead to the expected improvements in the delivery of health services. For example, the beneficiary may not or may rarely use the medical equipment funded by the project, equipment may be used for commercial purposes, contrary to the objectives of the funding, etc.

Excessive prices may be paid for medical equipment. Requests for reimbursements may include costs for ineligible supplies or activities. The project may cover only new

medical equipment, while the actual spending may be for ineligible second-hand equipment (with an inflated price, as if it was new). Double-funding is another potential risk.

7. TOOLS TO STRENGTHEN THE FIGHT AGAINST FRAUD

The Commission will build on its existing tools and develop new ones to tackle the challenges that have arisen during the COVID-19 pandemic and new ways of managing EU funding.

7.1. ARACHNE

The Commission encourages the use of ARACHNE, an integrated IT tool for data mining and data enrichment. It has been developed by the Commission to support managing authorities in their administrative controls and management checks in Structural Funds (European Social Fund and European Regional Development Fund). It has also been extended to the European Agricultural Fund for Rural Development (EAFRD) projects and will be used for all agricultural funds following the CAP reform.

ARACHNE establishes a comprehensive database of EU projects implemented under the Funds, provided by managing authorities and paying agencies, and enriches these data with publicly available information in order to identify, based on a set of risk indicators, the projects, beneficiaries, contracts and contractors which might be susceptible to risks of fraud, conflict of interest and irregularities.

The tool provides highly valuable risks alerts to enrich management verifications, but it does not supply any proof of error, irregularity or fraud. ARACHNE can increase the efficiency of projects selection, management checks and further strengthen fraud identification, prevention and detection.

In view of the risks highlighted in Section 6, a generalised and systematic use of tools like ARACHNE would allow stepping up the fight against fraud, irregularities, conflict of interest and double-funding.

7.2. The Early Detection and Exclusion System (EDES)

The Commission manages the Early Detection and Exclusion System (EDES). EDES is referred to in Articles 135 to 145 of the Financial Regulation applicable to the EU budget⁸⁷. It is a tool to strengthen the protection of the EU's financial interests against unreliable entities and persons by excluding such economic operators from participation in EU funds award procedures under direct and indirect management. Prohibited practices include a broad range of behaviours that affect professional integrity (e.g. fraud, corruption and grave professional misconduct) and bad performances (such as significant deficiencies in the implementation of contracts).

⁸⁷ Regulation (EU, Euratom) 2018/1046 of the European Parliament and of the Council of 18 July 2018 on the financial rules applicable to the general budget of the Union, amending Regulations (EU) No 1296/2013, (EU) No 1301/2013, (EU) No 1303/2013, (EU) No 1304/2013, (EU) No 1309/2013, (EU) No 1316/2013, (EU) No 223/2014, (EU) No 283/2014, and Decision No 541/2014/EU and repealing Regulation (EU, Euratom) No 966/2012, OJ L 193 of 30.7.2018, p.1.

In particular, EDES allows for:

- the early detection of entities or persons, which pose a risk to the EU's financial interests;
- the exclusion of such economic operators from obtaining EU funds under direct and indirect management and/or the imposition of a financial penalty;
- the registration of the above information in the EDES Database which is accessible to the community of financial actors in charge of the implementation of Union's funds;
- in the most serious cases of exclusion, the publication of the names of the entities or persons concerned, on the Commission's internet site.⁸⁸

EDES allows for a centralised assessment of exclusion situations, while protecting the fundamental rights of persons and entities concerned, in particular their right to be heard.

The singularity and strength of the EDES system lies in the power given to the EU institutions and bodies⁸⁹ to act "*in the absence of a final national judgment or, where applicable, a final administrative decision*".⁹⁰ The imposition of sanctions can be based on established "facts and findings" stemming from audits, checks or controls performed under the responsibility of the competent authorising officer⁹¹, investigations carried out by the OLAF or non-final administrative decisions of national authorities or international organisations.

The decision to impose a sanction on unreliable economic operators may be adopted by the relevant authorising officer only after first obtaining a formal recommendation⁹² from the centralised inter-institutional panel⁹³.

7.3. GetI project

The GetI project aims at boosting the analytical capacity of OLAF staff working both on operational and strategic tasks, by improving the accessibility and visualisation of information, speed and flexibility in querying data.

The diversity of data formats and the volume of unstructured data has generated in recent years the need for an environment, tools and functions that facilitate the analytical work. Through a collection of open sources and commercial software, GetI aims at automating many time-consuming tasks and deploying modern technologies, such as artificial intelligence.

⁸⁸ http://ec.europa.eu/budget/edes/index_en.cfm

⁸⁹ For their respective budget implementation.

⁹⁰ Wording used in Article 136 of the Financial Regulation.

⁹¹ The authorising services can be that of EU institutions, agencies, offices and bodies.

⁹² For the situations referred to in Article 136(1)(c) to (h) of the Financial Regulation (*i.e.* grave professional misconduct, fraud, serious breaches of contractual obligations, irregularities, shell companies creation).

⁹³ For a detailed overview of the decisions taken by the Panel in 2020 see 'Early Detection and Exclusion System (EDES) — Panel referred to in Article 143 of the Financial Regulation' accompanying this report.

7.4. National IT tools to protect the EU's financial interests

In 2020 EU Member States communicated the development of several IT tools (see **Table 8**) to strengthen the protection of the EU's financial interests⁹⁴ which will be of particular importance in tackling the challenges that have arisen with the COVID-19 pandemic and new ways of managing EU funding.

Table 8 – IT tools deployed by EU Member States in 2020

Member State	Tool	Budgetary sector
Bulgaria	Use of a centralised electronic platform in public procurement	All expenditure
Czechia	Update of procedures for checking ownership structures and conflicts of interest	Cohesion policy
Denmark	Merging data to identify cases of double-financing	Cohesion policy
Estonia	Launch of a cybercrime information and notification website	Horizontal
	Enhancement of the Public Procurement Register	All expenditure
Germany	Fraud risk self-assessment for the Federal ESF and ERDF programmes	Cohesion policy
Hungary	Use of ARACHNE and EDES	Cohesion policy and Fund for the most deprived
Lithuania	Acquisition of the analytical software and hardware to implement anti-money laundering and counter-terrorist financing measures	Horizontal
	IT tools and regulatory measures	Agriculture
The Netherlands	Enhanced digital subsidy application	Agriculture
	Risk-scoring tool: selection of lots susceptible to fraud	Agriculture
Romania	Digitalised checks of ESIF competent bodies to make checks more efficient in the area of public procurement	Cohesion policy
Spain	Direct access by AFCOS to the databases of the Spanish Social Security	All expenditure
Sweden	Better procurement statistics	All expenditure

8. CONCLUSIONS AND RECOMMENDATIONS

The health crisis caused by COVID-19 has had and will continue to have great economic and social impacts on our lives. The EU response, through the resources provided for the next EU budget and Next Generation EU represent the biggest recovery plan in Europe since the Marshall Plan.

A revamped EU anti-fraud architecture is in place to protect EU taxpayers' money, relying on:

- the investigative and prosecutorial powers of the EPPO;
- the coordinating role of Eurojust;
- the analytical capacity of Europol; and
- a reformed OLAF equipped with the tools to work with the EPPO and to carry out even more effective investigations.

A close and effective cooperation with national authorities is needed as they are adapting to cope with new risks and new ways of managing EU funds. The management of the

⁹⁴ See Section 5 of 'Measures adopted by the Member States to protect the EU's financial interests in 2020, accompanying this report.

RRF and a significant part of the spending programmes for 2021-2027 will be performance-based and EU Member States will bear an increased share of responsibility.

These exceptional changes do not speak in favour of a 'business as usual' approach. Increased efforts and measures are needed for a European recovery, which call for a renewed and joint European vision for fighting fraud, corruption and other illegal activities affecting the EU's financial interests.

This vision could be built around the following elements:

- A **more efficient collection and use of data**, fully exploiting the opportunities offered by IT interconnectivity, data mining and risk-scoring tools. The use of pan-European tools would further increase this efficiency and target more effectively risky areas.
- Improved **transparency** for beneficiaries (including contractors, sub-contractors and beneficial owners) of public (European and national) funding.
- Better coordinated, holistic anti-fraud efforts at EU Member State level, based on developing and implementing national **anti-fraud strategies**.
- More **cooperation** within national authorities, between EU Member States and with the European level.

Recommendation

EU Member States which have not joined the EPPO should consider doing so.

EU Member States which have not adopted a national anti-fraud strategy should consider doing so. National strategies adopted in the past and not adapted to the new significant risks should be swiftly updated.

Revenue

EU and national customs policies made a significant contribution to the EU's COVID-19 response in 2020 ensuring smooth trade flows for Europeans and protecting the EU's financial interests. Some EU Member States were faster and more flexible in adjusting their control activities. The degree of divergence at national level and the differing length of confinement measures as well as country-specific challenges had an impact on EU Member States' capacity to adapt to the harsh reality of 2020.

It is now essential to explore all avenues for ensuring that the customs union and EU Member States' customs authorities operate optimally, remain flexible and resilient in times of crisis and better anticipate problems. This implies, above all, a new emphasis on ensuring greater availability and use of data and data analysis for customs purposes as well as the development of an appropriate set of foresight and common crisis management tools. Therefore, further steps towards risk assessment, standardised checks and EU-wide and international coordination and cooperation in detecting irregular cases are required, taking into account that fraud and the spreading of specific fraud mechanisms are not constrained by national borders.

Recommendations

EU Member States are invited to assess the risks and shortcomings of the national customs control strategies revealed through the COVID-19 pandemic, and to report lessons-learned and remedial measures taken in order to:

- improve flexibility for the type of customs checks;

- diminish the potential impact of unexpected future events;
- ensure the implementation of uniform controls within the EU.

Furthermore, Member States are invited to assess the financial risks that might not have been sufficiently addressed during 2020 and to establish catch-up plans for carrying out appropriate customs checks where due to confinement measures such customs checks had to be cancelled or postponed e.g. checks at operators' premises and physical checks before releasing goods into free circulation.

Expenditure

Risks can only be mitigated if they have been identified. A lost opportunity in terms of risk identification weakens EU Member States and exposes them to the full extent of the risks both in terms of impact and likelihood. It is therefore critical in the current circumstances that EU Member States perform in-depth and targeted risk assessments. This will contribute to strengthening rules on internal control frameworks.

Recommendation

If not already done, EU Member States are invited to launch **targeted risk management exercises** linked to the impact of COVID-19 and the upcoming implementation of the Recovery and Resilience Facility.

In this respect, **transparency** as regards the use of the public resources is key. It does not only constitute a deterrent element, but also involves civil society, contributing to improving taxpayer's trust in how public authorities manage public money.

Data analysis to identify and target suspicious transactions has become an essential part of the fight against fraud and its importance will continue to grow in the coming years.

Recommendation

The way in which underlying data, as well as those concerning detected irregularities and fraud, are collected and used, needs to be further improved. The Commission will further develop the Irregularity Management System. National authorities will need to report quality data that is reliable.

In terms of data mining and risk-scoring capabilities, a pan-European IT tool would:

- Make the collection and monitoring of data easier for the Commission and greatly benefit the investigative tasks of OLAF, EPPO and national law enforcement, in particular in relation to cross-border cases;
- Increase the possibility for the Commission, OLAF and EU Member States of i) analysing risk patterns and trends; ii) identifying risky beneficiaries, and iii) excluding unreliable beneficiaries from EU funding.

Recommendation

All EU Member States should make use of the integrated and interoperable information and monitoring system that the Commission will make available for the Recovery and Resilience Facility and the EU budget.