

Special Report

Tackling fraud in EU cohesion spending: managing authorities need to strengthen detection, response and coordination

(pursuant to Article 287(4), second subparagraph, TFEU)



EUROPEAN
COURT
OF AUDITORS

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Executive summary

I EU legislation defines fraud as a deliberate infringement that is, or could be, prejudicial to the EU budget. It is the joint responsibility of the EU and the Member States to counter fraud and any other illegal activities, such as corruption, affecting the EU's financial interests. Between 2013 and 2017, the Commission and the Member States identified more than 4 000 potentially fraudulent irregularities. The EU support affected by these irregularities amounted to almost €1.5 billion, 72 % of which concerned EU cohesion policy. In this field, the managing authorities in the Member States are responsible for setting up proportionate and effective anti-fraud measures that take account of the identified risks. Such measures should cover the full anti-fraud management process (fraud prevention, detection and response, up to and including reporting on detected cases and recovery of funds unduly paid). The rate of detected fraud in relation to EU cohesion funding for the 2007-2013 period ranged from 0 % to 2.1 %, depending on the Member State.

II Through this audit, we assessed whether managing authorities have properly met their responsibilities at each stage of the anti-fraud management process. To this end, we assessed whether managing authorities have:

- (a) developed anti-fraud policies, performed a thorough risk assessment and implemented adequate preventive and detective measures; and
- (b) properly responded to detected fraud in coordination with other anti-fraud bodies.

III We found that managing authorities assessed the risk of fraud in the use of Cohesion funding better for the 2014-2020 programming period, using in most cases the "ready-to-use" tool included in the Commission guidance. However, some of these analyses were not sufficiently thorough. Although they have improved fraud prevention measures, they have made no significant progress towards proactive fraud detection. Additionally, they have not often developed procedures for monitoring and evaluating the impact of their prevention and detection measures.

IV In the area of fraud response, managing authorities, in coordination with other anti-fraud bodies, have not been sufficiently reactive to all detected cases of fraud. In particular, reporting arrangements are unsatisfactory, several managing authorities fail to systematically communicate suspicions of fraud to the competent bodies, corrective measures have a limited deterrent effect and the coordination of anti-fraud activities is insufficient. We also found that the fraud detection rate for the 2007-2013

programming period in the Commission's 2017 report on the protection of the EU's financial interests is not a true representation of the level of fraud actually detected in the Member States visited, but rather show an indication of the fraud cases that they decided to report to the Commission.

V As a result of our audit, we recommend that:

- (i) Member States that do not have a national anti-fraud strategy should formulate one; unless a sufficiently detailed strategy exists at national level, the Commission should require managing authorities to develop formal strategies and policies to combat fraud against EU funds;
- (ii) managing authorities make fraud risk assessment more robust by involving relevant external actors in the process;
- (iii) Member States improve fraud detection measures by generalising the use of data analytics tools and the Commission by promoting actively the use of other 'proactive' and other new fraud detection methods;
- (iv) the Commission monitors fraud response mechanisms to ensure they are consistently applied; and
- (v) the Commission encourages Member States to expand the AFCOSs' functions to improve coordination.

VI During the negotiations and approval process of the CPR for the period 2021-2027, the co-legislators could consider:

- making compulsory the adoption of national strategies or anti-fraud policies and the use of proper data analytics tools (e.g. Arachne);
- introducing sanctions and penalties for those responsible for fraud against EU's financial interests.

VII While respecting the Member States' right to flexibility in defining and organising their own work against fraud in line with the principle of subsidiarity, the EU co-legislators could consider determining minimum functions for the Anti-Fraud Coordination Service (AFCOS) in the Member States in order to ensure an effective coordination role.

Introduction

The fight against fraud in the EU

01 EU legislation distinguishes between¹:

- o 'Non-fraudulent irregularities', defined as any infringement of a provision of EU law resulting from an act or omission by an economic operator which has, or would have, the effect of prejudicing the general budget of the EU or budgets managed by them because of an unjustified item of expenditure².
- o 'Fraudulent irregularities' (or 'fraud'), defined³ as any intentional act or omission relating to:
 - the use or presentation of false, incorrect or incomplete statements or documents, which has as its effect the misappropriation or wrongful retention of funds from the general budget of the EU or budgets managed by, or on behalf of, the EU,
 - non-disclosure of information in violation of a specific obligation, with the same effect, or
 - the misapplication of such funds for purposes other than those for which they were originally granted.

02 Article 325 of the Treaty on the Functioning of the European Union (TFEU) stipulates that it is the joint responsibility of the EU (represented by the Commission) and the Member States to counter fraud and any other illegal activities affecting the EU's financial interests. This obligation covers all EU revenue and expenditure programmes and all policy areas.

¹ We have removed references to EU revenue from these definitions.

² Article 1(2) of Council Regulation (EC, Euratom) No 2988/95 of 18 December 1995 on the protection of the European Communities' financial interests (the 'PIF Regulation') (OJ L 312, 23.12.1995, p. 1).

³ Article 1(a) of the Annex to the Council Act of 26 July 1995 drawing up the Convention on the protection of the European Communities' financial interests (the 'PIF Convention').

03 EU cohesion policy is structured around three of the European Structural and Investment Funds⁴ (ESIFs): the European Regional Development Fund (ERDF), the Cohesion Fund (CF) and the European Social Fund (ESF) — which together are known as the EU cohesion policy funds. The Commission and the Member States jointly implement these funds through operational programmes (OPs), which detail how Member States will spend EU funding during a programming period:

- There were 440 OPs in Cohesion for the 2007-2013 programming period. Almost two thirds of these OPs are already closed.
- There are 389 OPs for the 2014-2020 programming period. These OPs are still ongoing.

04 At the level of the Commission, two directorates-general are responsible for the implementation of EU cohesion policy: the Directorate-General for Employment, Social Affairs and Inclusion and the Directorate-General for Regional and Urban Policy. In the Member States, three different types of ‘programme authorities’ are involved in implementing and checking each OP:

- the managing authority (responsible for implementing the OP),
- the certifying authority (responsible for submitting payment applications to the Commission and preparing the OP’s annual accounts), and
- the audit authority (responsible for providing an independent opinion on the reliability of the accounts, the legality of the expenditure incurred and the functioning of the management and control systems).

05 The legal framework for EU cohesion policy in the 2007-2013 programming period made Member States responsible for the prevention, detection and correction of irregularities (including fraud) and for the recovery of funds unduly paid⁵. This

⁴ The other ESIFs are the European Agricultural Fund for Rural Development (EAFRD) and the European Maritime and Fisheries Fund (EMFF).

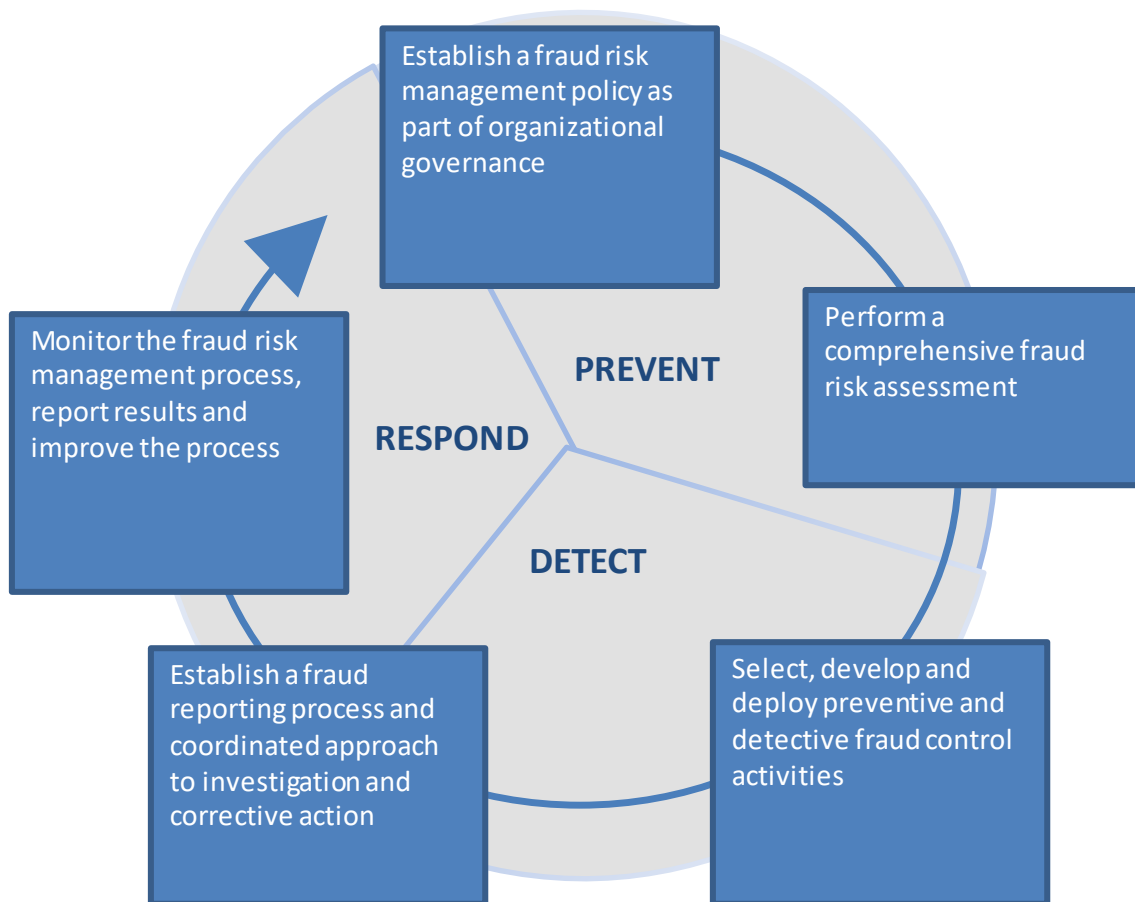
⁵ Articles 58(h), 70(1)(b) and 98(1) of the consolidated version of Council Regulation (EC) No 1083/2006 of 11 July 2006, laying down general provisions on the European Regional Development Fund, the European Social Fund and the Cohesion Fund and repealing Regulation (EC) No 1260/1999 (OJ L 210, 31.7.2006, p. 25), and Articles 20(2)(a), 28(1)(e) and (n), 28(2), 30 and 33(2) of the consolidated version of Commission Regulation (EC)

requirement is more explicit in the Common Provisions Regulation (CPR) for the 2014-2020 programming period, which requires managing authorities to “put in place effective and proportionate anti-fraud measures taking into account the risks identified”⁶. The Commission recommends⁷ that managing authorities deal with the full anti-fraud management process (see *Figure 1*), which comprises fraud prevention, fraud detection and fraud response (mainly including reporting on detected cases and recovery of funds unduly paid). In this regard, the Commission applies a principle of zero tolerance for fraud and corruption⁸.

No 1828/2006 of 8 December 2006 setting out rules for the implementation of Council Regulation (EC) No 1083/2006 (OJ L 371, 27.12.2006, p. 1).

- ⁶ Article 72 and 125(4)(c) of Regulation (EU) No 1303/2013 of the European Parliament and the Council of 17 December 2013 laying down common provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund, the European Agricultural Fund for Rural Development and the European Maritime Fisheries Fund and laying down general provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund and the European Maritime Fisheries Fund (OJ L 347, 20.12.2013, p. 320), hereafter referred to as CPR. Throughout this report we refer to the ‘anti-fraud management process’, which corresponds to the term ‘anti-fraud management cycle’ used by the Commission in its guidance documents.
- ⁷ Commission’s guidance for Member States and programme authorities on fraud risk assessment and effective and proportionate anti-fraud measures (EGESIF 14-0021), page 11.
- ⁸ Section 2.2.1 of the Joint Anti-fraud Strategy 2015-2020 for ERDF, CF, ESF, FEAD, EGF, EUSF and EMFF, Ares (2015) 6023058 of 23 December 2015 (available at: <http://ec.europa.eu/sfc/sites/sfc2014/files/sfc-files/JOINT%20ANTI-FRAUD-STRATEGY2015-2020.pdf>).

Figure 1 – Fraud risk management process



Source: ECA, based on COSO framework

06 The European Anti-Fraud Office (OLAF) is the key anti-fraud body for the EU. It contributes to the design and implementation of the Commission’s anti-fraud policy and conducts administrative investigation into fraud, corruption and any other illegal activity affecting the EU budget.

07 At the level of the Member States, managing authorities are not alone in the implementation of anti-fraud measures. Since 2013, each Member State has been required to designate an anti-fraud coordination service (AFCOS) to facilitate effective cooperation and exchange of information, including information of an operational

nature, with OLAF⁹. Through further guidance¹⁰, the Commission specified that AFCOSs should have the mandate, within the Member State, to coordinate all legislative, administrative and investigative obligations and activities relating to the protection of the EU's financial interests. In shared management, Member State authorities report cases of suspected or established fraud (and other irregularities) to the Commission through the Irregularity Management System (IMS) hosted at OLAF's anti-fraud information platform.

Significant incidence of reported fraud in EU cohesion policy compared to other spending areas

08 On 5 July 2017, the European Parliament and the Council adopted Directive (EU) 2017/1371 on the fight against fraud to the Union's financial interests by means of criminal law (the 'PIF Directive'¹¹). The Directive establishes a common definition of fraud against the EU's financial interests, in particular in the field of public procurement. Member States must enact the PIF Directive in national legislation by 6 July 2019¹².

09 In September 2018, the Commission published its 29th annual report on the protection of the European Union's financial interests¹³ (hereafter referred to as the 2017 PIF report). For shared management, the Commission prepares this report based on the information reported by Member States through the IMS (see paragraph **07**). The analysis of the 2017 PIF report shows that the incidence of reported fraud (suspected and established) in EU cohesion policy is significantly higher than in other areas: Cohesion represents just one third of the budget but accounts for 39 % of all

⁹ Article 3(4) of Regulation (EU, Euratom) No 883/2013 of the European Parliament and of the Council of 11 September 2013 concerning investigations conducted by the European Anti-Fraud Office (OLAF) (OJ L 248, 18.9.2013, p. 1), as amended by Regulation (EU, Euratom) 2016/2030 of the European Parliament and of the Council of 26 October 2016 (OJ L 317, 23.11.2016, p. 1).

¹⁰ Guidance note on main tasks and responsibilities of an Anti-Fraud Coordination Service (AFCOS), 13 November 2013, Ares (2013) 3403880.

¹¹ The abbreviation PIF comes from the French '*protection des intérêts financiers*' and generally refers to the protection of the EU's financial interests.

¹² Article 17(1) of Directive 2017/1371.

¹³ COM(2018) 553 final of 3 September 2018.

reported fraud cases and 72 % of the total financial amounts involved in these cases (see [Figure 2](#)).

Figure 2 – Irregularities reported as fraudulent by policy area (2013-2017)

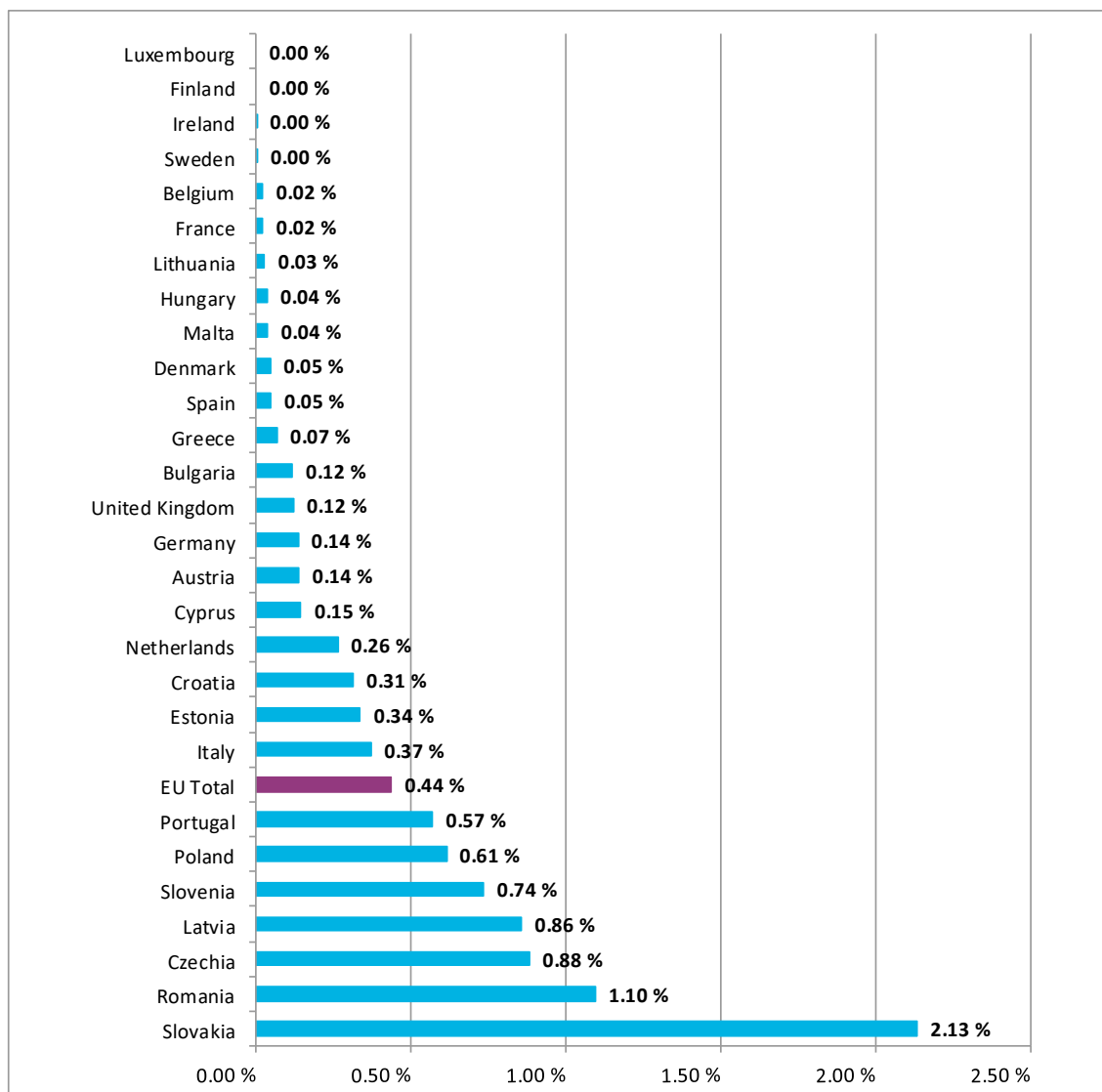
Policy area	Irregularities reported as fraudulent		Financial amounts involved	
	<i>(number)</i>	<i>(percentage)</i>	<i>(million euro)</i>	<i>(percentage)</i>
Common agricultural policy	2 081	50 %	350.9	24 %
Cohesion and fisheries policies				
- Fisheries part	64	2 %	20.1	1 %
- Agricultural part (pre-2007)	24	1 %	3.4	0 %
- Cohesion part	1 645	39 %	1 063.6	72 %
Pre-accession policy	133	3 %	28.8	2 %
Direct management	206	5 %	21.5	1 %
TOTAL (Expenditure part)	4 153	100 %	1 488.3	100 %

Source: 2017 PIF report - Statistical Annex Part II (Expenditure)

10 According to the data supporting the 2017 PIF report, irregularities reported as fraudulent by Member States represent 0.44 % of the EU funds paid in the field of cohesion policy. This indicator is known as the fraud detection rate¹⁴ and varies widely by Member State (see [Figure 3](#)), ranging from 0 % to 2.1 % in relation to EU cohesion funding for the whole 2007-2013 programming period. The 2017 PIF report does not provide any specific explanation regarding the significantly higher fraud detection rate reported for Slovakia. The average individual value of the irregularities as fraudulent amounts to €0.8 million.

¹⁴ Statistical annex to the 2017 PIF report, page 93. The FDR is the ratio between the amounts involved in cases reported as fraudulent and the payments made in the 2007-2013 programming period (page 91). This indicator does not include undetected or unreported fraud.

Figure 3 – Fraud detected and reported as a percentage of cohesion policy funds received by EU Member States in the 2007-2013 programming period



N.B. The calculation of the fraud detection rate represented in this figure excludes irregularities concerning fisheries policy (which are included in the statistics published by the Commission under cohesion and fisheries policies and which do not increase the fraud detection rate for the EU Total. This figure also excludes the multi-country European Territorial Cooperation (ETC) programmes. However, these programmes are considered for the calculation of the EU average in the figure. As regards the Member States presenting a zero FDR, Finland and Luxembourg reported no fraudulent irregularities, while Ireland and Sweden reported some irregularities with a low financial value.

Source: ECA, based on 2017 PIF report, Statistical annex, page 93.

11 We considered it necessary to assess the work carried out by managing authorities, as they are in the front line of the fight against fraud in EU cohesion policy. According to the Commission¹⁵, the combination of a thorough risk assessment leading to adequate preventive and detective measures by managing authorities, on the one hand, and coordinated and timely investigations by competent bodies (usually the police or prosecutors), on the other hand, could significantly reduce fraud risk in the field of cohesion policy and provide suitable deterrence against fraud. This audit was structured around these two broad areas.

¹⁵ Commission's guidance for Member States and programme authorities on fraud risk assessment and effective and proportionate anti-fraud measures, page 11 (EGESIF 14-0021 of 16 June 2014).

Audit scope and approach

12 We decided to audit the work of managing authorities in fighting fraud in cohesion policy because of the key role they play, and will continue to play in the 2021-2027 programming period. We assessed whether managing authorities have properly fulfilled their responsibilities at each stage of the anti-fraud management process: fraud prevention, fraud detection and fraud response (including reporting on fraud and recovery of funds unduly paid). To this end, we assessed whether managing authorities have:

- (a) developed anti-fraud policies, performed a thorough risk assessment and implemented adequate preventive and detective measures; and
- (b) properly responded to detected fraud in coordination with the investigation and prosecution bodies and with AFCOSs, considering the design of these services in the Member States we visited.

13 We looked at the role played by managing authorities and AFCOSs in the Member States in cohesion policy. We audited the managing authorities for the operational programmes funded by the three main European Structural and Investment Funds concerning EU cohesion policy: the CF, the ESF and the ERDF. We decided to exclude the European Territorial Cooperation objective (ETC) of the ERDF, as the projects financed by the corresponding OPs involve partners from different countries under the supervision of authorities in different Member States.

14 We reviewed how managing authorities had considered the Member States' legal and strategic anti-fraud framework for the management of the anti-fraud process, in particular when a national anti-fraud strategy was available. We invited all managing authorities to participate in a survey on fraud prevention and detection measures and obtained replies from authorities in 23 Member States.

15 We visited seven Member States: Bulgaria, France, Hungary, Greece, Latvia, Romania and Spain. For the selection of these Member States, we considered the fraud detection rates and the number of fraud cases presented in the 2016 PIF report, as well as their correlation with other available fraud risk indicators. During our visits, we met with representatives of the authorities responsible for implementing a total of 43 OPs (22 OPs for 2007-2013 and 21 OPs for 2014-2020) and with key actors in the fight against fraud (prosecution and judicial bodies, investigative bodies, anti-fraud agencies, competition authorities). In the Member States we visited we audited a

judgemental sample of OPs selected to be representative of all funds (ERDF, ESF and, where applicable, CF) and a range of intervention types.

16 We reviewed the case files of a sample of 138 irregularities reported to the Commission as fraudulent from the 22 OPs we tested for 2007-2013. Wherever the size of the population allowed, we applied the random method known as monetary unit sampling to select the irregularities to be reviewed. We did not assess the work of investigation, prosecution and judicial bodies – although we did look at the managing authorities' coordination and communication with those bodies.

17 The findings in this report complement those in special report 01/2019: "Fighting fraud in EU spending: action needed", published on 10 January 2019, which covered the design and implementation of the Commission's Anti-Fraud Strategy. In that report, we mainly focused on the role of OLAF, but also looked at the work done on anti-fraud policies by the Commission DGs responsible for the implementation of EU cohesion policy (see paragraph [04](#)).

Observations

Anti-fraud policy, fraud prevention and detection measures

Managing authorities generally have no specific anti-fraud policy

18 The Commission has provided guidelines for Member States and managing authorities to help them comply with their legal obligation to put in place anti-fraud measures that are proportionate and effective.

- At the level of the Member States, the Commission recommends the adoption of national anti-fraud strategies for the protection of the ESI Funds, with the objective of ensuring homogenous and effective implementation of anti-fraud measures, especially where Member States' organisational structures are decentralised.
- At the level of operational programmes, the Commission recommends that managing authorities develop a structured approach to tackling fraud, organised around the four key elements in the anti-fraud management process: prevention, detection, correction and prosecution¹⁶.
- The Commission has further defined concrete criteria for evaluating the way managing authorities have complied with their legal obligations for setting up proportionate and effective anti-fraud measures¹⁷.

¹⁶ Commission's Guidance for Member States and programme authorities on fraud risk assessment and effective and proportionate anti-fraud measures (EGESIF 14-0021 of 16 June 2014), OLAF's Handbook on the role of Member State auditors in fraud prevention and detection (October 2014) and Guidance on a common methodology for the assessment of management and control systems in the Member States (EGESIF 14-0010-final of 18 December 2014).

¹⁷ Article 30 and Annex IV of Commission Delegated Regulation (EU) No 480/2014 of 3 March 2014 supplementing Regulation (EU) No 1303/2013 of the European Parliament and of the Council (OJ L 138, 13.5.2014, p. 5) and defining key requirements of management and control systems and their classification with regard to their effective functioning - specifically key requirement 7 (effective implementation of proportionate anti-fraud measures).

19 The Commission recommends that managing authorities use a formal anti-fraud policy¹⁸ to communicate their determination to combat and address fraud. This policy should, in particular, include strategies for the development of an anti-fraud culture and the allocation of responsibilities for tackling fraud. We consider that managing authorities should have prepared a formal anti-fraud policy or a similar single, stand-alone document specifying their fraud prevention, detection and response measures and making clear to their own staff, the beneficiaries of EU funding and other authorities that measures to tackle fraud are in place and being implemented.

20 We found during our visits that very few of these policies actually constitute formal reference documents summarising the measures to be implemented at each stage of the anti-fraud management process in response to identified fraud risks. We only found examples of formalised anti-fraud policies in Latvia, at specific intermediate bodies in Spain, and in France (where the policy has not been made public). In all other cases, to obtain a full description of anti-fraud measures we needed to consult multiple management documents and manuals of procedures. We consider that the absence of formalised anti-fraud policies limits Member States' ability to supervise and coordinate anti-fraud measures and evaluate their effectiveness. This is particularly relevant in that only ten Member States have adopted a national anti-fraud strategy¹⁹ based on the Commission's recommendation (see paragraph 18).

21 We also consider the absence of provisions requiring managing authorities to adopt formal anti-fraud policies as a shortcoming in the design of the anti-fraud framework for 2014-2020. Furthermore, Commission Delegated Regulation (EU) No 480/2014 (complementing the CPR for 2014-2020) does not mention shortcomings

¹⁸ In this sense, the concept of a formal anti-fraud policy corresponds to the 'fraud risk management programme' defined by the Association of Certified Fraud Examiners (ACFE) in its "Fraud examiners manual" or in the "Fraud Risk Management Guide" it developed with the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and to the "formal counter fraud and corruption strategies" defined by the Chartered Institute of Public Finance and Accountancy (CIPFA) in its "Code of practice on managing the risk of fraud and corruption".

¹⁹ National anti-fraud strategies exist in ten of the 28 Member States: Bulgaria, Czechia, Greece, France, Croatia, Italy, Latvia, Hungary, Malta and Slovakia. Romania also has a strategy, but it is now out-of-date (Source: 2017 PIF report, page 12). The Member States that have not adopted a national strategy are: Belgium, Denmark, Germany, Estonia, Ireland, Spain, Cyprus, Lithuania, Luxembourg, Netherlands, Austria, Poland, Portugal, Slovenia, Finland, Sweden and United Kingdom.

in the implementation of proportionate and effective anti-fraud measures in the context of determining ‘serious deficiencies’ that could lead on their own to the suspension of payments to or the financial correction of operational programmes²⁰. As a result, the use of anti-fraud measures is given less weight than other areas in the assessment of management and control systems. The Commission’s proposal for the CPR for 2021-2027 does not consider anti-fraud measures as one of the enabling conditions²¹ which Member States must meet before they can obtain EU cohesion funding.

Managing authorities systematically assess fraud risks, but this process could be further improved

Managing authorities systematically identify fraud risks

22 The most significant change compared to the 2007-2013 programming period is that managing authorities now have to assess fraud risks in line with the requirements of the 2014-2020 control framework (see paragraph **05**). The purpose of this exercise is for managing authorities to determine the suitability of existing internal controls to address the risks associated with different fraud scenarios and identify areas where additional controls are necessary.

23 Among other anti-fraud topics, the EGESIF guidelines for Member States and managing authorities (see paragraph **18**) address the task of fraud risk assessment including a practical “ready-to-use” tool to perform the assessment²². All the managing authorities we visited in the context of our audit had complied with their obligation to perform a fraud risk assessment. This marks an improvement in the way these authorities approach the fight against fraud in Cohesion. In most cases, the authorities

²⁰ Article 30 and Annex IV.

²¹ Article 11 and Annex III of Commission’s proposal for a CPR for 2021-2027, COM(2018) 375 of 29 May 2018.

²² In the guidance document, the Commission developed a fraud risk assessment model based on 31 standard inherent risks, further subdivided into 40 risks and 128 recommended mitigating controls, all of them structured around four generic management processes (selection of applicants, implementation and verification of operations, certification and payments, and direct procurement by managing authorities). However, the document does not cover financial instruments or risks in relation to state aid.

applied the model fraud risk assessment developed by the Commission or their own adaptation of that model.

24 On 28 November 2018, the Commission published the results of a study²³ on the fraud and corruption prevention practices implemented by Member States in response to the specific provisions in place for the 2014-2020 programming period that it had outsourced in December 2016. The study concluded that the new legislative requirements, in particular as regards the fraud risk assessment process, had helped to make Member States' efforts to tackle fraud more formalised and systematic. However, the study also concluded that some authorities may underestimate their self-assessed levels of risk (see **Box 1**).

²³ DG REGIO – Preventing fraud and corruption in the European Structural and Investment Funds – taking stock of practices in the EU Member States, October 2018, available at: https://ec.europa.eu/regional_policy/en/information/publications/studies/2018/study-on-the-implementation-of-article-125-4-c-of-the-regulation-eu-no-1303-2013-laying-down-the-common-provisions-on-the-european-structural-and-investment-fund-in-member-states.

Box 1**Stock taking study on preventing fraud and corruption in the ESIFs**

The study was based on a sample of 50 2014-2020 OPs (41 of which related to Cohesion, excluding ETC) selected by the Commission on a judgemental basis to cover all Member States and a range of sectors and funds. The study team reviewed information from Member States (in particular the outcome of their fraud risk assessments) and conducted interviews with programme authorities and AFCOSs.

The study focused on the design of fraud prevention measures and (to a lesser extent) fraud detection methods and assessed how proportionated the measures were to the identified risks. However, it did not address the manner in which the fraud risk assessment had been conducted. The study did not conclude on the effectiveness of the measures put in place, either.

The key lessons drawn from the study can be summarized as follows:

Positive remarks	Areas for improvement
Anti-fraud and anti-corruption efforts are more formalised and systematic in the 2014-2020 programming period.	Proportionateness of mitigating measures is lowest for the risks of collusive bidding and double funding.
Mitigating measures are generally proportionate to the self-assessed risks.	Some authorities may underestimate their self-assessed levels of fraud risk.
Most authorities are using the Commission`s fraud risk assessment template.	Not all managing authorities conduct a fraud risk assessment at OP level.
A more inclusive fraud risk assessment process is better suited to reducing fraud risks.	There is a need for more communication to Member State authorities on anti-fraud activities.
	In its current form, the managing authorities in the sample perceive Arachne as not entirely meeting their needs.

There are some areas for further improvement

25 However, we note that some of the managing authorities we visited take a mechanical approach to the assessment of fraud risks, suggesting that they favour form over substance.

26 In addition, they generally base the identification of fraud risks on their own experience, without any additional input from other knowledgeable actors (anti-fraud coordination services, investigative and prosecution bodies or other specialised expert agencies).

27 During our Member State visits, we found indications that several managing authorities and intermediate bodies might have inadequately evaluated fraud risks:

- In Bulgaria, the audit authority had already detected that some managing authorities had incorrectly classified specific fraud risks as low and therefore failed to address them through additional control procedures.
- In France, the managing authorities we visited had not assessed the impact of additional controls on the residual risk of fraud.
- In Spain, where the responsibility for fraud risk assessment is partly delegated to intermediate bodies, an independent evaluation mandated by the managing authority detected coherence problems between identified risks and planned controls (e.g. certain risks not covered by an action plan or controls set up in areas marked as not applicable).
- In one of the OPs audited in Romania, intermediate bodies dealing with similar delegated functions and funding provided different fraud risk assessments.
- In Hungary, we found that the fraud risk assessment was insufficiently comprehensive (it excluded previous audit results) and did not identify risks specifically associated with the types of operations and beneficiaries covered by the OPs.

28 In nearly all cases the managing authorities concluded that existing anti-fraud measures address the identified fraud risks. Given the shortcomings identified, we consider that this conclusion may be too optimistic.

Managing authorities have improved their fraud prevention measures but made no significant progress towards proactive fraud detection











29 Managing authorities are expected to develop effective and proportionate fraud prevention and detection measures in response to identified risks, in such a way that the opportunity to commit fraud is substantially reduced.

Managing authorities have developed specific fraud prevention measures for 2014-2020

30 We found that the additional anti-fraud measures developed for the 2014-2020 period largely focus on preventive actions, which are more comprehensive than those set up for 2007-2013. Our survey showed that such additional preventive measures mainly comprise fraud-awareness training for staff, policies on conflicts of interest and ethical guidance for employees and beneficiaries, and the publication of high-level institutional anti-fraud statements or declarations.

31 Our survey also showed that managing authorities consider fraud-awareness measures (both staff training and measures targeting intermediate bodies and project beneficiaries), policies on conflicts of interest and codes of conduct to be the most effective way of preventing fraud in the use of EU Cohesion funding (see [Figure 4](#)). Other fraud prevention measures, such as employee support programmes (aimed at reducing pressure on employees exposed to fraud) and bounty schemes (whereby managing authorities make public their intention to reward whistleblowers of fraud), remain infrequent, although they are considered reasonably effective.

Figure 4 – Fraud prevention measures implemented by managing authorities and their perceived effectiveness

Percentage of MAs declaring they have the following fraud prevention measures			Percentage of MAs perceiving the measure as effective	
1	Anti-fraud training for staff	86 %		92 %
2	Formal policy on conflicts of interest	83 %		91 %
3	Adoption of a code of conduct for employees	73 %		88 %
4	Publication of an anti-fraud policy	71 %		82 %
5	Fraud risk-awareness measures for project beneficiaries	57 %		90 %
6	Fraud risk-awareness measures for intermediate bodies	54 %		92 %
7	Background checks on employees	29 %		75 %
8	Employee support programmes	20 %		86 %
9	Other	13 %		89 %
10	Reward / Bounty schemes	4 %		67 %

Source: ECA survey of managing authorities

32 Several Member States have taken a more innovative approach to preventing fraud against the EU's financial interests, such as by involving civil society organisations in monitoring the execution of public contracts or running campaigns questioning the social acceptability of certain fraudulent practices (see **Box 2**).

Box 2

Innovative fraud prevention measures

Integrity pacts

In 2015 the European Commission and Transparency International, a global non-governmental organisation actively fighting corruption and particularly known for its publication of the Corruption Perception Index (CPI), launched a pilot project on 'integrity pacts' as an innovative way of preventing fraud in EU cohesion policy projects. An integrity pact is an agreement in which the authority responsible for awarding a public contract and the economic operators bidding for the contract undertake to abstain from corrupt practices and ensure transparency in the procurement process. Pacts also include a separate agreement engaging a civil society organisation (such as an NGO, a foundation or a local community-based organisation) to monitor all parties' compliance with their commitments. The purpose of integrity pacts is to increase transparency, accountability and good governance in public contracting, enhance trust in public authorities and promote cost efficiency and savings through better procurement. The second phase of the project began in 2016 and will run for four years²⁴. We discussed the use of integrity pacts with civil society organisations in Latvia, Romania and Hungary, which were generally positive about the initiative.

"FRAUD OFF!" campaign









In March 2017, the Latvian AFCOS launched an awareness-raising campaign called "FRAUD OFF!" questioning the social acceptability of certain types of fraudulent behaviour. National TV channels ran campaign advertisements featuring national celebrities, and publicity material was distributed to institutions, businesses, shops and the population in general. The campaign reached a significant audience and trended heavily for a while.

²⁴ More information on integrity pacts can be found on the Commission website at http://ec.europa.eu/regional_policy/en/policy/how/improving-investment/integrity-pacts/.

Fraud detection measures for 2014-2020 remain largely the same as for 2007-2013

33 While the compulsory fraud risk assessment has meant a greater focus on fraud prevention, managing authorities have developed very few additional fraud detection methods for the 2014-2020 programming period. They rely instead on the internal controls and procedures that were already in place for 2007-2013 under a weaker control framework (see [Figure 5](#)). These are mainly on-the-spot checks (audits), internal fraud reporting mechanisms and, to a lesser extent, the identification of specific fraud indicators²⁵ (red flags). Both through the survey and during our visits to Member States, we found very few additional 'proactive' controls to detect fraud (e.g. specific checks for collusion in public procurement, such as the semantic analysis of bids received or the identification of abnormal bidding patterns).

Figure 5 – Fraud detection measures implemented by managing authorities and their perceived effectiveness

Percentage of MAs declaring they have the following fraud detection measures			Percentage of MAs perceiving the measure as effective	
1	On-the-spot checks / audits	87 %		95 %
2	Internal fraud-reporting mechanisms	86 %		87 %
3	Identification of fraud indicators / red flags	69 %		79 %
4	Fraud risk assessment on project beneficiaries	60 %		83 %
5	Arachne risk-scoring tool	49 %		71 %
6	Data analytics / data-mining techniques	46 %		91 %
7	Fraud hotline for whistleblowers	44 %		74 %
8	Other	21 %		80 %

Source: ECA survey of managing authorities

²⁵ Based on those made available by the Commission in its information note of 18 February 2009 on fraud indicators for ERDF, ESF and CF.

Practical problems limit the usefulness of fraud hotlines for whistleblowers

34 Our survey showed that managing authorities make little use of fraud hotlines for whistleblowers, even though they generally consider this tool to be an effective fraud detection method. Fraud hotlines and other whistleblowing mechanisms allow managing authorities (and other relevant Member State authorities) to become aware of potential fraud that other controls have failed to detect²⁶. Various studies show that these methods are regarded as the most important source of fraud reports²⁷. During our visits, we assessed whistleblowing mechanisms and found a number of practical problems with their use. For example, they are not always anonymous and there is a risk of insufficient awareness of them among project beneficiaries and the general public. In the event of regulatory limitations on the use of anonymous denunciation channels, managing authorities and AFCOSs can always redirect anonymous whistleblowers to the fraud notification system put in place by OLAF²⁸.

35 On 23 April 2018 the Commission proposed a Directive on the protection of whistleblowers. This aimed to unify the different approaches currently applied by Member States and to increase the level of protection for people reporting on breaches of Union law, including all breaches affecting the EU's financial interests. In our opinion on the proposal, issued on 15 October 2018, we stated our view that the introduction or expansion of whistleblowing arrangements in all Member States would help improve the management of EU policies through the actions of citizens and employees. However, we also highlighted some areas of concern, such as the overly complex material scope of the proposal, which could reduce the legal certainty for potential whistleblowers and thus deter them from reporting. Other issues we raised were the lack of clear obligations regarding awareness-raising and staff training, and our conviction that people who have reported anonymously should not be denied

²⁶ It is in the very nature of fraud against EU cohesion policy funds that perpetrators identify the limitations of existing controls and attempt to exploit them in order to obtain direct or indirect unlawful gains.

²⁷ In particular 'Report to the Nations', the 2018 global study on occupational fraud and abuse published by the Association of Certified Fraud Examiners (ACFE). According to this study, fraud is mainly detected through tip-offs, whether from employees, customers, competitors or anonymous sources.

²⁸ The "Report fraud" tool at https://ec.europa.eu/anti-fraud/olaf-and-you/report-fraud_en.

whistleblower protection if their identity is subsequently revealed²⁹. In relation to the adoption of this Directive, the European Parliament and the Member States reached on 12 March 2019 a provisional agreement on the new rules that would guarantee protection for whistleblowers who report breaches of EU law³⁰.

Data analytics is under-used for fraud detection

36 The Commission encourages managing authorities to use data analytics proactively to detect potentially high-risk situations, identify red flags and refine the aim of measures to combat fraud. Data analytics should be a systematic part of project selection, management verifications and audits³¹. In the framework of the fight against fraud, the Commission offers a specific data-mining tool (Arachne) to help managing authorities identify projects that might be subject to risks of fraud. According to the information we received from the Commission, in December 2018 Arachne was being used by 21 Member States for 165 OPs representing 54 % of all EU cohesion funding for 2014-2020 (excluding ETC). In our special report 01/2019: “Fighting fraud in EU spending: action needed”, we highlighted the importance of Arachne as a fraud prevention tool. We have now assessed Arachne’s role as a data analytics tool for fraud detection.

37 One of the most significant observations arising from our audit work is that managing authorities do not sufficiently use data analytics for fraud detection. Our survey showed that only one in every two managing authorities uses data analytics tools in this way (see [Figure 5](#)). Arachne in particular is under-used. In the Member States we visited we found that:

- o One Member State (Greece) has not provided any information as to whether or not Arachne will be introduced in the near future. However, the Greek managing authorities have not adopted an equivalent data analytics tool which could be used for all OPs in the country.

²⁹ Paragraphs 3, 12, 21, 23 and 32 of ECA Opinion No 4/2018 concerning the proposal for a Directive of the European Parliament and of the Council on the protection of persons reporting on breaches of Union law.

³⁰ See Commission’s press release IP/19/1604 “European Commission welcomes provisional agreement to better protect whistleblowers across the EU” (http://europa.eu/rapid/press-release_IP-19-1604_en.htm).

³¹ Commission’s guidance for Member States and programme authorities on fraud risk assessment and effective and proportionate anti-fraud measures (EGESIF 14-0021).

- o In four of the remaining six Member States, even where they have decided to use Arachne the managing authorities have made little progress on uploading the necessary operational data or using the tool for their internal controls.
- o The Arachne Charter allows access only to managing authorities, certifying authorities and audit authorities. Thus, Arachne cannot be automatically used by investigative bodies.

We also found that, in two of the Member States we visited, managing authorities which have fully incorporated Arachne into their management procedures have used the tool to help them to adapt their specific anti-fraud measures to high-risk beneficiaries.

38 We did not obtain any convincing explanation as to why managing authorities were not making full use of the tool, which the Commission makes available free of charge. However, the Commission’s own November 2018 study (see paragraph [24](#) and [Box 1](#)) concluded that managing authorities consider that, its current form, Arachne does not entirely meet their needs. The authors of the study found this particularly worrying, as the usefulness of Arachne is largely perceived to depend on the number of OPs feeding information into the tool³².

39 Nevertheless, during our visits we were able to identify some examples of good practice where Member State authorities had developed data analytics tools to help with the identification of potential fraud risks (see [Box 3](#)).

³² Page 51 of DG REGIO’s study “Preventing fraud and corruption in the European Structural and Investment Funds – taking stock of practices in the EU Member States”.

Box 3**Good practices in data analytics by Member States**

We identified the following data analytics tools that are used directly to detect potential fraud in the use of EU Cohesion funding:

- In Romania, the National Integrity Agency has developed an IT system ('PREVENT') that compares the public procurement information provided by contracting authorities and bidders with information from other national databases (e.g. the trade register). Use of the system in connection with 839 public procurement procedures financed by the EU enabled the Agency to issue 42 integrity warnings for correction or investigation.
- In Spain, the intermediate body responsible for implementing a large part of the OP 'Comunidad Valenciana', in cooperation with higher education institutions, has developed a rapid alert IT system ('SALER') combining four separate national and regional databases in order to identify fraud risks. Implementation of this tool is ongoing.

Managing authorities lack procedures for monitoring and evaluating fraud prevention and detection measures

40 The Commission encourages Member States and managing authorities to define procedures for monitoring the implementation of fraud prevention and detection measures. These should include specific arrangements for reporting what anti-fraud measures have been set up and how they are applied. Member States and managing authorities should use the results of monitoring to evaluate the measures' effectiveness and rework their anti-fraud strategies and policies as necessary.

41 Except in Latvia, we found that none of the managing authorities we visited examines the effectiveness of fraud prevention and detection measures. They keep limited records of which measures are used and seldom link them to specific results. Consequently, anti-fraud systems are not evaluated in terms of their actual results – either by managing authorities or by any other programme authority (e.g. the audit authority) or the AFCOS.

Similar levels of fraud reported for the 2007-2013 and 2014-2020 programming periods

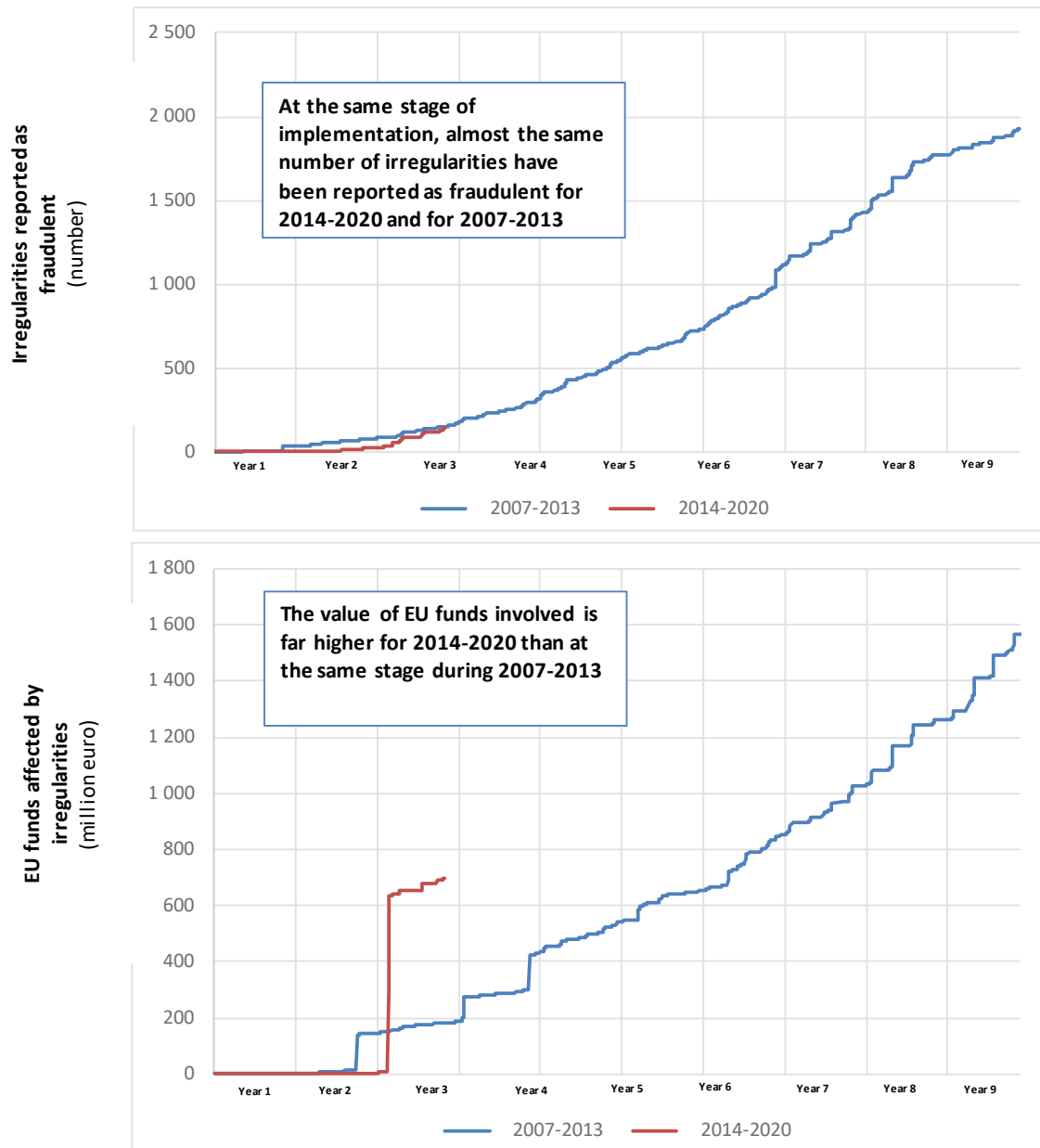
42 Managing authorities and other Member State bodies report fraudulent and non-fraudulent irregularities to the Commission through the IMS. As of December 2018, Member States (mainly managing and audit authorities) had reported a total of 1 925

and 155 irregularities as fraudulent, respectively, for the 2007-2013 and 2014-2020 programming periods. These concerned suspected and established fraud cases potentially affecting €1.6 billion (2007-2013) and €0.7 billion (2014-2020) in EU funds.

43 *Figure 6* charts the evolution in the number and value of irregularities reported in the IMS for the 2007-2013 and 2014-2020 programming periods. So far, 155 irregularities have been reported as fraudulent for 2014-2020 – 10 % fewer than at the same stage in the 2007-2013 period (174). In financial terms the situation is rather different: the potential impact of reported fraud on EU cohesion policy funds in the 2014-2020 programming period (€0.7 billion) is more than three times higher than at the same stage of the previous period (€0.2 billion). However, this significant increase is the result of two separate cases of suspected fraud that we consider to be data outliers³³.

³³ The two irregularities were reported by Slovakia and are worth close to €0.6 billion. By definition, they are at an early stage in the fraud management process and may yet evolve significantly.

Figure 6 – Evolution of irregularities reported as fraudulent



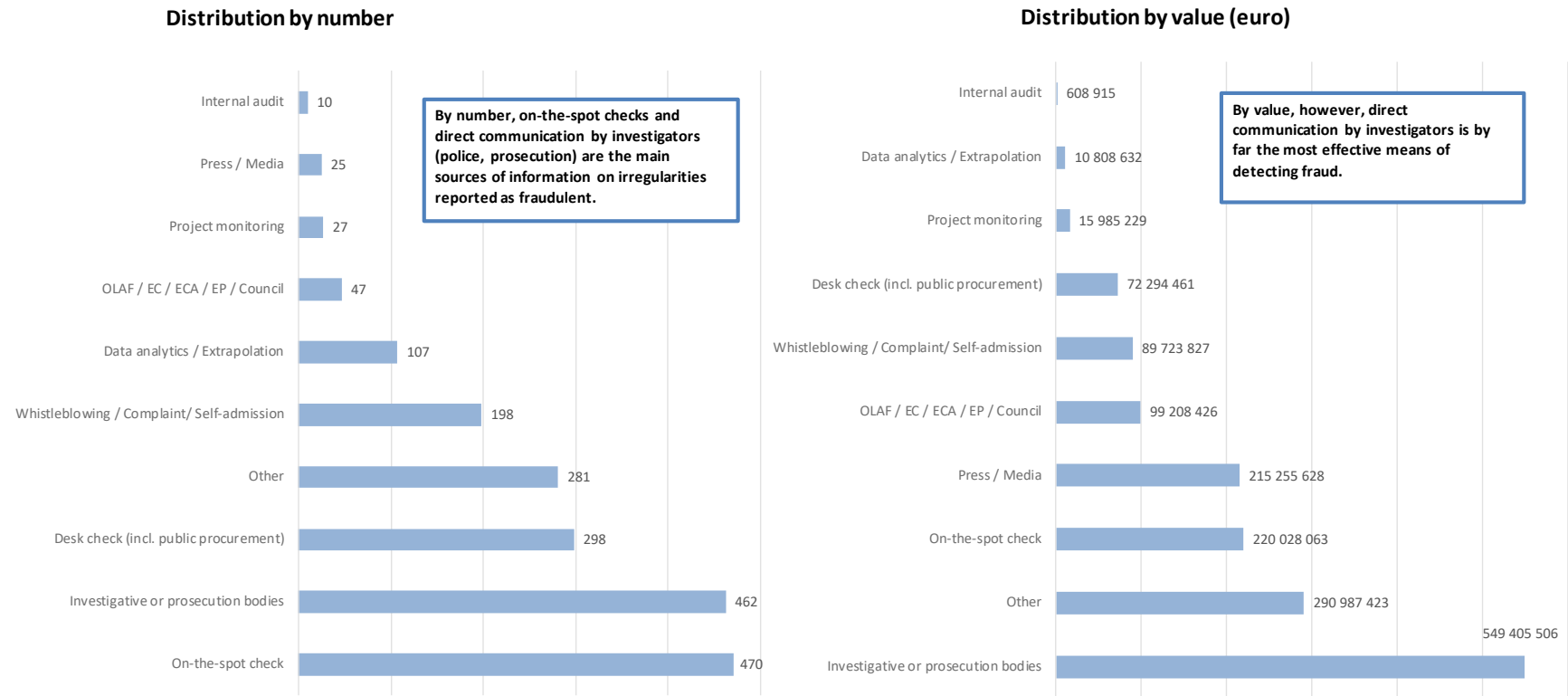
Source: ECA, based on IMS data

Most fraud cases reported to the Commission are detected through on-the-spot checks or revealed by investigative and prosecution bodies or the media

44 The IMS contains a number of data fields that are to be used to characterise irregularities and indicate the status of any proceedings. One of these fields is headed 'source of the information leading to a suspicion of an irregularity', which represents the method of detection. Based on the data recorded in the IMS up to and including December 2018, we analysed the sources of information leading to the reporting of irregularities as fraudulent for the 2007-2013 programming period (see [Figure 7](#)). We did not assess the data for 2014-2020 because it is still very incomplete and contains outliers (see paragraph [43](#)).

45 By number, most irregularities were detected by means of on-the-spot checks by programme authorities (see paragraph [04](#)), followed by reports from investigative or prosecution bodies. This would suggest that these are the most effective means of detecting fraud in the use of Cohesion funding. However, the statistics are influenced by the generalised use of audits as a fraud detection method (see paragraph [33](#) and [Figure 5](#)). By value, the bulk of reports of fraudulent irregularities resulted from cases opened directly by investigative and prosecution bodies, or from revelations in the press and other media. We consider that the statistics on the sources of information on fraud by value are strongly affected by uncertainty about the true amounts concerned, although less so when the information comes from an investigative or prosecution body.

Figure 7 – Irregularities reported as fraudulent for 2007-2013 in the field of Cohesion by information source



Source: ECA, based on IMS data

Fraud response, investigation and coordination among the relevant bodies

46 The Commission requires managing authorities to develop effective fraud response measures. These should include clear mechanisms for reporting suspected fraud and clear procedures for referring cases to the competent investigation and prosecution authorities. There should also be procedures for following up suspected fraud and, where necessary, recovering EU funds. Managing authorities should work with their AFCOSs, and there is a need for adequate coordination among all administrative and law enforcement bodies.

Managing authorities' under-reporting has affected the reliability of the fraud detection rates published in PIF reports

47 Member States must use the IMS to notify the Commission of irregularities exceeding €10 000 that cause them to suspect or establish fraud³⁴. Member States must report suspected or established fraud cases even if they have been resolved before certification of the related expenditure to the Commission.

Not all potential fraud is reported as such in the IMS

48 *Figure 3* above presents the fraud detection rates for 2007-2013 in EU cohesion policy. These are based on IMS data and were published in the 2017 PIF report. In special report 01/2019, we stated that the PIF report data on detected fraud was incomplete³⁵. Our work for this audit confirmed that assessment. We also detected several cases that raised questions about the completeness and reliability of the fraud data in the IMS and therefore limit the use that the Commission and Member States can make of the system.

49 We found that not all Member States interpret the EU definition of fraud in the same way (see paragraph **01**). For instance, cartel offences (bid rigging) are not always

³⁴ Article 122(2) of the CPR; Articles 3 and 4 of Commission Delegated Regulation (EU) 2015/1970 supplementing Regulation (EU) No 1303/2013 of the European Parliament and of the Council with specific provisions on the reporting of irregularities (OJ L 293, 10.11.2015, p. 1); Article 28(2) of Commission Regulation (EC) No 1828/2006 (rules for implementation).

³⁵ ECA special report 01/2019: "Fighting fraud in EU spending: action needed", paragraphs 21 to 32.

reported as fraudulent in Spain but other Member States, such as Latvia, systematically report them.

50 We came across cases where irregularities giving clear indications of fraud were not properly reported to the Commission because they had been detected and corrected before certification of the related expenditure to the Commission. However, Member States are supposed to report suspicions of fraud (as ‘attempted fraud’) even if there is ultimately no EU co-financing. In Hungary, the managing authorities do not report suspicions of fraud that are resolved prior to certification to the Commission. In Spain, the managing authority responsible for the ESF withheld payments as a precautionary measure, but without reporting to the Commission on the expenditure affected by cases of alleged fraud that had appeared in the press.

51 We found inconsistencies in the Member States’ use of administrative or legal acts to trigger reporting to the Commission. For instance, Romania does not systematically report ongoing investigations or decisions to prosecute in the IMS. As required by Romanian law, suspicions of fraud are only encoded when a managing authority, the audit authority, the AFCOS or OLAF issues an additional separate control/investigation report, even if an investigation is already ongoing or has been concluded. As a result, reporting in IMS is unduly delayed and some cases in the courts might be totally excluded from the system.

52 Finally, we also found that the Hungarian AFCOS has a large backlog of cases to be analysed prior to reporting in the IMS.

The IMS contains some inaccuracies and obsolete data

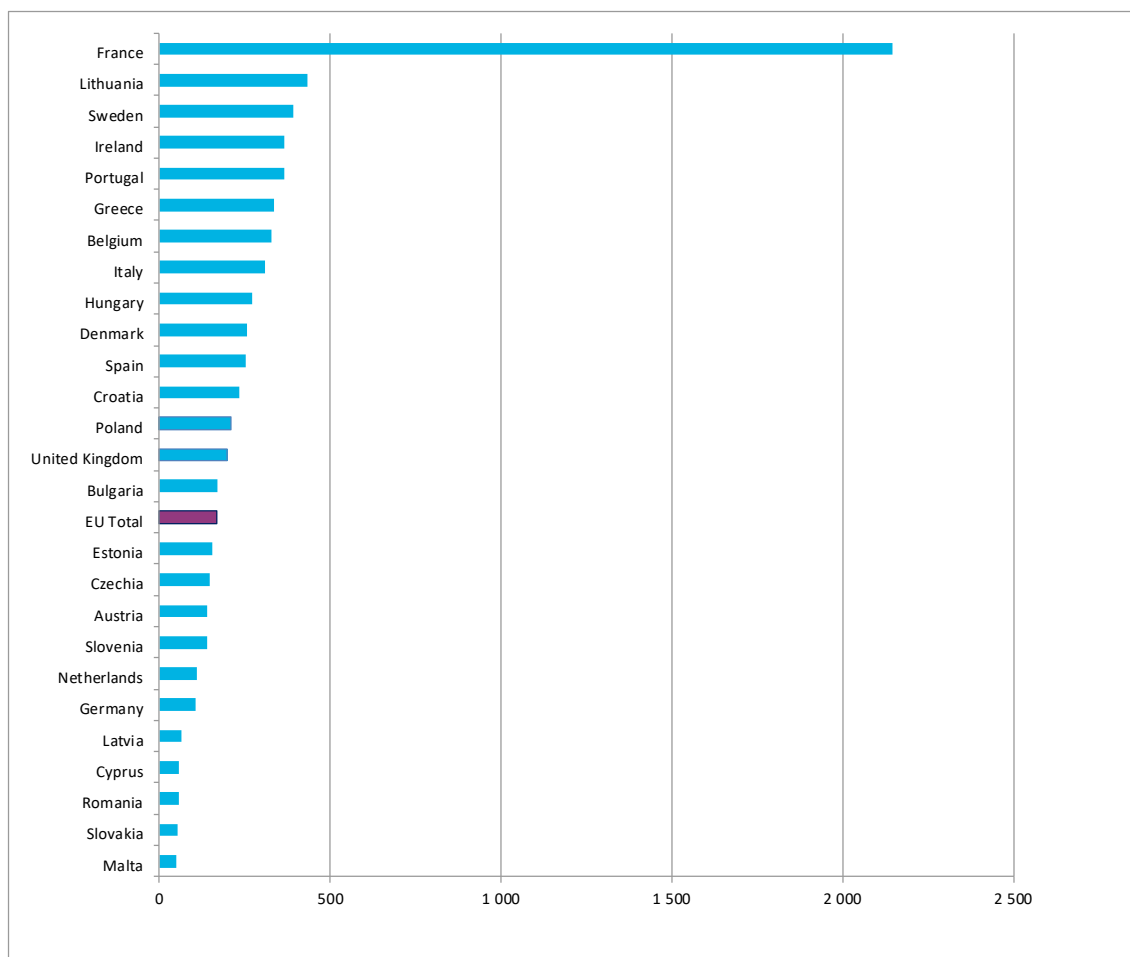
53 We found examples of inaccurate or obsolete data in the IMS, particularly in relation to the status of a case and the key dates in the sanctioning procedure. This could indicate that a managing authority, the data validator or AFCOS has not carefully checked data quality. While this situation is not satisfactory, it does not usually affect the number of fraud cases reported in IMS.

54 We identified inconsistencies in the approach taken by managing authorities to assess the financial impact of potential fraud. As a result, similar legal offences may be quantified differently in the IMS by different Member States. Most concerned are cases where it is difficult to state accurately how much expenditure is affected (e.g. conflicts of interest in project selection or public procurement infringements).

Under-reporting has affected the reliability of fraud detection rates

55 The 2017 PIF report gives fraud detection rates for each Member State and for the EU as a whole, based on the data reported in the IMS by Member States' authorities and AFCOSs (see paragraph 07). It does not provide a similar comparative indicator regarding the number of irregularities across the EU in the field of cohesion policy. To compute this figure, we compared the number of fraudulent irregularities reported by each Member State with the amount they had received in EU funds (see Figure 8). We found that France reports the fewest fraudulent irregularities for each euro it receives from the EU. In our view, France does not adequately report irregularities, including suspicions of fraud.

Figure 8 – Cohesion policy funds – EU funds received per irregularity reported as fraudulent - 2007-2013 programming period



Source: ECA, based on 2017 PIF report. This chart does not include Finland or Luxembourg, which reported no fraudulent irregularities for the period.

56 In our view, the fraud detection rates published by the Commission are actually fraud reporting rates: they do not necessarily reflect the effectiveness of Member States' detection mechanisms or even indicate how much fraud is actually detected, but rather show how many cases Member States have decided to report to the Commission (see paragraphs 48 to 52). In our special report 01/2019, we concluded that the correlation between fraud detection rates and other corruption risk indicators is weak³⁶.

57 In the light of the problems we identified, we consider that the fraud detection rate published in the 2017 PIF report for cohesion policy does not give a true representation of the incidence of fraud in the Member States we visited.

Several managing authorities fail to systematically communicate suspicions of fraud to investigation or prosecution bodies

58 A key part of reducing fraud risk and heightening fraud deterrence is for competent judicial bodies (police, prosecutors and others) to investigate reports of fraud in a coordinated and timely manner. Although this audit did not cover the work of investigation and prosecution bodies, we did assess the way managing authorities communicate and coordinate with them.

59 Putting the principle of fraud deterrence into practice requires managing authorities (or any other authority detecting potential irregularities) promptly and systematically to communicate suspicions of fraud to the relevant investigative or prosecution bodies, which are the only ones capable of determining intent. In several cases we found that managing authorities failed to systematically report suspected fraud to the bodies charged with investigation. In Greece, for instance, the managing authorities had not referred any of the suspicions of fraud sampled for our audit to the prosecution services. In Spain we found no specific instructions or procedures requiring managing authorities to report all suspected fraud in this way. Failure to communicate suspicions of fraud severely limits the deterrent effect of possible investigation and prosecution.

60 Investigators and prosecutors regularly turn down requests to open criminal investigation of cases referred to them by managing authorities. This is quite normal, as only these specialised services have the legal capacity and investigative resources to establish whether a criminal act may have taken place. However, managing authorities

³⁶ Special report 01/2019: "Fighting fraud in EU spending: action needed", paragraph 29.

should always analyse the reasons for a rejection and, where possible and appropriate, amend their operational procedures. We found that only Latvia has made arrangements to analyse why referred cases are rejected and take the necessary action.

Corrective measures have a limited deterrent effect

61 Managing authorities are expected to recover EU funds that are spent fraudulently³⁷. They are also charged with making a thorough and critical review of any internal control systems that may have exposed them to potential or proven fraud.

62 The most common corrective measure is to withdraw affected expenditure from the declarations made to the Commission, but without recovering funds from the perpetrator of fraud or imposing any type of additional deterrent action such as a sanction or penalty. There is nothing unusual about this procedure, as in most of the cases we reviewed the actual occurrence of fraud had not yet been established. According to the IMS, however, Member State authorities had initiated the recovery of EU funds in only 84 out of 159 cases of established fraud³⁸. Withdrawing expenditure from declarations to the Commission is an effective way of protecting the EU's financial interests. However, this protection does not extend to national public funding – i.e. Member States' budgets are still affected if there is no recovery – which places limits on the deterrent effect of corrective action taken by managing authorities. Our special report 01/2019 provides additional information on the recovery of funds related to established fraud cases³⁹.

63 As well as recovering any EU funds affected by fraud, managing authorities are expected to assess the horizontal implications for their management and control systems and other projects (e.g. same beneficiary or similar signs of fraud).

64 Of the seven Member States we visited, we only found evidence of this kind of assessment in Spain (see [Box 4](#)). However, even there, verification is not systematic.

³⁷ Annex IV of Commission Delegated Regulation (EU) No 480/2014 of 3 March 2014 supplementing Regulation (EU) No 1303/2013.

³⁸ The amount to be recovered in relation to these 84 fraud cases was €7 million.

³⁹ Special report 01/2019: "Fighting fraud in EU spending: action needed", paragraphs 112 to 115.

Box 4

Example of good practice: checking for systematic fraud based on an initial case

Most individual suspicions of fraud reported by Spain in relation to the 2007-2013 programming period can be traced to a single investigation triggered by an intermediate body.

Based on the preliminary conclusions of an initial verification, the intermediate body made horizontal checks of all other grants awarded to the same final beneficiary. It concluded that there was enough evidence to suspect systematic fraud involving false invoicing and collusion with external suppliers.

The intermediate body duly reported the results of its checks and its suspicions of fraud to the Spanish prosecutors and to the Commission. The investigation currently covers 73 % of all the cases of suspected fraud reported in Spain for the 2007-2013 programming period and 56 % of their estimated potential impact on the EU contribution.

The fight against fraud is weakened by various management issues

It can take a long time to punish fraud

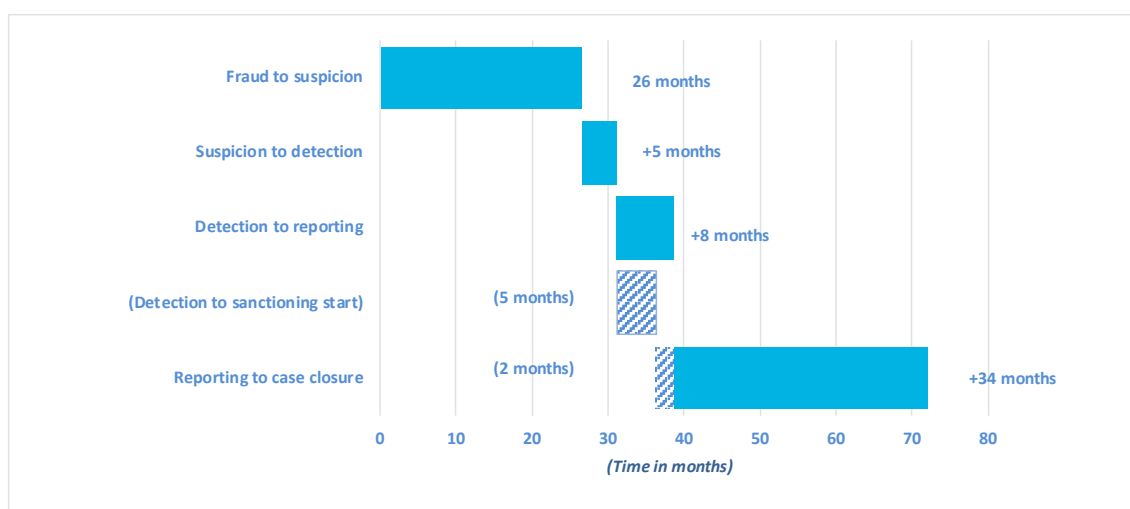
65 There may be a long time between the commission of fraud and the imposition of sanctions (see [Figure 9](#)). According to the data recorded in the IMS, on average suspicions of fraud are raised around two years after the perpetration of an irregularity⁴⁰. It can take another year to confirm those suspicions through a preliminary assessment leading to a primary administrative or judicial finding⁴¹ and to report the case to the Commission through the IMS. From this point onwards, the Commission is in a position to monitor the case and consider it for the purposes of the annual PIF report. Following the preliminary assessment (and in parallel to reporting to

⁴⁰ Calculated on the basis of the information recorded in the IMS. As already stated, this information is not always accurate.

⁴¹ A primary administrative or judicial finding (PACA) is the first written assessment by a competent authority concluding that an irregularity may be fraudulent, without prejudice to further assessment of the case. PACAs can come in a variety of forms, such as a management verification report by a managing authority or intermediate body, an audit report from the audit authority, the Commission or the ECA, or the indictment decision taken by a prosecutor or a judge to trigger a formal criminal investigation.

the Commission), it takes around five months to initiate any administrative or criminal proceedings with a view to imposing sanctions. These proceedings take three years on average to come to term.

Figure 9 – Average time taken for fraud to be detected, reported and closed by the competent Member State authorities



Source: ECA, based on information extracted from IMS

The functions of AFCOSs are insufficiently defined in the Regulation and vary considerably among Member States

66 Even though the main responsibility for fighting fraud in the use of Cohesion funding lies with the managing authorities, the AFCOSs play an essential role in coordinating the work of these authorities with other Member State bodies and with OLAF. The EU legislation establishing the AFCOSs⁴² does not provide guidance regarding their terms of reference, organisational framework or tasks. The Commission has provided specific recommendations in this respect through further guidance⁴³ (see paragraph 07). However, it is up to each Member State to make specific arrangements for its AFCOS.

⁴² Regulation (EU, Euratom) No 883/2013 of the European Parliament and of the Council of 11 September 2013 concerning investigations conducted by the European Anti-Fraud Office (OLAF) (OJ L 248, 18.9.2013, p. 1), as amended by Regulation (EU, Euratom) 2016/2030 of the European Parliament and of the Council of 26 October 2016 (OJ L 317, 23.11.2016, p. 1).

⁴³ Guidance note on main tasks and responsibilities of an Anti-Fraud Coordination Service (AFCOS), 13 November 2013, Ares (2013) 3403880.

67 The resources and organisational arrangements of AFCOSs should allow them to properly monitor fraud reporting and coordinate the work of all parties involved in the fight against fraud. In the absence of clear guidance, we found that the AFCOSs in the seven Member States we visited had significantly different structures and powers. They ranged from small departments without investigative authority to complex structures that are fully empowered to carry out administrative investigations (see [Figure 10](#)). The French AFCOS has the same number of staff as the Latvian AFCOS, despite the difference between the two countries in terms of size and volume of funds received.

Figure 10 – Overview of AFCOSs in the Member States we visited

Member States visited	AFCOS position in the national institutional system	Staff (full-time equivalent)	Investigative powers	Close follow-up of IMS cases	Public annual activity report	Coordination mechanisms involving external actors
LV	Ministry of Finance	1.5	No	Yes	Yes	Yes
FR	Ministry of Economy and Finance	1	No	No	Yes	No
BG	Ministry of Interior	30	Yes	No	Yes	Yes
RO	Working apparatus of the Government	131	Yes	Yes	Yes	Bilateral (with MAs, CA and AA)
GR	Ministry of Justice	35	No	No	Yes	Yes
ES	General State Comptroller (Ministry of Finance)	7	No	Yes	Yes	No
HU	Ministry of Economy (until 15 June 2018)/ Ministry of Finance (after 15 June 2018)	11	No	No	No	No

Source: ECA

68 The Hungarian AFCOS lacks proper arrangements for reporting on activities carried out by the Member State to protect the EU's financial interests. This AFCOS does not make public any reports on those activities or on potential fraud in EU Cohesion spending (see [Figure 10](#)).

69 On 23 May 2018, the Commission issued a proposal for amendments to the OLAF Regulation⁴⁴. Before putting forward the proposal, in 2017 the Commission had conducted an evaluation⁴⁵ of the way the OLAF Regulation was being applied. The

⁴⁴ Proposal for a Regulation of the European Parliament and of the Council amending Regulation (EU, Euratom) No 883/2013 concerning investigations conducted by the European Anti-Fraud Office (OLAF) as regards cooperation with the European Public Prosecutor's Office and the effectiveness of OLAF investigations, COM(2018) 338 final 2018/0170 (COD).

⁴⁵ Report from the Commission to the European Parliament and the Council on the evaluation of the application of Regulation (EU, Euratom) No 883/2013, SWD(2017) 332 final.

evaluation identified discrepancies in the way AFCOSs were set up in different Member States, and in their powers, as the main factor inhibiting their effectiveness.

70 On 22 November 2018, the Court gave its opinion on the proposal⁴⁶. Our view was that the proposal does not sufficiently contribute to the more harmonised and effective implementation of AFCOSs in all Member States, as it only addresses the services' cooperation with OLAF and fails to provide clarity as to their minimum functions.

The status of fraud cases is inadequately reported and followed up

71 In order to follow up the status of a case, it may be necessary to consult parties involved in the fight against fraud that are outside the OP management and control structures. We consider that, as the central structures liaising with OLAF in the fight against fraud, AFCOSs should have an overview at all times of cases of fraud involving EU funding. To do this, they should be able to obtain information on the status of cases investigated by the competent authorities in their Member States. In addition, they should have statistics on the number and progress of cases under investigation, with due regard to procedural confidentiality.

72 In five of the Member States we visited, the AFCOSs were insufficiently aware of the investigative status of cases reported to the Commission. In Romania and Hungary we found no formal mechanism for systematic cooperation between the managing authorities, the AFCOS and the investigative and prosecution bodies; thus the AFCOS had no full overview of ongoing investigations involving EU-funded projects. That said, the Romanian AFCOS periodically approaches the prosecution bodies for information on the status of ongoing investigations about which it is aware. In Spain, the AFCOS also takes a proactive approach by requesting data on ongoing investigations. In spite of this, it is unable to ensure that updated information is forwarded to the Commission.

73 We found coordination and information exchange issues in six of the seven Member States. We were also unable to reconcile the information recorded in the IMS regarding cases of suspected and confirmed fraud involving EU funding with that held by the various authorities. This finding raises questions about the reliability of the information reported to the Commission. The Member States concerned keep no

⁴⁶ Opinion No 8/2018 on the Commission's proposal of 23 May 2018 on amending Regulation 883/2013 as regards cooperation with the European Public Prosecutor's Office and the effectiveness of OLAF investigations – see in particular paragraphs 16, 38 and 39.

central database or other form of centralised statistical records that might provide an overview of the nature and status of fraud cases (see paragraph 48).

Coordination mechanisms are often lacking

74 Protection for the EU's financial interests at the level of the Member States does not exclusively concern the authorities responsible for the implementation of Cohesion funding or the AFCOSs. Other interested parties include investigation and prosecution bodies, competition authorities, procurement agencies and, depending on the country, certain other institutions. Member States should put in place adequate coordination mechanisms so that the various actors can exchange information about measures taken and planned, as well as recommendations for improvement.

75 However, most of the Member States we visited do not have proper coordination mechanisms involving all the relevant parties in the fight against fraud involving EU Cohesion funding.

76 In Bulgaria, where 60 % of the cases we examined had been rejected or terminated by the prosecutor's office, neither the AFCOS nor the managing authorities systematically analyse the reasons for rejection. In Hungary, the AFCOS does not have an overview of measures actually implemented as part of the anti-fraud management process or of the status of reported cases. The Romanian AFCOS carries out coordination work solely on the basis of bilateral agreements with each of the programme authorities, but there is no national multilateral coordination mechanism involving all stakeholders. In Spain, the establishment of a body meant to assist the AFCOS by coordinating all parties to the fight against fraud has been pending since the AFCOS was set up in 2016⁴⁷.

⁴⁷ The Royal Decree regulating the composition and the functioning of this body was finally adopted on 1 March 2019 and published on 19 March 2019.

77 We found an example of good coordination practice in Latvia (see [Box 5](#)).

Box 5

Coordination between managing authorities and investigation and prosecution bodies

In Latvia, the investigative authorities refused to start criminal proceedings in a number of cases identified by the managing authority and its delegated intermediate bodies. To analyse the reasons for these refusals and determine whether changes were required to working practices, the AFCOS set up an interinstitutional working group involving the authorities, the Ministry of Justice, the police and the State prosecution service. The working group now meets regularly to examine cases of suspected fraud in the implementation of Cohesion funding.

Conclusions and recommendations

78 Through this audit, we assessed whether managing authorities have properly met their responsibilities at each stage of the anti-fraud management process: fraud prevention, fraud detection and fraud response (including reporting on fraud and recovery of funds unduly paid). To this end, we assessed whether managing authorities have:

- (a) developed anti-fraud policies, performed a thorough risk assessment and implemented adequate preventive and detective measures; and
- (b) properly responded to detected fraud in coordination with AFCOSs and other competent anti-fraud bodies.

79 Our overall conclusion is that, although there have been improvements in the way managing authorities identify fraud risks and design preventive measures, they still need to strengthen fraud detection, response and coordination.

Managing authorities generally have no specific anti-fraud policy

80 Managing authorities seldom prepare a formal anti-fraud policy or a similar single document specifying the fraud prevention, detection and response (correction and prosecution) measures which they have designed following a risk assessment. We consider that the preparation and publication of a formal anti-fraud policy in the form of a single, stand-alone document is essential in order to communicate a managing authority's determination to actively combat fraud. This is particularly relevant, as only ten Member States have adopted a national anti-fraud strategy based on the Commission's recommendation. We consider the absence of provisions requiring managing authorities to adopt formal anti-fraud policies to be a shortcoming in the design of the anti-fraud framework for 2014-2020 (paragraphs [18](#) to [21](#)).

Recommendation 1 – Develop formal strategies and policies to combat fraud against EU funds

- (a) Member States that do not have a national anti-fraud strategy (see paragraph 20 and footnote 19) should formulate one. The strategy should at least:
- be based on the assessment of existing risks and involve knowledgeable actors from different areas (managers of EU funds, competent fraud investigation and prosecution bodies, etc.) in its preparation;
 - outline concrete measures for fraud prevention, detection, investigation and prosecution, and recovery and sanctions;
 - contain specific arrangements for monitoring the implementation of anti-fraud measures and measuring results; and
 - explicitly assign responsibilities for the implementation, monitoring, coordination and comparative evaluation of anti-fraud measures.
- (b) Unless a sufficiently detailed strategy exists at national level, the Commission should require managing authorities to adopt a formal anti-fraud policy or statement covering the OPs under their responsibility. This policy should serve as a single reference source specifying the strategies for the development of an anti-fraud culture, the allocation of responsibilities for tackling fraud, the reporting mechanisms for suspicious of fraud and the way different actors need to cooperate in line with Key Requirement 7 and the Commission’s guidance.

Timeframe: by the end of 2019

81 In line with the zero-tolerance approach to fraud, and during negotiations and approval process for the CPR for the period 2021-2027, the co-legislators could consider making compulsory the adoption of national strategies or anti-fraud policies.

Managing authorities systematically assess fraud risks, but this process could be further improved

82 In line with the provisions of the 2014-2020 control framework, managing authorities now systematically assess fraud risks (largely based on the guidance provided by the Commission), which is an improvement in the fight against fraud (paragraphs 22 and 23). However, for some of the managing authorities we visited the

approach is still too mechanical and does not include additional input from other knowledgeable parties such as the AFCOSs or investigative and prosecution bodies.

83 Managing authorities generally conclude that their existing anti-fraud measures are good enough to address fraud risks. We consider that this conclusion may be too optimistic (paragraphs [24](#) to [28](#)).

Recommendation 2 – Make fraud risk assessment more robust by involving relevant external actors in the process

Managing authorities, in particular those in charge of programmes with particular high risk and high financial volume, should seek to involve relevant external actors with proven experience in combating fraud (e.g. representatives from prosecution bodies) in the evaluation of risks and of the suitability of existing anti-fraud measures.

Timeframe: by the end of 2019

Managing authorities have improved fraud prevention measures but made no significant progress towards proactive fraud detection

84 The additional anti-fraud measures developed for the 2014-2020 period largely focus on preventive measures, which are more comprehensive than those set up for 2007-2013 (paragraphs [29](#) to [32](#)).

85 However, fraud detection measures for 2014-2020 remain largely the same as for 2007-2013, which were designed in a weaker control framework (paragraphs [33](#) to [35](#)). Managing authorities make insufficient use of data analytics for fraud detection, and most of the Member States we visited did not use the Arachne tool to its full potential (paragraphs [36](#) to [38](#)).

86 Managing authorities made no significant progress towards 'proactive' fraud detection, for example by checking specifically for collusion in public procurement (paragraph [33](#)). Although managing authorities perceive fraud hotlines and whistleblowing mechanisms to be very effective fraud detection methods, fewer than half of the managing authorities that replied to our survey actually use them (paragraphs [34](#) and [35](#)).

87 Furthermore, it is not possible to assess the effectiveness of fraud prevention or detection measures, since managing authorities lack procedures for monitoring their implementation and evaluating their effectiveness (paragraphs [40](#) and [41](#)).

Recommendation 3 – Improve fraud detection measures by generalising the use of data analytics tools and promoting the use of other ‘proactive’ fraud detection methods

- (a) Managing authorities that do not currently use fraud data analytics tools, in particular Arachne, should take them on for their potential to identify fraud risks in a systematic and cost-efficient manner;
- (b) the Commission, in its supervisory capacity under shared management, should actively promote the use of ‘proactive’ and other new fraud detection methods by regularly disseminating specific cases of best practice; and
- (c) in cooperation with the AFCOSs, the Commission should develop minimum arrangements for monitoring and evaluating the implementation and effectiveness of fraud prevention and detection measures.

Timeframe: by the end of 2021

88 During negotiations and approval process for the CPR for the period 2021-2027, the co-legislators could consider making compulsory the use of proper data analytics tools (e.g. Arachne) for the 2021-2027 programming period, in order to improve the effectiveness of fraud detection at a relatively low cost.

Managing authorities under-report fraud cases for the PIF reports and fail to refer them to investigative and prosecution bodies

89 As regards fraud response, we found that managing authorities under-report fraud and that this affects the reliability of the fraud detection rates published in the PIF reports (paragraphs [48](#) to [57](#)). Several managing authorities also fail to systematically communicate suspicions of fraud to investigation or prosecution bodies (paragraphs [58](#) to [60](#)). We found that managing authorities focus on the withdrawal of EU funding and do not always recover fraudulent amounts from perpetrators or impose dissuasive penalties or sanctions (paragraphs [61](#) and [62](#)). Nor do managing authorities satisfactorily assess the possible horizontal implications of cases where

fraud is suspected (paragraphs 63 and 64; Box 4). All of these aspects severely limit the deterrent effect of fraud investigations.

Recommendation 4 – Monitor fraud response mechanisms to ensure they are consistently applied

- (a) The Commission should establish clear fraud reporting requirements for Member State bodies in general and managing authorities in particular. These should be based on the standard interpretation of fraud affecting the EU's financial interests in the new PIF Directive;
- (b) the Commission should require managing authorities to systematically assess the horizontal implications of suspected fraud in their management and control systems; and
- (c) the Commission should encourage managing authorities to communicate all suspicions of fraud to criminal investigation or prosecution bodies.
- (d) To ensure deterrence is effective, managing authorities should take proportionate measures to recover public funds from perpetrators of fraud and not just decertify the expenditure from EU funding.

Timeframe: by the end of 2019

90 During negotiations for the CPR for the 2021-2027 programming period, the co-legislators could consider introducing specific sanctions and penalties for those responsible for fraud against the EU's financial interests. In particular, as in other policy areas, these measures could include a specific monetary penalty that would vary according to the financial impact of the irregularity, or a mechanism for exclusion from EU funding for a specific number of years.

The fight against fraud is weakened by the Regulation's insufficient definition of AFCOS functions and little coordination among Member State bodies

91 Regarding the coordination of anti-fraud activities, we found considerable variation in the way AFCOSs are organised and resourced (paragraphs 66 to 70). In this respect, the Commission's proposal to amend the OLAF Regulation does not provide sufficient clarity as to the minimum functions of an AFCOS. The status of fraud cases is inadequately reported and followed up (paragraphs 71 to 73), as AFCOSs do not

always have access to information on the status of fraud cases under investigation. The frequent absence of coordination negatively impacts the effectiveness of the fight against fraud (paragraphs 74 to 78).

Recommendation 5 – Support the expansion of the AFCOSs’ function to improve coordination

The Commission should encourage Member States to expand the AFCOSs’ role of coordination with managing authorities to liaising with all national bodies charged with the investigation and prosecution of suspected fraud.

Timeframe: by the end of 2019

92 While respecting the Member States’ right to flexibility in defining and organising their own work against fraud in line with the principle of subsidiarity, the EU co-legislators could consider determining minimum functions for an AFCOS. This could be done, for example, in the context of the ongoing legislative process for modifying the OLAF Regulation in order to ensure AFCOSs’ effective coordination role. The functions of the AFCOSs could at least include the following:

- liaising between managing authorities (and the other programme authorities) and other Member State bodies involved in combating fraud, in particular investigation and prosecution bodies;
- monitoring the status of individual cases and reporting to the Commission on the follow-up given by the responsible managing authorities, with due regard to the confidentiality of ongoing investigations; and
- certifying annually, with a view to the Commission’s preparation of PIF reports, that the information recorded in the IMS is complete, reliable, accurate and up-to-date.

This Report was adopted by Chamber II, headed by Mrs Iliana IVANOVA, Member of the Court of Auditors, in Luxembourg at its meeting of 27 March 2019.

For the Court of Auditors

Klaus-Heiner LEHNE
President

Acronyms and abbreviations

AFCOS: Anti-fraud coordination service

CPR: Common Provisions Regulation

ESF: European Social Fund

ERDF: European Regional Development Fund

FDR: Fraud detection rate

FRA: Fraud Risk Assessment

IMS: Irregularity Management System

OLAF: European Anti-Fraud Office (*Office européen de lutte antifraude*)

OP: Operational programme

Glossary

Anti-fraud coordination service (AFCOS): A body designated by each Member State in accordance with the OLAF Regulation to facilitate cooperation and exchange of information with OLAF.

Anti-fraud policy: Tool used to communicate an organisation's determination to combat and address fraud. It should cover:

- Strategies for the development of an anti-fraud culture;
- Allocation of responsibilities for tackling fraud;
- Reporting mechanisms for suspicions of fraud;
- Cooperation between the various actors.

The anti-fraud policy should be visible within the organisation (distributed to all new staff, included on intranet) and it should be clear to staff that it is actively implemented (through regular updates on fraud matters and reporting of outcomes of investigations into fraud). *(Source: EGESIF_14-0021-00, section 4.1 and Annex 3)*

Arachne: Risk-scoring IT tool developed by the Commission (DG EMPL and DG REGIO) for the ERDF, CF and ESF, and made available to the Member States free of charge in exchange for management data.

COCOLAF: Advisory Committee for the Coordination of Fraud Prevention (COCOLAF) set up by the Commission Decision 94/140/EC of 23 February 1994. The committee coordinates action by the Member States and the European Commission to combat fraud affecting the Community financial interest.

COCOLAF oversees a series of other groups, which deal with specific issues:

- Fraud prevention group;
- Reporting & analysis of fraudulent and other irregularities group;
- Anti-Fraud Coordination Service (AFCOS) Group and
- OLAF Anti-Fraud Communicators' Network (OAFCN).

EGESIF: Expert group on the European Structural and Investment Funds, which assists the Commission in relation to the implementation of EU cohesion policy legislation and coordination and information exchange among Member State authorities.

EGESIF discusses and adopts specific guidance on a range of topics relating to the implementation of Cohesion funding. While this guidance is not legally binding, it is generally used by the Commission when assessing the work of Member State authorities. In the 2007-2013 programming period the group was referred to as COCOF.

Established fraud: An irregularity that has been judged to constitute 'fraud' by a definitive criminal court decision.

European Anti-Fraud Office (OLAF): The Commission department responsible for fighting fraud affecting the financial interests of the EU. OLAF is charged with developing and coordinating EU anti-fraud policies and conducting investigations into fraud and corruption involving EU funds (revenue and expenditure) and/or EU officials.

Fraud deterrence: Assumed impact of anti-fraud policies and measures in reducing the likelihood that natural or legal persons will act in a fraudulent manner.

Irregularity: An act or omission in breach of EU law (or of national law relating to its application) which has a potentially negative impact on EU financial interests. Member States shall notify the Commission of irregularities that exceed €10 000.

Irregularities reported as fraudulent: A term which the Commission uses in its annual PIF reports to distinguish suspected and established cases of fraud reported by Member States from irregularities not deemed to be intentional.

Irregularity Management System (IMS): A web-based application used by Member States for reporting irregularities (fraudulent and non-fraudulent) in the field of shared management.

Primary administrative or judicial finding (PACA): A first written assessment by a competent authority, either administrative or judicial, concluding on the basis of specific facts that an infringement has occurred, intentionally or otherwise, that may be detrimental to the EU budget.

PIF: Relating to the protection of the EU's financial interests. From the French "*protection des intérêts financiers*".

Programme authorities: The Member State bodies in charge of managing and monitoring the implementation of operational programmes funded by the ESIFs. There are three types: managing authorities (often supported by intermediate bodies), certifying authorities and audit authorities.

- Managing authorities (MAs) are in charge of the overall management of each OP. They are often supported by delegated 'intermediate bodies'. Their tasks include selecting eligible operations and carrying out the financial control of these operations. MAs are the main authority responsible for setting up anti-fraud measures.
- Certifying authorities (CAs) are responsible for preparing the annual accounts and certifying their completeness and accuracy. They are also responsible for submitting payment applications to the Commission. CAs may perform checks resulting in the identification of suspected fraud.
- Audit authorities (AAs) are independent national or regional bodies responsible for establishing whether or not the annual accounts submitted by the certifying authorities paint a fair and accurate picture, the expenditure declared to the Commission is legal and regular, and OP control systems function properly. AAs may address anti-fraud measures set up by MAs through their systems audits and may identify suspected fraud through their audits of operations/transactions.

Suspected fraud: An irregularity that gives rise to the initiation of administrative or judicial proceedings at national level to establish whether the act (or omission) was intentional.

REPLIES OF THE COMMISSION TO THE SPECIAL REPORT OF THE EUROPEAN COURT OF AUDITORS

“TACKLING FRAUD IN EU COHESION SPENDING: MANAGING AUTHORITIES NEED TO STRENGTHEN DETECTION, RESPONSE AND COORDINATION”

EXECUTIVE SUMMARY

III. The Commission has ordered an external study: "*Preventing fraud and corruption in the European Structural and Investment Funds – taking stock of practices in the EU Member States*¹" to assess the set-up of effective and proportionate anti-fraud measures. It was published in November 2018.

This study, based on the analysis of 50 programmes, concluded that the anti-fraud efforts were more formalised and systematic in 2014-2020. A vast majority of managing authorities used the risk assessment tool provided by the Commission in its 2014 Guidance. The fraud risk assessment process is one example showing anti-fraud efforts became more formalised. The study mentions that going through this process with a list of Commission recommended controls contributed to some authorities adopting new detection controls or improving existing ones. For example,

- Existence of a “Commission of Tender Experts” giving the possibility to tenderers to revert to this Commission in case the procedure is perceived as flawed;
- Pre-defined budgets via market research, which are not disclosed (manipulation of public procurement).
- Use of IT tools for identification of double claims (manipulation of costs and quality)
- Collaboration with public procurement or competition authorities (collusive bidding)
- Complaint mechanism for beneficiaries

The Commission has designed and actively promotes a data-mining tool, Arachne, and provides it to the Member States free of charge. It is currently used by 165 programmes to improve detection of fraud red flags.

IV. The Commission pointed out several times in its Annual Reports on the protection of the EU’s financial interests (PIF Reports) the concrete possibility of under-reporting by some Member States. The Commission is continuously developing IMS and provides guidance on reporting to Member States in order to mitigate such risks. Furthermore, the fraud detection rates and their related multiannual analysis have been designed taking into account such shortcomings.

The Commission is aiming, in the framework of its revised Commission Anti-Fraud Strategy (CAFS), at enhancing its analysis based on additional elements, in particular by developing country profiles to better understand differences in detection and reporting among Member States.

V.

First indent: The Commission fully supports the adoption of national anti-fraud strategies by Member States and has for this purpose developed, under the auspices of the Advisory Committee for Coordination for Fraud Prevention (COCOLAF), guidelines for national anti-fraud strategies. The Commission welcomes the fact that ten Member States have already done so. Through its guidance the Commission has also recommended managing authorities to adopt anti-fraud policy statements.

¹ Link to the study: https://ec.europa.eu/regional_policy/en/information/publications/studies/2018/study-on-the-implementation-of-article-125-4-c-of-the-regulation-eu-no-1303-2013-laying-down-the-common-provisions-on-the-european-structural-and-investment-fund-in-member-states

The Commission will continue to encourage the adoption of the national anti-fraud strategies (NAFS) by Member States and to provide them assistance accordingly. However, it has no legal basis to require each of the managing authorities to adopt a formal, stand-alone anti-fraud policy at OP level. Notwithstanding this, the Commission has recommended managing authorities to publish an anti-fraud policy statement and proposed the guidance for this.

Second indent: The Commission supports and promotes cooperation between Cohesion funds authorities and other key national anti-fraud players in general, and will continue to do so, in particular for programmes presenting particularly high risks, or involving high financial volumes, in accordance with the principle of proportionality.

Third indent: The Commission has already produced extensive guidance for Member States on fraud prevention and detection measures. The Commission supports and will continue to actively promote the use of any data mining tool, including in particular Arachne, by programme authorities. The Commission has designed Arachne specifically for the needs of programme authorities under Cohesion policy and provides it to Member States free of charge.

Fourth indent: In line with the provisions of the Common Provisions Regulation (CPR), the Commission will monitor the implementation of the anti-fraud measures to be adopted by the Member States at the level of operational programmes (OP). Moreover, the Commission, in the framework of its revised Anti-Fraud Strategy, is developing country profiles on the anti-fraud capabilities of Member States in relation to, inter alia, prevention and detection. These country profiles will help to better assess the implementation of fraud prevention and detection measures. However, measuring the effectiveness of fraud prevention and detection methods is a highly complex and challenging task, as fraud is influenced by a great variety of exogenous factors, of which not all are policy domain -specific.

Fifth indent: The Commission will continue encouraging the Member States to strengthen the coordination role of Anti-Fraud Coordination Services (AFCOS), in particular through expanding their network.

VI.

The Commission will carefully assess any amendment of this kind put forward by the co-legislators.

VII. The Commission agrees with the ECA on the importance of ensuring the effectiveness of AFCOSs and could support a clearer definition of their functions. The Commission's proposal to amend the OLAF Regulation represents already a significant improvement over the current situation as the AFCOSs would need to ensure that the assistance to OLAF is provided regardless of the way it is provided (i.e. directly by the AFCOS, or by a different authority acting on the AFCOS' request).

INTRODUCTION

05. The 2014-2020 Common Provisions Regulation introduced for the first time a requirement to have a risk-based approach and to put proportionate and effective anti-fraud measures in place at operational programme level. This is an important step towards better financial management and the protection of the EU budget.

07. The anti-fraud information platform referred to by the ECA is OLAF's Anti-Fraud Information System (AFIS).

Common Commission reply to paragraphs 08 and 09:

The proportion of both fraud suspicion and non-fraudulent irregularities reported by Member States' authorities under Cohesion policy can be interpreted as the growing capacity of Member States to detect and report irregularities, including potential fraud cases, to the Commission. The financial impact fluctuates greatly between Member States and between the years.

In the PIF Reports, the Commission has regularly and consistently observed that this may be due to the fact that projects funded in particular under the European Regional Development Fund (ERDF) and the Cohesion Fund (CF) may involve very large sums compared to other policy areas.

10. Concerning Slovakia, the high fraud detection rate for 2007-2013 is, at least in part, due to a few cases (4) with exceptional financial amounts involved, which were reported in 2017.

OBSERVATIONS

Common Commission reply to paragraphs 18 and 19:

The Commission fully supports the adoption of national anti-fraud strategies by Member States through which the Member States indicate to beneficiaries and the public how they intend to fight fraud. It should be noted that there is no legal obligation for Member States to adopt a national anti-fraud strategy. Despite this, ten Member States have adopted a national anti-fraud strategy and one Member State is updating its existing one (see the 2017 PIF report).

The Commission guidance note for Member States and programme authorities on fraud risk assessment and effective and proportionate anti-fraud measures (EGESIF 14-0021 of 16 June 2014) includes a voluntary template for an anti-fraud policy statement at programme level.

The purpose of this statement is to indicate to beneficiaries and the public the zero tolerance for fraud and how managing authorities intend to fight fraud.

In addition, in order to increase awareness of fraud and corruption and assist managing authorities in the fight against fraud, the Commission organised several anti-fraud and anti-corruption seminars in Member States in 2014-2015 in collaboration with Transparency International.

The Commission further refers to its guidance on how to assess management and control systems' key requirements (KR), and in particular assessment criterion 7.3 in relation to KR7 on "proportionate and effective antifraud measures". Even though this KR does not refer to an anti-fraud policy per se but to the need to conduct a self-assessment leading to targeted controls, it adds also other aspects than the assessment of fraud risks identified, and makes clear what the position of the programme authorities against fraud should be.

Common Commission reply to paragraphs 20 and 21:

First, the Commission considers that the Member States have taken a number of measures to implement the guidance and their obligations under the Regulation. One of the conclusions of the external study on anti-fraud measures in Member States commissioned by the Commission is that the Commission efforts to address fraud and corruption have catalysed a number of changes at Member State level and have resulted in a more structured and systematic approach. In particular, conducting the fraud risk assessment in accordance with the criteria set out in the template helped to put more focus on fraud and corruption risks, and created clear links between identified risks and specific mitigating measures (Quoted external Study, p.49).

Second, it is the combination of deficiencies in Key Requirement 7 with other non-essential key requirements which can be defined as "serious deficiencies at the level of the overall management and control system", and therefore lead to interruptions in the payment deadline or financial correction. In this context, Key Requirement 4 "*Adequate management verifications*" and 16 "*Adequate audits of operations*" act as mitigating controls, as they allow the detection of potential fraud. The non-compliance of one aspect of the management and control system associated with financial impact on the legality and regularity of the underlying transaction(s) leads to the interruption of payment or to financial corrections by the Commission. The Commission therefore considers that the 2014-2020 legal framework has been clearly reinforced by introduction of the obligation to put in place effective and proportionate anti-fraud measures, even though no legal requirement for formal anti-fraud policies is imposed.

Enabling conditions are fewer and more focused on the specific goals of the Fund concerned. Once met, they are meant to 'enable' Member States' authorities to start the implementation of the Funds. Anti-fraud measures are aimed at minimizing risks and need to be periodically reviewed. Therefore, anti-fraud measures are not suitable for inclusion into the enabling conditions.

Common Commission reply to paragraphs 22 to 23bis:

The Commission's practical ready-to-use fraud risk assessment tool mentioned by the ECA allows a consistent approach to risk assessments across Member States for all programmes.

The external study on anti-fraud measures mentioned by the ECA confirmed the fact that managing authorities now assess fraud risks in line with the requirements of the 2014-2020 control framework, determine the readiness of existing internal controls to address the risks associated with different fraud scenarios and identify areas where additional controls are necessary. New requirements have led to a more structured approach to fraud risk assessment.

The Commission has also made practical presentations on the use of its recommended risk assessment tool during anti-fraud/anti-corruption awareness seminars in 2014-2015, covering 15 Member States (BG, RO, IT, SK, CZ, HR, LV, HU, MT, SI, LT, ES, PL, PT, EE). In addition, in 2015, the tool was presented to all Member States as part of the Irregularity Management System (IMS) training. The Commission shares the ECA's conclusion that Member States have used the model designed by the Commission.

The Commission will continue to support the Member State authorities in improving their administrative capacity when fighting fraud. For now, the new training module for experts (in cooperation with EIPA) on *Identifying and preventing fraud and corruption in ESI funds 2014-2020*, and a follow up study, which will build on the outputs from the stocktaking study, are planned.

Common Commission reply to paragraphs 24 and 25:

The Commission is of the view that managing authorities generally take a more proactive approach towards the assessment of fraud risks.

The Commission's view is confirmed by the external study, which found that "in most OPs (40) authorities took an active approach to developing their fraud risk assessments", 'a large majority of the fraud risk assessments based on the Commission's template (76%) were filled in comprehensively, 14% only partially, and 8% contained only basic information. The two fraud risk assessments (FRA) that had the least information were from those OPs where the passive approach was taken'. The study also concludes that '...furthermore some authorities expanded the scope of FRAs self assessments to other forms of risks ... while other MAs provided more granularity to their assessment'. Additionally, managing authorities notice an increase in awareness of their staff with respect to the importance of anti-fraud risk assessment and improvement of IT systems used to prevent and detect fraud.

According to the Commission's guidance, the anti-fraud process starts with a self-assessment based on the managing authorities' knowledge of the environment and its specific fraud risks as well as on commonly recognised and recurring fraud schemes. The Commission recommends for the self-assessment team that the most relevant actors take part in the process, which could mean different departments of the managing authority (MA) as well as certifying authority (CA) and implementing bodies (IB). Involving AFCOS or other specialised bodies is left at the discretion of managing authorities (section 3.2). The audit authority (AA) will audit the process without taking any direct role. As regards the fraud risk assessment, the external study also confirms that the 'involvement of variety of authorities in the antifraud activities (MA, IBs, AA, CA, AFCOS and law enforcement authorities) leads to enhanced coordination of antifraud activities and reduces fraud risks'.

26. Fraud risk assessment is an ongoing exercise, which must be fine-tuned and revised during implementation of the programme.

First bullet: The 2014-2020 assurance model is based on supervision of the managing authority by the audit authority through system audits and audits on operations, resulting in an assessment of each key requirement of management and control systems, including key requirement (KR7) specifically referring to anti-fraud measures. In the Bulgarian case, the audit authority has detected some fraud risks and the responsible managing authority took adequate action to correct the situation. The overall system therefore functioned to ensure more robust anti-fraud measures.

Second bullet: The Commission will explore any possible action to raise awareness with the French authorities and improve the assessment with the concerned managing authorities and audit authorities in the context of respective annual meetings.

Third bullet: The Spanish example shows that the managing authority takes its responsibilities in relation to antifraud measures and the supervision of intermediate bodies seriously. Through the mandated evaluation, the managing authority could recommend actions to adjust the identified weaknesses, followed up by the internal audit section of the managing authority.

Fifth bullet: The Commission services have made audit recommendations to Hungary to improve further their anti-fraud measures. For example, the Hungarian managing authorities should ensure that the verification procedures at the selection and management verification stages include proportionate anti-fraud measures including the tailoring of the IT subsystem.

Hence, the Commission expects the fraud risk assessment in Hungary to improve.

27. It should be noted that Member States are expected to put in place anti-fraud measures taking account of the principle of proportionality. These measures can always be improved based on fraud detection cases and newly identified risks, however they should remain proportionate to the risk identified.

The external stocktaking study concluded that anti-fraud measures put in place are generally proportionate to the risks identified, even when taking into account that some authorities may underestimate the risks during their self-assessment. In addition, managing authorities proposed self-created mitigating measures in response to identified risks beyond what was proposed by the Commission, suggesting that some reflection was conducted on the best way to tackle the risks.

29. The Commission recommends managing authorities to adopt a proactive, structured and targeted approach for managing the risk of fraud. In line with the principle of proportionality embedded in the regulatory provisions, the risk-based measures must also be cost-effective.

Common Commission reply to paragraphs 30 to 32:

According to the Commission Guidance on fraud risk assessment and effective and proportionate anti-fraud measures, prevention techniques most often revolve around implementing a robust system of internal controls, combined with a proactive, structured and targeted fraud risk assessment. Additionally, comprehensive training and awareness raising activities and the development of an 'ethical' culture (code of conduct, mission statements) and clear allocation of responsibilities (to set up a management and control system that effectively fights fraud) can also be very useful in fighting fraud and recusing the opportunities to commit fraud. Besides the above mentioned the Commission also proposes other mitigating measures, for specific areas (conflict of interest, public procurement, double funding), which according to the external study, almost all Member States authorities in the sample use in their fraud prevention mechanisms. Furthermore, the study concluded that some Member States, besides using what the Commission has proposed, also developed their own measures to prevent fraud.

Additionally, the Commission is exploring new innovative ways of preventing corrupt practices in projects funded by EU funds and ensuring tax payers' money is spent efficiently and transparently, such as Pilot Integrity Pacts as referred to by the Court in Box 1.

Over the past years, the Commission has also issued specific documents to reinforce fraud prevention, most of them under the auspices of the Advisory Committee for Coordination of Fraud Prevention (COCOLAF). For example:

- Fraud in Public Procurement, A collection of Red Flags and Best Practices (2017);
- Guidelines on National Anti-Fraud Strategies (2014 and 2016);
- Identifying conflicts of interests in public procurement procedures for structural actions, A practical guide for managers (2013);
- Compendium of anonymised cases – Structural Actions (2012).

33. Prevention and detection of fraud are interlinked. Detection is indeed part of the normal controls in place for all programmes, both at the level of the managing authority (management verifications), and of the audit authority (audits and controls).

The external study confirmed that additional controls have been developed by managing authorities to complement those recommended by the Commission for 2014-2020. These also include measures contributing to fraud detection, such as:

- Existence of a “Commission of Tender Experts” giving the possibility to tenderers to revert to this Commission in case the procedure is perceived as flawed;
- Pre-defined budgets via market research, which are not disclosed (manipulation of public procurement);
- Use of IT tools for identification of double claims (manipulation of costs and quality);
- Collaboration with public procurement or competition authorities (collusive bidding);
- Complaint mechanism for beneficiaries.

The opportunities of existing and available datamining tools such as Arachne are already used by some programme authorities in a more comprehensive way. For example, as a risk scoring and detection tool to check in the award and grant processes potential beneficiary companies, their beneficial owners and business partners, to assess potential conflicts of interest and risks of double funding, to identify red flags, and to increase the effectiveness and efficiency of management verifications.

Finally, in the 2017 PIF Report, the Commission recommended Member States to exploit the potential of risk analysis (understood as focusing controls on projects' risk profiles to be designed and tailored on the basis of in-depth assessments) in view of increasing their pro-active detection capabilities.

Common Commission reply to paragraphs 34 and 35:

The absence of secure reporting channels for whistleblowing reporting, was a strong concern voiced in the responses to the Commission's 2017 public consultation.

Current proposal of the Whistleblower Directive includes the internal and external reporting channels ensuring confidentiality in all entities in the private and public sector, across the EU.

The proposed Directive requires: i) legal entities in the private and public sector; ii) competent authorities and, iii) Member States to provide easily accessible information on the reporting channels, the protection, the conditions to benefit from the protection and remedies available, thereby increasing legal certainty for whistleblowers. Moreover, the proposal provides that whistleblowers qualify for protection if, when reporting, they had reasonable grounds to believe that

the information reported falls within the scope of this Directive. This safeguard ensures that whistleblowers do not lose protection if in the end it turns out that the report does not fall within the scope (if for instance the breach involved use of national and not EU funds).

With regard to awareness raising, the amendments currently discussed with the co-legislators make it explicit that anonymous whistleblowers, are protected in case their identity is subsequently revealed and they meet the conditions for protection set out in the proposal.

Common Commission reply to paragraphs 36 and 37:

Arachne as a risk-scoring tool can increase the efficiency of projects' selection, management verifications and audit, and further strengthen fraud identification, prevention and detection. The effective use of Arachne is a good practice in order to identify red flags and target fraud combatting measures, and should be taken into account when assessing the adequacy of current preventive and detective controls in place. In the 2015 and following PIF Reports the Commission explicitly recommended Member States to increase their use of IT risk scoring tools (namely Arachne) and risk analysis and stressed their importance in the fight against fraud.

The opportunities of existing and available datamining tools such as Arachne are already used by some programme authorities in a more comprehensive way. For example, as a risk scoring and detection tool to check in the award and grant processes potential beneficiary companies, their beneficial owners and business partners, to assess potential conflicts of interest and risks of double funding, to identify red flags, and to increase the effectiveness and efficiency of management verifications.

See also the Commission reply to paragraph 33.

37.

First bullet: The Commission services organised a meeting in February 2019 with the Greek authorities to clarify their position on the integration of the use of Arachne in the management and control system for Greek programmes. The conclusion of this meeting is that Arachne could be complementary to the tools developed internally by the Greek programme authorities and therefore further work, jointly with the Commission, is needed to integrate Arachne into the management and control system.

Second bullet: The Commission is continuously encouraging Member States to regularly update operational data in order to exploit the full capacity of the Arachne datamining tool. For the four Member States audited by the ECA, the Commission notes an increase in the number of active users or in the number of OPs covered by Arachne.

Third bullet: Arachne can be used by the investigative bodies on a case-by-case basis with due regard to data protection regulations.

38. The Commission continues to visit programme authorities to promote the benefits and functionalities of the Arachne datamining tool. In parallel, the Commission is also exploring the possibility of further targeting risk areas by either eliminating (obsolete) indicators or by creating new indicators, e.g. an indicator to confirm the SME status of a company.

The perception by some Member States that the usefulness of the tool depends on the number of OPs that regularly upload and update data is incorrect.

The usefulness of Arachne instead depends on the input by the authorities of their own programme data regularly updated. This OP's internal data is then crosschecked and processed by Arachne with data on companies across Europe and the world, which come from external databases.

Common Commission reply to paragraphs 40 and 41:

Fighting fraud is a continuous process which starts with putting in place a fraud risk assessment and mitigating measures.. Member States' audit authorities must systematically review the implementation of effective and proportionate anti-fraud measures at the level of intermediate bodies as part of their system audits (KR7 assesses the adequacy of such measures).² Additionally, the implementation of anti-fraud measures is audited by the Commission.

The Commission's and national authorities' audit results so far show that for 263 OPs tested, 100 OPs have in place well-functioning anti-fraud measures, for 152 OPs anti-fraud measures were functioning well but requiring some improvements and for 11 OPs these measures require significant improvements.

Effectiveness of fraud prevention actions is hard to measure, especially in the first years of implementation, as it is linked to the level of expenditure on the ground and certification to the Commission.

Fraud detection can be tracked, but measuring its effectiveness would necessitate a comparison with the unknown total extent of fraud, including undetected fraud. However, as already indicated in the Commission's reply to Special Report 1/2019, there is no cost-effective method to estimate undetected fraud reliably and defendably enough for evidence-based policy. Furthermore, the effectiveness of fraud detection also depends on exogenous factors.

The Commission encourages Member States to use the findings of the audit authorities to develop action plans to handle errors and risks found. Furthermore, every time an error/risk is detected in the OP's management and control system, the managing authorities and the central bodies intervene and review the rules of procedure applicable to the given control activities. Thus, the annual fraud risk analysis does not show the errors found during the year.

43. It should be noted that the 2014-2020 assurance model has been strongly reinforced on Member State's accountability which together with the new requirement on the anti-fraud measures in Article 125(4) of the Regulation (EU) N° 1303/2013 (the CPR) can explain the trend depicted by the ECA.

Common Commission reply to paragraphs 44 and 45:

In the PIF Report 2017, the Commission published its own analysis of the "reasons for performing the control" (a structured field) which led to detection in the programming period 2007-2013. Results are similar and complementary.³ Nonetheless, the Commission reaches different conclusions from such analysis. The higher value of detections originating from investigative and prosecution bodies has been highlighted since the 2014 PIF Report⁴ and, according to the Commission's analysis, is linked to the effectiveness of the investigations and the strong investigative capabilities of the authorities concerned.

46. The Council Regulation (EU) 2017/1939 establishing the EPPO (European Public Prosecutor's Office) under enhanced cooperation provides for the obligation of all competent authorities to report cases of fraud affecting the EU financial interests to the European Public Prosecutor's Office⁵. This includes managing authorities.

Moreover, OLAF, as provided for in Regulation 883/2013, will continue to play its key role in the fight against fraud, corruption and any other illegal activity affecting the financial interests of the Union in all Member States.

² The Commission guidance mentions: "*Depending on the results of such audits and on the identified fraud risk environment, follow-up audits may be carried out as often as necessary*". A targeted and proportionate approach is recommended.

³ See SWD(2018) 386 final 2/2, paragraph 4.3, pages 86-88.

⁴ See COM(2015) 386 final, paragraph 4.2.2, page 23.

⁵ O.J. L 283, 31.10.2017, p.1.

Finally, the reporting provisions on irregularities including fraud, provided for in the sectorial legislation, oblige the Member States to inform the Commission of the outcome of any proceeding related to fraud cases.

The above mentioned obligations also apply to the managing authorities.

The Commission has also recommended embedding anti-fraud measures in the framework of national anti-fraud strategies⁶. This recommendation has been followed-up by the Commission's "*General guidelines on National Anti-Fraud Strategies*"⁷. National anti-fraud strategies promote cooperation and coordination as key elements for the protection of the EU financial interests.

Common Commission reply to paragraphs 47 to 48:

Any use made by the Commission of the data reported in IMS is based on the awareness that reporting may be incomplete. This is also clearly stated in several PIF Reports and in the accompanying "Methodology for the evaluation of reported irregularities".⁸ Reporting of detected fraudulent irregularities is linked to the efficiency of the system, as it implies that different bodies and authorities cooperate in this domain. On the basis of these assumptions, the Commission has repeatedly expressed its doubts about the reliability of data received by Member States which report a very low number of fraudulent irregularities.

49. The issue of differing interpretations of the EU definition of fraud has also been acknowledged in the PIF Reports. Sometimes these differences of interpretations are inherent in the different legal systems and the way in which certain behaviours are considered (e.g. conflict of interests is regarded as criminal behaviour in certain countries and not in others and reported accordingly). The Commission proposed to harmonise these definitions in the PIF Directive but the Directive, as adopted by the EP and the Council, although providing for deeper harmonisation of the main PIF offences, does not feature definitions of all relevant offences.

50. The Commission considers that the ECA's finding that managing authorities in Hungary do not properly report suspicions of fraud that are resolved prior to certification to the Commission, is mainly an issue of misinterpretation of the reporting provisions by the Member State. Cases of "suspected fraud" once reported must not be withdrawn from IMS even if there is no longer expenditure submitted to the Commission, as this may have been the case in Hungary. The Commission will call the attention of the Hungarian authorities to the correct application of the provision concerned.

51. The Commission is aware that the triggering moment of reporting may differ among Member States and even within Member States. To this end, the "Handbook on the reporting of irregularities", prepared in cooperation with national experts, was finalised in 2017⁹. It will not solve all situations, but it will surely ensure more consistency in this respect. Its adoption is too recent to have produced its effects already on the data sampled by the ECA.

However, to overcome this issue, in its PIF Reports the Commission follows a multi-annual analysis, which, in relation to Cohesion Policy, encompasses whole programming periods, thus mitigating the impact of delayed reporting.

Common Commission reply to paragraphs 53 and 54:

⁶ See PIF Report 2014 - COM(2015) 386 final of 31/07/2015, recommendation 1, page 30.

⁷ Ares(2016)6943965 of 13/12/2016), developed in the framework of the COCOLAF subgroup on "Fraud Prevention" in cooperation with national experts.

⁸ See SWD(2016) 237 final, paragraph 2.4.

⁹ ARES(2017)5692256 of 21.11.2017.

Whenever there are developments related to a case in IMS, reporting authorities can and must update the related information. Data may be inaccurate and/or obsolete at some point in time, but corrected afterwards. IMS is a "living system", which, albeit not perfect, is still the most complete systems available to date.

The Commission regularly reminds the reporting authorities of the need to check the quality of the reported information and update it, if necessary.

The assessment of the financial impact of fraudulent cases remains a controversial aspect in many respects. The Commission will continue to provide assistance to national authorities, but differences in interpretation are unlikely to disappear completely.

55. The low number of fraudulent irregularities reported by some Member States can be due to many variables, such as the level of controls of EU funds or the proportion of EU funds as compared to the total public investment in that Member State.

The under-reporting by France is known to the Commission and has already been pointed out in previous PIF Reports, which contained specific recommendations to this Member State (among others).

See also Commission replies to paragraphs 47-48 and 53-54 above.

Common Commission reply to paragraphs 56 and 57:

Fraud detection rate measures the financial impact of detected and reported fraudulent irregularities on the payments.

Despite mentioned shortcomings, of which the Commission is fully aware, IMS is the only tool that allows the analysis of fraud detected and reported by the Member States on EU scale.

Based on these analyses and taking into account the known limitations of the system, the Commission draws specific conclusions as regards risks linked to specific policy areas and in relation to the detection efforts and the reporting behaviour of the Member States.

In the framework of its revised Anti-Fraud Strategy, while relying on an improved IMS, the Commission is also aiming at enhancing its analysis based on additional elements, in particular by developing country profiles to better understand differences in detection and reporting among Member States.

As already indicated in relation to the ECA Special Report 01/2019, the absence of a strong correlation between reported fraud detection rates and perception of corruption should not be over-emphasised. Corruption is one of the many *modi operandi* through which fraud against the EU budget is perpetrated.

59. The Commission's guidance note on fraud risk assessment states in section 4.3.3 that "*Managing authorities should have clear reporting mechanisms ensuring sufficient coordination on anti-fraud matters with the audit authority and competent investigative authorities in the Member State*". This is to be translated into the management and control instructions and specific set-up can usually be found under the management and control system description of each programme.

In its 2014 PIF report the Commission carried out a mapping exercise of national obligations¹⁰. In 2014, only four Member States (UK, Ireland, Sweden and Denmark) specified in their replies to the questionnaire on the specific part of 'Article 325 TFEU Report', that they did not have an obligation for public officials to inform prosecution/law enforcement of potential cases of fraud¹¹.

¹⁰ (SWD(2015) 154 final, paragraph 3.2, pages 57-61).

¹¹ See SWD(2015) 154 final, paragraph 3.2, pages 57-61.

The regulation establishing the EPPO already provides a reporting duty for all competent authorities (Article 24), and this will include managing authorities when the EPPO has been set up (by November 2020 at the earliest). In Greece, each managing authority is obliged to inform the AFCOS of each case of suspected fraud and, in this context, an AFCOS liaison person has been appointed within each managing authority. At the same time, a prosecutor has been seconded to the Greek AFCOS office. The Commission will monitor whether this set-up ensures effective communication between the managing authorities and the AFCOS.

In Spain, officials working in public administrations are obliged by national law to report all suspected cases of fraud.

60. The Commission is of the opinion that the analysis of the reasons for rejection of a potential fraudulent case by the competent authority is a shared responsibility. Services analysing and investigating these cases should offer feedback to managing authorities on the research carried out and the reasons not to open an investigation.

AFCOS could play a larger role in this context to ensure a better coordination between the managing authorities and the prosecutor. For example, arrangements of this kind exist in Bulgaria (see the latest annual action plan, adopted on 24 January 2019 - <http://www.afcos.bg/bg/node/227>) and in Greece (where the complaints management system involves the AFCOS).

62. The Commission and Member States have to in the first instance protect the EU budget. This is effective through for example, withdrawal of affected expenditure from the EU co-funded programme by the programme authorities. However, the judicial proceeding may continue at national level and the recovery from perpetrators will take time, depending on the outcome of this judicial proceeding, which can take several years to be finalised. It is therefore, from a point of view of administrative efficiency and legal security of the EU budget, preferable to have the concerned amounts withdrawn immediately from the co-funded operational programme, while the Member State will follow up at national level the required judicial proceedings. Moreover, the Commission has no legal means to force Member States to enter into such judicial proceedings or to recover funds from the perpetrator once expenditure has been withdrawn and, consequently, no longer forms part of the EU co-funded programme.

Common Commission reply to paragraphs 63, 64 and Box 3:

The Commission regularly reminds the Member States of their obligations regarding the possible horizontal implications of a single fraud case identified, based on the guidance note on fraud risk assessment, section 4.4. Some Member States indeed assess the implications of potential fraud cases on their systems and apply corrective measures.

Common Commission reply to paragraphs 66 and 67:

According to the current provisions of Regulation 883/2013, the role of AFCOSs is to facilitate effective cooperation and exchange of information with OLAF. However, the organisation and powers of AFCOSs are left for the decision of each Member State. Since Regulation 883/2013 relates to OLAF's investigations, the role of AFCOSs, as defined in Article 3(4) is limited to investigative cooperation and does not require including tasks such as monitoring of fraud reporting or coordinating the work of all the parties involved at the national level. The Commission, however, could support expanding the role of AFCOSs.

The Commission issued a Guidance Note in 2013, shortly after the entry into force of Regulation 883/2013, encouraging Member States to consider a possible broader role for the AFCOS, by entrusting them also with other anti-fraud tasks. It was intended to support the Member States in the setting up of their AFCOS in the period 2013-2014 and was not binding upon the Member States.

69. The evaluation of the OLAF Regulation showed that the creation of the AFCOSs had brought about a clear improvement in the cooperation and exchange of information between OLAF and the Member States, but it has also identified room for further improvement.

While the diversity of AFCOSs was acknowledged, there were diverging views (notably among the AFCOSs themselves) on the need to further align their role and powers.

70. While the Commission agrees that more coherence among the AFCOSs in various Member States would be desirable, at this point it is up to the co-legislators to decide on any changes.

The Commission proposal to amend the OLAF Regulation, which is now in the legislative process, represents already a significant improvement over the current situation, from several perspectives.

Firstly, it proposes (Article 12a) to further specify the role of the AFCOSs in the Member States in support of OLAF in particular by creating an obligation of result to ensure that OLAF is provided with the assistance it needs for its investigations, either directly by AFCOS or by a different authority.

While abstaining from harmonisation of the organisation and powers of AFCOS, the proposal stipulates that AFCOS should “provide”, “obtain” or “coordinate” the assistance required by OLAF.

Secondly, the proposal also introduces a legal basis for AFCOS to cooperate among themselves, horizontally, which is currently lacking from the legal setting of operation of AFCOS.

71. While the Commission agrees that information on case status and statistics would be useful for effective anti-fraud coordination, the current legal mandate of the AFCOS, as defined in Article 3(4) of Regulation 883/2013, does not require such access to statistics on the number and progress of cases under investigation by competent national authorities.

72. The current OLAF Regulation 883/2013 does not oblige the AFCOS to have a full overview of investigations by competent national authorities involving EU funding in the respective Member State.

73. See common Commission reply to paragraphs 47 and 48.

74. The Commission agrees that for the protection of the EU’s financial interests Member States should put in place adequate coordination mechanisms where different actors can exchange information on the steps taken and planned and recommendations for improvement.

75. OLAF encourages the Member States to set up AFCOS networks to improve national coordination of fight against fraud.

76. Intervening at the level of the operations of the National Prosecutor is not within the competences of the Commission; however, the Commission is adamant about the need for cooperation between the bodies responsible for the management of EU funds, audit and fraud prevention and other relevant national bodies such as the prosecutor's office. In this context, when appropriate, the Commission requests information on measures taken or intended to be taken in order to ensure that ESIF co-financed interventions are implemented in a regular, efficient and effective manner.

See Commission replies to paragraphs 46 and 75.

CONCLUSIONS AND RECOMMENDATIONS

80. The Commission fully supports the adoption of national anti-fraud strategies by Member States in their fight against fraud. Regardless of the absence of legal obligation, ten Member States have on a voluntary basis adopted a national anti-fraud strategy and one Member State is updating its existing one.

The Commission's 2014 guidance note on fraud risk assessment and effective and proportionate anti-fraud measures includes a voluntary template for an anti-fraud policy statement at programme level, the purpose of which is to indicate to beneficiaries and the public that programme authorities have zero tolerance for fraud and how they intend to fight fraud.

The Commission also further refers to its guidance on how to assess management and control systems' key requirements (KR), and in particular assessment criterion 7.3 in relation to KR7 on "proportionate and effective antifraud measures". Even though this KR does not refer to an anti-fraud policy per se but to the need to conduct a self-assessment leading to targeted controls on fraud risks identified, it makes clear what the position of the programme authorities against fraud should be. Non-compliance may lead under certain further conditions (i.e. in combination with other weaknesses) to interruption of payments or financial corrections by the Commission.

Recommendation 1 – Develop formal strategies and policies to combat fraud against EU funds

(a) The Commission notes that the recommendation is addressed to the Member States.

The Commission fully supports the adoption of national anti-fraud strategies by Member States. For this purpose, the Commission has developed under the auspices of the Advisory Committee for Coordination for Fraud Prevention (COCOLAF) guidelines for national anti-fraud strategies.

(b) The Commission accepts the recommendation.

The Commission will continue to encourage the adoption of national anti-fraud strategies by Member States and will continue to assist the Member States accordingly. However, it has no legal basis to require each managing authority to adopt a formal, stand-alone anti-fraud policy at OP level, but has recommended them to do so through its guidance.

A clear policy statement per programme authority as provided in the Commission guidance is indeed an appropriate instrument to indicate to beneficiaries and the public how managing authorities intend to address the fight against fraud. Those managing authorities who wish to go beyond the immediate regulatory requirements can use the template for an anti-fraud policy statement at the programme level provided in the guidance.

81. The Commission will carefully assess any amendment of this kind put forward by the co-legislators.

82. The conclusion of the external study on anti-fraud measures outsourced by the Commission shows that where the Commission's fraud risk assessment tool is used for the OPs, the Member State's approach is more formalised and structured and that in a majority of OPs a 'self-assessment' of the fraud risks is done. Managing authorities have not only mechanically used the Commission proposed mitigating measures, but have added some controls which were not in the suggested options, suggesting that some reflection was conducted on the best way to tackle the risks identified.

83. The anti-fraud measures expected to be put in place by Member States must comply with the principle of proportionality. The measures can always be improved based on fraud detection and newly identified risks. The study outsourced by the Commission concluded that anti-fraud measures put in place are generally proportionate to the risks identified.

Recommendation 2 – Make fraud risk assessment more robust by involving relevant external actors in the process

The Commission notes that this recommendation is addressed to the Member States.

The Commission supports and promotes cooperation between Cohesion funds authorities and other key national anti-fraud players in general, and will continue to do so, in particular for programmes presenting particularly high risks, or with high financial volumes, in accordance with the principle of proportionality.

84. Under the 2014 – 2020 legal framework “anti-fraud measures taking into account the risks identified “ are an additional compulsory requirement for managing authorities compared to previous periods (see Article 125(4)(c) of Regulation 1303/2013). The Member States use not only the mitigating actions proposed by the Commission in its guidance, but have additionally developed their own measures. These additional controls per risk area operate at system and at project level and further include investigations by competent national investigative authorities.

85. Fraud detection is indeed part of the normal controls in place, both at managing authority level and at audit authority level. The fact that system audits now cover the procedures in place for effective and proportionate anti-fraud measures (system key requirement KR 7) provides an additional tool to assess the adequacy of such measures, as shown by the audit assessments reported by audit authorities.

The opportunities of existing and available data-mining tools such as the one designed by the Commission, Arachne, are already used by some programme authorities in a more comprehensive way. For example, as a risk scoring and detection tool to check in the award and grant processes potential beneficiary companies, their beneficial owners and business partners, to assess potential conflicts of interest and risks of double funding, to identify red flags, and to increase the effectiveness and efficiency of management verifications.”

Arachne was modernized in accordance with users’ requirements in 2016 and the update covered the improvement of existing functionalities. It should be stressed again, that in the absence of a legal basis requiring its compulsory use, Arachne is offered to the Member States on a voluntary basis and free of charge by the Commission. It is up to the Member States whether to use the Arachne or any other tool and to what extent.

86. Managing authorities put increasing emphasis on the detection measures, e.g. of collusive bidding through verification measures, including development of checklists and red-flags, collaboration with public procurement and competition authorities and ad-hoc comparison of costs.

Increased use of hotlines and other whistleblowing mechanisms is part of the recommendation from the Commission to the Member States included in the PIF Report 2017. OLAF also provides ‘The Fraud Notification System, which is a web-based tool available to any person who seeks to pass on information concerning potential corruption and fraud. http://ec.europa.eu/anti-fraud/olaf-and-you/report-fraud_en

The current proposal of the Whistleblower Directive includes the internal and external reporting channels ensuring confidentiality in all entities in the private and public sector, across the EU.

87. It should be noted, that effectiveness of fraud prevention is by nature hard to measure and depends on exogenous factors. Fraud detection can be tracked, but measuring its effectiveness would necessitate a comparison with the unknown total extent of fraud, including fraud. However, as already indicated in the Commission's reply to Special Report 1/2019, there is no cost-effective method to estimate undetected fraud reliably and defendably enough for evidence-based policy. Member States must monitor and report fraud and regularly reassess and update the risks identified and proceed with additional proportionate mitigating controls, if necessary.

Recommendation 3 – Improve fraud detection measures by generalising the use of data analytics tools and promoting the use of other ‘proactive’ fraud detection methods

(a) The Commission notes that this recommendation is addressed to the Member States.

The Commission supports and will continue to actively promote the use of any data-mining tool, including in particular Arachne, by programme authorities. The Commission has designed Arachne specifically for the needs of programme authorities under Cohesion policy and provides it to Member States free of charge.

(b) The Commission accepts this recommendation.

In line with its upcoming revised Anti-Fraud Strategy, the Commission will continue to issue documents to disseminate the best practices among national authorities in charge of the implementation of Cohesion Policy.

Examples of such documents issued over the past years under the auspices of the Advisory Committee for Coordination of Fraud Prevention (COCOLAF) include:

- Fraud in Public Procurement, A collection of Red Flags and Best Practices (2017)
- Handbook: The role of Member States' auditors in fraud prevention and detection for EU Structural and Investment Funds, Experience and practice in the Member States (2014)
- Detection of forged documents in the field of structural actions, A practical guide for managing authorities (2013)
- Identifying conflicts of interests in public procurement procedures for structural actions, A practical guide for managers (2013)
- Compendium of anonymised cases – Structural Actions (2012)

Finally, some of the practices identified in the Member States by the external study on effective and proportionate anti-fraud measures outsourced by the Commission are made publicly available in a *Compendium of anti-fraud practices for preventing and detecting fraud and corruption in ESIF* on the Europa site.

(c) The Commission partially accepts this recommendation.

Measuring the effectiveness of fraud prevention and detection methods is a highly complex and challenging task, as fraud is influenced by a great variety of exogenous factors, of which not all are policy domain specific. However, the Commission, in the framework of the revised Commission Anti-Fraud Strategy, is developing country profiles on the anti-fraud capabilities of Member States in relation to, inter alia, prevention and detection. These country profiles will help to better assess the implementation of fraud prevention and detection measures in the Member States.

88. The Commission will carefully assess any amendment of this kind put forward by the co-legislators. The Commission is actively encouraging the Member States to use data-mining tools, in particular Arachne.

89. The Commission pointed out several times in the PIF Reports the concrete possibility of under-reporting by some Member States. The Commission is continuously developing IMS and provides guidance on reporting to Member States in order to mitigate such risks. Furthermore, the fraud detection rates and their related multiannual analysis have been designed taking into account such shortcomings.

The Commission is aiming, in the framework of its revised Anti-Fraud Strategy, at enhancing its analysis based on additional elements, in particular by developing country profiles to better understand differences in detection and reporting among Member States.

Furthermore, the analysis of the reasons for rejection of a potential fraudulent case by the competent authority is a shared responsibility between the managing authorities and the investigative bodies. Services analysing and investigating these cases should offer feedback to managing authorities on the research carried out and the reasons not to open an investigation. In this context, AFCOS could play a larger role in ensuring a better coordination between the managing authorities and the judicial authority.

In shared management, the Commission applies suspension of payments, interruption and financial corrections to Member States to ensure that the EU budget is effectively protected. Member States

also protect the EU budget by withdrawing irregular or fraudulent expenditure from co-funded programmes. It is the Member States' responsibility to recover public funds from fraudsters, in line with national legislation or once national judicial proceedings confirmed fraud.

The Commission regularly recalls the Member States' obligations regarding the possible horizontal implications of a single fraud case identified at programme level, based on the guidance note on fraud risk assessment, section 4.4. There are examples of Member States who have assessed the horizontal implications of potential fraud cases on their systems or for a specific beneficiary and applied corrective measures.

Recommendation 4 – Monitor fraud response mechanisms to ensure they are consistently applied

(a) The Commission accepts this recommendation.

The CPR proposal for post 2020 provides the legal basis for the reporting of irregularities. The implementing provisions will take into account the definition of fraud in the PIF Directive.

The managing authorities' prime responsibility with regard to suspected fraud is to report such cases to the national bodies competent to investigate and to prosecute fraud. It is for OLAF, National Fraud-Investigation Bodies and national Courts to establish whether conduct was intentional and should be categorised as 'suspected fraud'.

Reporting duties are included in the 2021 – 2027 legal framework for Cohesion Funds as well. The Commission would not suggest limiting these obligations to instances in which fraud has already been identified.

(b) The Commission accepts this recommendation.

The Commission will continue to encourage Member States to systematically assess the horizontal implication of suspected fraud identified at programme level, as provided in section 4.4. of the guidance note on fraud risk assessment.

(c) The Commission accepts this recommendation.

The Commission will remind Member States about their obligation to report fraud to competent investigative authorities (see section 4.3.3 on reporting mechanisms of the 2014 Guidance on fraud risk assessment and effective and proportionate anti-fraud measures).

The Regulation establishing the EPPO already provides a reporting duty for all competent authorities (Article 24), and this will include managing authorities when the EPPO has been set up (by November 2020 at the earliest).

Last alinea: **The Commission notes that this recommendation is addressed to the Member States.**

The Commission agrees that effective recovery from perpetrators is part of the deterrent effect of measures taken.

90. The Commission will carefully assess any amendment of this kind put forward by the co-legislators.

91. According to the current provisions of Regulation 883/2013, the role of AFCOSs is to facilitate effective cooperation and exchange of information with OLAF. However, the organisation and powers of AFCOSs is left for the decision of each Member State. Thus, their set-up differs across the Member States, not least because of different national systems, and the effectiveness of AFCOSs is sometimes affected by the limited powers and resources that some Member States grant to them.

The Commission issued a guidance note in 2013 to assist the Member States in setting up their AFCOSs, outlining a potentially broader role for AFCOS, but this document had no binding effect.

The evaluation of the OLAF Regulation showed that the creation of the AFCOSs had brought about a clear improvement in the cooperation and exchange of information between OLAF and the Member States, but it also identified room for further improvement. While the diversity of AFCOSs was acknowledged, there were diverging views (notably among the AFCOSs themselves) on the need to further align their role and powers.

The Commission's proposal to amend OLAF Regulation clarifies the responsibilities of AFCOS as regards providing assistance to OLAF; to this end, it provides for an obligation of result on AFCOS, while abstaining from harmonisation of their organisation and powers by way of introducing minimum functions. In addition, the proposal also provides for a legal basis for horizontal cooperation between AFCOS.

The Commission agrees that good coordination among the Member State's authorities is vital for successful fight against fraud.

Recommendation 5 – Support expansion of the AFCOSs' functions to improve coordination

The Commission accepts this recommendation.

The AFCOSs have a general role to support OLAF's investigations in the Member State, and this task can indeed require liaising between and coordination with managing authorities and other Member State bodies involved in the fight against fraud. Therefore, this is already now part of the role of the AFCOSs, and the Commission will continue encouraging the Member States' AFCOSs to expand their network. The AFCOSs are best placed to determine the authorities concerned, which could be many and vary from Member State to Member State.

92. The Commission agrees with the ECA on the importance of ensuring the effectiveness of the AFCOS and could support a clearer definition of the functions of AFCOS.

The Commission's proposal to amend the OLAF Regulation, however, leaves unchanged the general principle that the organisation and tasks of AFCOS should be determined by national law. The scope of Regulation 883/2013 is limited to the investigative mandate of OLAF and therefore, as regards the role of AFCOS, it focuses on the support that AFCOS should provide to OLAF in exercising this mandate. While abstaining from any harmonisation, the proposal stipulates that AFCOS should either "provide" or "obtain" the assistance required by OLAF (an obligation of result on the AFCOS). Therefore, the Commission proposal represents already a significant improvement over the current situation, as the AFCOS would need to ensure that assistance to OLAF is provided, regardless of whether assistance is directly provided by the AFCOS, or by a different authority acting on the AFCOS' request).

Audit team

The ECA's special reports set out the results of its audits of EU policies and programmes, or of management-related topics from specific budgetary areas. The ECA selects and designs these audit tasks to be of maximum impact by considering the risks to performance or compliance, the level of income or spending involved, forthcoming developments and political and public interest.

This performance audit was carried out by Audit Chamber II: Investment for cohesion, growth and inclusion spending areas, which is headed by ECA Member Iliana Ivanova. The audit was led by ECA Member Henri Grethen, supported by Ildikó Preiss, Private Office Attaché; Juan Ignacio González Bastero, Principal Manager; Jorge Guevara López, Head of Task (CFE); Dana Christina Ionita, Sandra Dreimane (CFE), Florence Fornaroli, Efstratios Varetidis, Márton Baranyi, Zhivka Kalaydzhieva, and Janka Nagy-Babos Auditors. Thomas Everett provided linguistic support.



From left to right: Márton Baranyi, Thomas Everett, Efstratios Varetidis, Henri Grethen, Ildikó Preiss, Dana Christina Ionita, Juan Ignacio González Bastero, Janka Nagy-Babos, Jorge Guevara López, Florence Fornaroli, Sandra Dreimane.

Event	Date
Adoption of Audit Planning Memorandum (APM) / Start of audit	10.1.2018
Official sending of draft report to Commission (or other auditee)	23.1.2019
Adoption of the final report after the adversarial procedure	27.3.2019
Commission's (or other auditee's) official replies received in all languages	6.5.2019

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The Commission and the Member States share the responsibility to counter fraud and any other illegal activities affecting the EU's financial interests. In the field of EU cohesion policy, where there is a significant incidence of reported fraud compared to other spending areas, the bodies in the front line of the fight against fraud are the Member State authorities responsible for managing EU programmes.

In this audit, we assessed whether managing authorities have properly fulfilled their responsibilities at each stage of the anti-fraud management process: fraud prevention, fraud detection and fraud response.

We found that managing authorities have improved the way they assess fraud risks and design preventive measures, but they still need to strengthen fraud detection, response and coordination among different Member State bodies. In particular, they have made no significant progress towards proactive fraud detection and the use of data analytics tools. Managing authorities under-report fraud cases to the Commission, which affects the reliability of published fraud detection rates. Deterrence is limited to the threat of withdrawing EU funding, with no other dissuasive penalties or sanctions. Moreover, suspicions of fraud are not systematically communicated to investigation or prosecution bodies.



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