

THE FIGHT AGAINST FRAUD AND TAX EVASION IN THE EUROPEAN UNION. THE PROTECTION OF COMMUNITY FINANCIAL INTERESTS IN ROMANIA

*Stela Aurelia Toader¹
Mihai Aristotel Ungureanu²
Iuliana Predescu³
Antoni Predescu⁴*

ABSTRACT: The European Union budget is financed by taxes paid by European taxpayers and serves for the development of projects of common interest. The European Community and its Member States attach great importance to its protection, both in terms of proper collection of taxes and duties and also in terms of proper use of appropriations. This is one of the priorities of the institutions involved, as an obligation imposed by the Treaty establishing the European Community. The protection of European Union financial interests involve the detection, control and effective monitoring of fraud and any other illegal acts which result from the misuse of EU funds and thus prejudicing the Community budget. Cooperation between national authorities and between them and EU institutions is a prerequisite for successful fight against fraud. In Romania, national coordinator of the fight against fraud, with responsibilities in control line use of community funds is European Anti-Fraud Office (OLAF).

Key words: OLAF, DLAF, European funds, fraud

JEL codes: F36, F39, F55, G28, H26, H87

General considerations on the need to combat tax fraud and other irregularities that may affect the financial interests of the European Communities

Romania's integration into the European Union has made fighting domestic tax fraud a domain of comunitary interest and this because, today, domestic tax fraud affects not only the national public budget, but also the Community, taking into account the own resources system which provides funds for the EU budget, introduced in 1970, includes four categories of financial resources namely: agricultural levies, customs duties, VAT resources and own resources taken from the gross national product.

Community institutions attach great importance to the protection of the Communities financial and economic interests and to the fight against Transnational Organized Crime, fraud, corruption and any other illegal activity that may affect the Community budget. The protection of Community financial interests concerns the proper collection of taxes and duties and the proper use of EU budget appropriations.

The wide interest at the European level in preventing and combating fraud and tax evasion practices, result not only from budgetary losses they incur but also from the distortions they cause to the movement of capital and competitive conditions, affecting, thus, common market functioning.

¹ Romanian-American University

² Romanian-American University

³ Romanian-American University, iulianapredescu@yahoo.com

⁴ "Spiru Haret" University

The prevention and fighting fraud and tax evasion requires close cooperation between tax administrations of the community, in accordance with the common principles and rules, national measures not being sufficient since their effect does not go beyond national borders.

Consequently, the Treaty of the European Union calls on the Commission and Member States to coordinate measures in order to protect the EU budget and to combat fraud and other illegal activities affecting it. Thus, Member States should be as rigorous in protecting the EU budget as in controlling expenditure and income of their national budgets.

In areas where Member States implement the budget and in order to collect the Community own resources, legislation requires Member States to notify suspected fraud and other irregularities affecting the Communities' financial interests.

It is important to distinguish between fraud and other irregularities. An *irregularity* is any infringement of Community provisions by an operator who can or might prejudice the Communities' financial interests. *Fraud* is an irregularity committed intentionally, which constitutes a criminal offense. Member States shall identify among the communicated the deficiencies those who are suspected of fraud. Real financial impact of fraud can not be measured until after the court proceedings.

Table no.1 contains centralized statistics on fraud and other irregularities found by the Commission departments in budgetary areas that are subject to centrally direct management.

Table no.1

Irregularities number and their values-the years 2007 and 2008

Domain	Number of irregularities reported		Estimated total financial impact of irregularities, including suspected fraud (million)	
	2007	2008	2007	2008
<i>Agriculture (EAGGF and EAFRD)</i>	1.548	1.133	155	102,3
<i>Structural and Cohesion Fund</i>	3.756	4.007	804	585,2
<i>Pre-accession funds</i>	332	523	32	61
<i>Direct Expenditure</i>	411	932	33	34,7
<i>Total expenditure</i>	6.047	6.595	1.024	783,2
<i>Own resources</i>	6.097	5.344	401	351

2008 Annual Report of the European Parliament and Council on the protection of the Communities' financial interests - Fight against fraud

Overall statistics for 2008 shows that the number of irregularities increased for structural funds and cohesion funds, pre-accession funds and direct expenditures. Total expenditures irregularities increased from 6047 in 2007 to 6595 in 2008.

For the traditional own resources domain (Customs duties and agricultural levies), the number of irregularities decreased by approximately 12% from 6097, in 2007, to 5344 in 2008, just as the financial impact that decreased from 401 million Euros in 2007, at 351 million Euros in 2008.

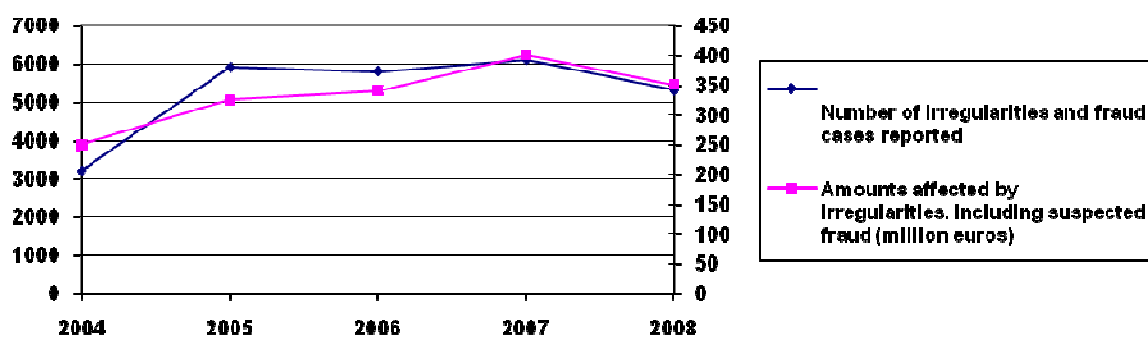


Figure no.1 - Number of irregularities reported and estimated financial impact - traditional own resources (2004-2008)

Suspensions of fraud is found in about 20% of irregularities cases reported, giving an estimated financial impact of 75 million Euros, or about 0.46% of total own resources in 2008 (compared to 130.78 million Euros, approximately 0, 81% in 2007).

The affected products were, as in previous years, televisions and monitors. The most common deficiencies were false declaration (wrong description, wrong value, origin and preferential arrangements) and omissions of the form (obligation and commitment failures). In the second position was located the tobacco. The clothing sector increased in importance, as well as the one of machinery, plastic and beef, while (parts of) the cars and motorcycles sector remained relatively stable.

European legal regulations aimed to protect the financial interests of the Community

At European level is deemed that effective fight against fraud affecting the Communities' financial interests requires a common legal framework for all areas covered by Community policies.

European Union considers the prevention of tax evasion as a separate section of the chapter on taxation, apart from general principles, direct taxation, indirect taxation and other taxes.

1. Exchange of information

In accordance with 77/799/EEC Directive [3], authorities of the Member States shall exchange any information that may allow a correct assessment of income taxes and taxes on capital, being understood by it all taxes on total income, on total capital, including taxes on gains from disposal of movable or immovable property, taxes on wages paid by companies and capital charges.

Information sharing can be achieved:

- On request;
- Automatically, regularly, without a prior request;
- Spontaneously, without prior request.

A. Exchange of information on request

Under Article 2 (1) of the 77/799/EEC Directive, the competent authority of a Member State may request the competent authority of another Member State to submit information in order to enable a correct assessment of taxes on income and capital taxes. The competent authority of the requested State is not required to answer the request if the competent authority of the requesting State has not exhausted its sources of information that could be used, in those circumstances, to obtain the required information without the risk of endangering the result sought.

B. Automatic exchange of information

Occurs when the consultation procedure, on bilateral problems, between the competent authorities of the Member States concerned, or between the competent authorities of all Member States and Commission, to the extent that problems are not solely of bilateral interest.

C. Spontaneously exchange of information

Takes place in the following situations:

- authority of a Member State has grounds for supposing that there may be losses of tax in another Member State;→
- a taxpayer get a reduction or exemption from tax in a Member State which may cause an increase in tax or a liability to tax in another Member State;
- business between a taxpayer in a Member State with a taxable person in another Member State are conducted through one or more countries so as to result in a reduction of taxes in one or the other Member State or in both;
- authority of a Member State has grounds for supposing that there is a saving of tax, from artificial transfers of profits within groups of enterprises;
- information submitted by a Member State, by the competent authority of another Member State, allowed obtaining information that may be relevant in assessing liability to tax in the other state.

Information disclosed to a Member State shall be confidential in that State, as well as information received under law. These can be made available only to those directly involved in the assessment of taxes or administrative control of the evaluation. If the authority of the Member State providing the information agrees, the information may be disclosed during public hearings or in judgments.

In all cases, the limits of privacy are established by legislation or administrative practice of each Member State, it may refuse to exchange information if the State concerned does not agree to respect the limits of confidentiality.

If a competent authority of a Member State considers that the information received from the competent authority of another Member State may be relevant to a competent authority of a third Member State may transmit it to the latter competent authority with the permission of the one that provided the information.

Requested Member State shall not be required to undertake research or to provide information if it is hindered by national laws, regulations or administrative practices, to collect or use information for its own purposes.

The requested Member State is not required to provide information if it leads to the disclosure of a trade, industrial or professional secret or if it disclosure is contrary to public policy.

The requested Member State may refuse to provide information if the State concerned can not provide for legal or practical reasons, similar information.

2. Compliance with legality and reality monitoring of transactions involving financial interests of the Community

In accordance with rules, regulations and administrative provisions of national law, Member States shall take the measures necessary to ensure the operations legality and veracity involving the Community financial interests.

Control measures must take into account the existing administrative structures and practices in Member States and be set in a manner that does not lead to constraints or excessive administrative costs.

Controls ordered by the European Commission target:

- The conformity of administrative practices with Community rules;
- The existence of the necessary supporting documents and their concordance with the incomes and expenditures of the Communities;
- Circumstances in which these financial operations are carried out and audited.

In order to protect the financial interests of the European Communities, EC Regulation nr.2185/1996 [2], the European Commission may conduct controls and inspections on-site in the Member States, in one of the following situations:

- for the detection of serious or transnational irregularities that may involve businesses operating in several Member States, or;

- when, for the detection of irregularities, the situation in a Member State needs to strengthen controls and inspections, in some cases to improve the protection effectiveness of the financial interests and so to ensure an equivalent level of protection within the Community, or;
- at the request of the Member State concerned.

Spot checks and inspections are prepared and conducted by the Commission in close cooperation with the competent authorities of the Member State concerned, which shall be notified in time on the subject, purpose and legal basis of controls and inspections, so that it can provide any assistance that is necessary. Officials of the Member State may also participate on the on-site controls and inspections.

Over controlled entities can be taken administrative measures and sanctions (Article 7, Regulation 2988/95) where there is reason to believe that irregularities have been committed.

Commission inspectors must have access to the same conditions as national administrative inspectors and in accordance with national law, to all information and documentation on the operations concerned which are required to properly perform on-site controls and inspections. They can use the same facilities as national administrative inspectors and they especially can copy relevant documents.

On-site controls and inspections may concern, in particular:

- Professional books and documents such as invoices, lists of terms and conditions, pay checks, statements of materials used and work done, and bank statements of economic agents;
- Computer data;
- Systems and methods of production, packing and shipping;
- Physical checks as to the nature and quantity of goods or completed operations;
- Collection and checking of samples;
- Progress of works and investments for which financing was provided, and how they were used to investments made;
- Budgetary and accounting documents;
- Financial and technical implementation of subsidized projects.

Information obtained from controls and on-site inspections are reported to the competent authorities of the state of the control. It may not be communicated to persons other than those of the Community institutions or Member States who needs to know because their administrative positions, nor can they be used by Community institutions for purposes other than to ensure effective protection of the Communities' financial interests in all Member States.

Deviations from Community law and administrative penalties

European legislation [1] defines deviations from Community law, which may harm the financial interests of the European Communities and administrative measures and sanctions to punish them.

So, is considered misconduct any breach of a Community law provision resulting from an act or omission of a trader, who can or may harm the general budget of the Communities or budgets managed by them, either by reducing or losing revenue accruing from own resources collected directly on behalf of the Communities or by undue expenses.

Any deviation involves withdrawal of an unfair advantage:

- ✓ The obligation to pay due amounts or to repay amounts wrongly received;
- ✓ The total or partially loss of the provided guaranty for the application for a granted advantage or when receiving a receipt of an advance.

For irregularities committed intentionally or negligently the following administrative sanctions shall apply:

- Payment of an administrative fine.
- Payment of a sum greater than the amounts wrongly received or evaded, are added to the interest, if any. Interest is calculated as a percentage determined by specific rules and not exceeds what is strictly required to constitute a deterrent.

- Total or partial removal of an advantage granted by the European Union rules, even if the operator wrongly benefited from only a part of the advantage.
- Exclusion or withdrawal of a benefit to a subsequent period of the misconduct.
- The temporary withdrawal of approval or recognition necessary for participation in a Community aid scheme.
- Loss of a security or deposit provided to comply with conditions laid down by rules or to reconstitute a security issued wrongly.
- Other purely economic penalties with equivalent nature and scope.

Community administrative measures and penalties may be applied to the economic (persons or entities on which national law confers legal capacity), and to those forced to take responsibility for any deviation or to ensure that it is not committed.

The European Anti-Fraud Office

Protecting Communities' financial interests and fighting against fraud and other illegal activities detrimental to the Communities' financial interests are primary objectives of the European Union fiscal policy, which set up a specialist European Commission structure - **European Anti-Fraud Office (OLAF)** [4].

OLAF began its work on June 1st, 1999 and its task was to conduct investigations on cases of fraud. Despite its status as an independent body in conducting investigations, OLAF is part of the organizational structure of the European Commission, being subordinate to the Commissioner responsible for European Union budget.

OLAF exercise all the Commission's attributes in making administrative investigations in order to intensify the fight against fraud, corruption and other illegal activities in a manner adversely affecting the Community financial interests, but also against any act or activity contrary to the provisions of the Community.

The Office is empowered to make fully independent:

- Internal investigation, in any institution or body within the European Union budget financed area. Thus, the Office investigates serious facts linked to professional activities that may constitute a breach of obligations by officials and other servants of the Communities.
- External investigation, i.e. national, whenever the EU budget is involved. To this end, OLAF may carry out controls and inspections at the premises of economic operators, in close collaboration with the competent authorities of the Member State or third country.

Thus, OLAF activities focus on the detection and monitoring of customs fraud, near fraudulent grants and tax evasion, if the Community budget is affected, as well as on fight against corruption and other illegal activities damaging the Community financial interests.

The Office provides Member States with assistance from the Commission in order to organize a close and regular cooperation between their competent authorities, to coordinate their activities to protect the financial interests of the European Community. Furthermore, OLAF contributes to the design and development of methods of fighting fraud and any other illegal activity affecting the financial interests of the European Community.

At the conclusion of an investigation of the Office, it will be drafted a report, under the authority of the Director, maintaining established facts, financial loss, if any, and findings of the investigation, including Office's Director recommendations on measures to be taken. In drawing up such reports are considered procedural requirements stipulated by the national law of that Member State. Reports prepared on this basis shall constitute admissible evidence in administrative or judicial authorities of the Member State in which their use proves necessary, in the same manner and under the same conditions as administrative reports drawn up by national administrative inspectors.

Reports drawn up following an external investigation and any other useful related information are submitted to the competent authorities of the Member States concerned, in accordance with the rules relating to foreign investments.

In late 2008 there were 425 active cases of OLAF investigations, of which 351 in European Union countries and candidate countries. A significant proportion of these relate to a small number of countries: about 55% of active investigations in the European Union target about 6 Member States (Belgium, Bulgaria, Italy, Germany, Romania and United Kingdom). This does not necessarily mean that in the countries with highest number of OLAF investigations occurs more fraud, as better cooperation with local authorities can also lead to the automatic transmission to a greater number of official cases [7]. However, you may observe among the above 6 countries, European Union member states with the highest level of tax evasion (Italy, Romania, Bulgaria).

Protecting the financial interests of the European Union in Romania

The European Commission has encouraged candidate countries to designate a contact institution with the European Anti-Fraud Office - OLAF, in order to coordinate national anti-fraud and to protect Community financial interests.

In Romania, the national coordinator structure of the fight against fraud, with responsibilities of community funds usage control is the Anti-Fraud Fight Department (in Romanian DLAF). It was founded on June 1st, 2005, as an integrant part the Chancellery of the Prime Minister.

Now, DLAF is the institution in contact with the European Anti-Fraud Office (OLAF) and Anti-Fraud Coordination Service in Romania (AFCOS).

DLAF has the status of finding body on possible fraud affecting European Union financial interests, records of concluded control constitute evidence in criminal trials. Also, Anti-Fraud Department is the institution responsible for coordinating implementation of the *National Strategy for European Union's financial interests Anti-Fraud Protection in Romania* and it's action plan.

Anti-Fraud Department - DLAF consists of 3 departments, under the coordination of the Head of DLAF.

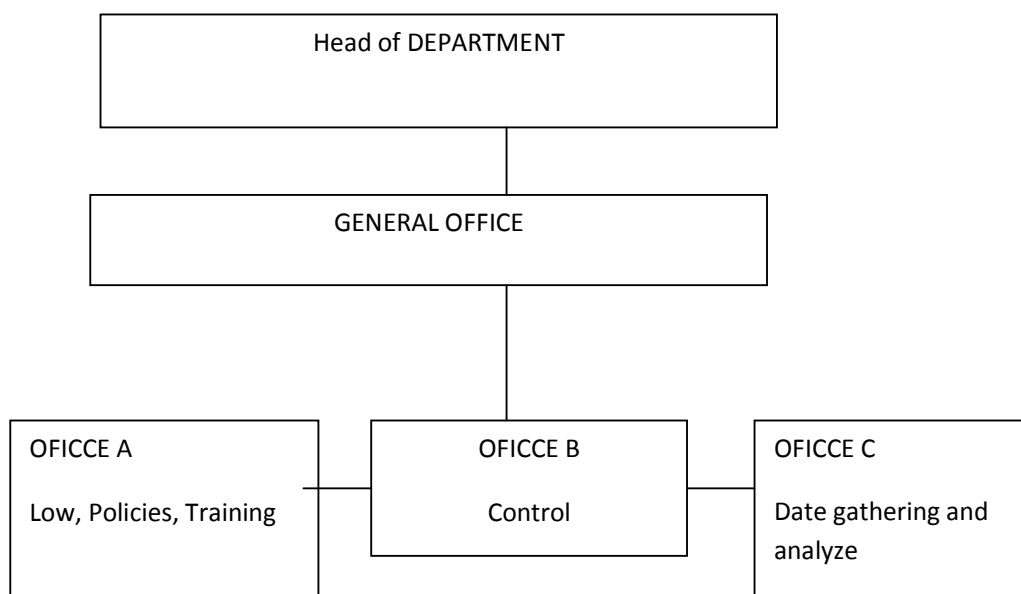


Figure no. 2 - The structure of the Department of Anti-Fraud

In order to accomplish its task, DLAF developed the coordination anti-fraud system, which cover both operational coordination of institutions involved in the field of protecting European Union financial interests, the business of collecting and analyzing data, training of personnel involved in the fight against fraud, as well as coordinating the work public relations.

Operational coordination is based on cooperation protocols closed between DLAF and institutions involved in the field of protecting EU financial interests. They seek both to inform DLAF about any irregularity or fraud detected in the control activity specific for every institutions, as well as providing operational support for control actions of DLAF.

Nationally, an important role in coordinating the fight against fraud detain the 3 network set up by DLAF: the Network Reporting Irregularities, the Network of Training Coordinators and the Anti-Fraud Communicators Network.

An important role, in coordinating the activities of public relation, plays the Anti-Fraud Communicators Network. Founded in 2005, the Network activity is based on 12 protocols of cooperation agreements between DLAF and institutions concerned with the protection of Community's financial interests in Romania (National Agency for Community Programs in Education and Training, Ministry of European Integration, Financial Guard, Romanian General Police Inspectorate, National Motorways and National Roads in Romania, Payment Agency for Rural Development and Fisheries, National Railway Company "CFR" SA, Ministry of Transport, Ministry of Finance, the Public Prosecutor of the High Court of Cassation and Justice, the National Anti-Corruption Agency for Payments and Intervention in Agriculture).

In operational terms, the main tasks of DLAF, conducted by the Directorate of Control DLAF, aims:

a. control of projects financed from European funds

DLAF carry out operative controls on-site following complaints received from OLAF, competent authorities in the management of Community financial assistance or ex officio. In exercising these powers, DLAF investigators:

- Unconditional access to premises, land, means of transport or other facilities used for business purposes;
- Take statements from perpetrators and witnesses who were present when committing a crime;
- Can prepare minutes on the actual circumstances of its perpetration;
- May hold the corpus delicti.

Financial and fiscal control bodies, as well the police and gendarmerie are required to provide operational support team in order to DLAF exercise its control.

In the event of such criminal elements in the management of European Union funds, control notes will be submitted to the National Anticorruption Department (DNA).

b. coordinating all national institutions involved in the fight against fraud

The Anti-Fraud Department provide operational coordination at national level by conducting inspections in cooperation with representatives of tax police financial control bodies, police force or other public servants. At the request of DLAF, operational support is granted to the control team based on collaboration protocols. In such situations, the control action takes place in mixed teams, under the direction of a representative DLAF, each participating institution to control having the obligation to verify all required aspects of the investigation.

So far, representatives of the Financial Guard participated in 26 DLAF controls and representatives of the Romanian General Police Inspectorate in 13 cases. There was a control in collaboration with the National Customs Authority based on a protocol signed with the National Tax Administration Agency. In 9 cases, DLAF received specialized technical assistance from the State Construction Inspectorate. In the interest of criminal investigations conducted in some cases of crimes against financial interests of the European Union and the good cooperation between the two institutions, DLAF conducted 7 inspections at the request of the National Anticorruption Directorate, all of them being labeled as fraud [8].

c. cooperation with the European Anti Fraud Office and corresponding structures of the Member States of the European Union

As an institution of contact with OLAF, the Anti-Fraud Department carries out common on-site controls in mixed teams, requires technical expertise of OLAF employees and facilitates requests for technical assistance by OLAF to the national institutions.

Also in the Financing Memorandum and Agreements related to the PHARE, ISPA and SAPARD and EU, as well as comunitary regulations governing the financial assistance of EU Member States, Romania has the obligation of reporting irregularities to the European Commission. Nationally, DLAF is responsible for reporting irregularities to the European Commission - OLAF for the entire financial grants for Romania.

At operational level, Anti-Fraud Department:

- OLAF receives complaints about possible irregularities affecting the financial interests of the European Union and appropriate controls;
- Makes available to the Office the control documents containing its findings and all data and information required;
- Carries out joint inspections conducted on-site in mixed teams with OLAF investigators;
- Request technical assistance form OLAF experts;
- Facilitate technical assistance requests made by national institutions to OLAF.

In May 2006, Romania became the first Member or acceding State that held common on-site controls, in mixed teams with OLAF [8].

OLAF investigators conducted together with representatives of DLAF, so far, 4 Common Controls on-site, of which 3 were completed with findings of possible fraud, while one is still in process. For completed cases, both DLAF investigators and OLAF representatives established control reports, which were submitted to the National Anticorruption Directorate and to the Ministry of European Integration.

OLAF referrals were valorized by DLAF controls, to this date 18 of the actions being initiated upon referral by the Department of European institution. Of these, 15 cases were identified as possible fraud, control notes being submitted to competent prosecutor, and in 2 cases the referred issues has not been confirmed.

DLAF regularly inform OLAF of cases that are identified as possible fraud.

Given the complexity of some checked DLAF projects and the involvement of many operators in the EU space, OLAF has given technical assistance by providing information on companies and consortia of Member States as United Kingdom, France, Germany or Italy. Through OLAF has been verified their ownership structure, the authenticity of documents and links with Romanian businesses. This information contributed to the settlement of 18 cases.

DLAF also eased transmission to OLAF of 4 requests for technical assistance, 2 belonging to the General Inspectorate of Romanian Police and other to National Customs Authority.

The 8 operational meetings that were held between OLAF and DLAF investigators have attempted to address requests for technical assistance and to carrying out checks in some cases in development.

According DLAF 2008 report [6], the main types of fraud / irregularities identified during controls carried out by DLAF were:

- Use of false or forged documents, statements or tax certificates (50%);
- Use of incorrect and incomplete documentation (29%);
- Violating conditions of eligibility (21%).

A common method of fraud in 2008 was the simulation auction proceeding by the beneficiaries, in order to purchase their own machinery-equipment. Also were found instances of collusion between applicants for European funding and local representatives of tax offices, materialized by issuing attesting false tax certificates, used to prove eligibility.

In 2008, DLAF initiated 129 control actions, with a growing volume of operational activity of 26% over the previous year. Of these 106 were completed, 84 confirmed and 22 unconfirmed. Of

the 84 cases confirmed, ascertaining the situation is the following: evidence of fraud in 14 cases, irregularities in 18 cases, evidence of fraud and irregularities in 52 cases.

Following checks by DLAF were recovered debts in the amount of approximately 4.5 million Euros, of which about 1 million in 2008.

The Activity Report of OLAF [9] recorded very good cooperation with the Romanian authorities. OLAF emphasizes that the number of controls the opened in Romania is determined by the very large volume of funds allocated, and the degree of involvement and efficiency of the Romanian authorities to uncover cases of fraud.

Conclusions

OLAF achieves its mission by conducting, in full independence, internal and external investigations, it also organises close and regular cooperation between the competent authorities of the Member States in order to coordinate their activities and by doing so protect the financial interest of the European Union.

In recent years we can see an increase in OLAF rol, as well as in it's carried out activites that makes us belive that the frauds intesified or that the anti-fraud fight intesified. The wide interest at the European level in preventing and combating fraud and tax evasion practices, result not only from budgetary losses they incur but also from the distortions they cause to the movement of capital and competitive conditions, affecting, thus, common market functioning. The prevention and fighting fraud and tax evasion requires close cooperation between tax administrations of the community, in accordance with the common principles and rules, national measures not being sufficient since their effect does not go beyond national borders.

References

1. Regulation (EC, Euratom). 2988/95 of 18 December 1995 on the protection of the European Communities
2. Regulation (Euratom, EC). 2185/96 on controls and inspections carried out by the Commission in order to protect the European Communities' financial interests against fraud and other irregularities
3. Council Directive 77/799/EEC concerning mutual assistance of the competent Member States authorities in the field of direct taxation
4. European Commission Decision, 1999/352/EC of 28 April 1999 to set-up the European Anti-Fraud Office (OLAF)
5. 2008 Annual Report of the European Parliament and Council on the protection of the Communities' financial interests - Fight against fraud
6. DLAF Activity Report for 01.01.2008-31.12.2008, www.antifrauda.gov.ro
7. European Anti-Fraud Office, Annual Report 2009, www.europa.eu
8. Anti-Fraud Department website www.antifrauda.gov.ro
9. 2007 Annual Activity Report of the European Anti-Fraud Office, www.europa.eu