

Risks of Fraud in the Absorption of Funds from the European Regional Development Fund

2.



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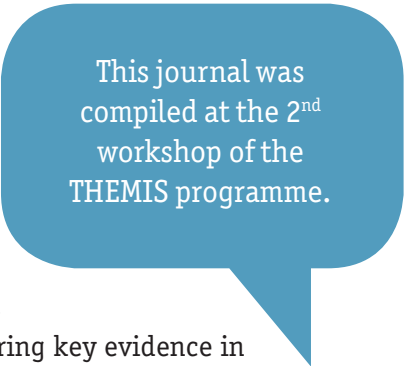
Foreword

This is a collection of papers presented at the 2nd workshop of the THEMIS programme, which is intended to provide training for crime investigators, prosecutors, judges, and other interested parties fighting fraud which is to the detriment of the European Union. Since these criminal offences are highly complex in terms of prevention, detection, investigation and prosecution, it is essential that all the authorities within this chain remain utterly professional and consistent in their approach to the task. The key factor in combating EU fraud is co-operation between competent authorities, enabling quicker detection of fraudulent behaviour and facilitating further action by those authorities.

Our previous experience in investigating criminal offences of fraud against the European Union has led to the conclusion that large amounts of available funds are provided by the European Regional Development Fund (hereinafter: ERDF), and that in certain cases these funds have been misused in the past. On the one hand such misuse has caused considerable material damage to the Fund, whilst on the other it has granted property benefits to certain individuals. In light of the above, the proceedings open with a description of control mechanisms applied by the Republic of Slovenia Budget Supervision Office, as the authority which supervises the use of national funds and funds acquired from the European Union. It continues with a presentation of the ERDF, in which fraud relating to construction of tourist facilities has been detected in the past. The next paper describes a case study based on an investigation of fraud to the detriment of the European Union and outlines the specifics observed by the investigators. The workshop proceedings also show why the offence of fraud to the detriment of the European Union was criminalised in the first place, specifies the characteristics of investigating such cases and describes the existing case law. The collection of papers ends with a description of

risks related to the corruption of foreign public officials, who are particularly exposed to bribery in the process of awarding certain funds to Member States.

It is our wish that this collection of papers will be used as a tool in investigations of fraud to the detriment of the European Union, since it contains the roles of certain authorities participating in the field of European funds. It also presents two case studies presented by the Police and the State Prosecutor's Office, which can be used as a reference for acquiring key evidence in pre-trial procedures, testifying to the existence of *dolus coloratus*.



This journal was
compiled at the 2nd
workshop of the
THEMIS programme.

David Smolej
Editor

Control over the use of European funds

Nataša Prah

The Republic of Slovenia Budget Supervision Office (hereinafter: BSO) is a body within the Ministry of Finance, which was founded in 2004 with the aim of carrying out various forms of control over budget funds. The competences of the BSO are defined by the Public Finance Act. Control tasks performed by the BSO refer to the internal supervision of public finance (internal controls and audits), budgetary inspections and external auditing (auditing of systems and expenditure financed by the European Union). The Republic of Slovenia has in place a decentralised system of internal control of public finances, based on the following:

- the responsibility of the management of budget spending centres to establish a system of internal controls and ensure internal auditing,
- functionally and organisationally independent functions of internal auditing and
- a central institution for the development, harmonisation and co-ordination of the system of internal control of public finances.

The control tasks performed by the BSO refer to the internal control of public finance.

It includes the control of all activities connected with public finances and is implemented via a system of internal controls and internal auditing. The system of internal controls is an integral part of the management function, intended for the protection of the corporate and financial integrity of a budget spending centre. Furthermore, the system of internal controls presents the measures and acts

undertaken by the management in order to mitigate risks at an acceptable level and accomplish its set objectives. Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve the operations of a budget spending centre. It helps an organisation mitigate its risks and accomplish its objectives by bringing a systematic, disciplined approach for evaluating and improving the operations and effectiveness of internal controls.

Budgetary inspections are, as previously mentioned, an important part of the BSO. Clients who are subject to an inspection control procedure include direct budget spending centres, indirect budget spending centres and other recipients of budgetary funds. The budgetary inspection's tasks relating to budget supervision are the performance of inspection checks against annual work plans, handling of complaints, requests and other applications, and notification of clients on the measures adopted. Complaints may be made by any person, legal entity or any other competent body, and inspection control in a reported case is initiated upon the existence of a suspicion or a real possibility of irregularities regarding the use of budgetary funds. External auditing is one of the main tasks of the BSO. External auditing is carried out by external auditors whose tasks are, similar to other audit authorities, laid down in the European regulations. External auditing is auditing of the use of funds received from all funds for which Slovenia is eligible, and which are approved on the basis of shared management. These include agricultural funds, the fisheries fund, structural funds, the cohesion fund and solidarities and migration funds. After carrying out the audits, the BSO prepares an audit report and annual control report and submits them to the European Commission.

The BSO is also responsible for co-ordination with the European Anti-Fraud Office (hereinafter: OLAF), since it operates a contact point for the Anti-Fraud Co-ordination Service (hereinafter: AFCOS), which presides over the multi-sectoral action group. The task of AFCOS is to

identify potential deficiencies in the management and control systems of the EU funds, launch initiatives for the required legal or organisational amendments with a view to improving the protection of the EU's financial interests, and notify authorities and organisations which are responsible for managing EU funds, both in terms of revenue as well as expenditure. Another task of the AFCOS contact point is to work together with OLAF in the implementation of specific training programmes. The operational activities of the BSO include reporting irregularities to OLAF, consolidating irregularities reports, and participating in OLAF's investigations in Slovenia. The BSO also deals with consulting and international activities, which take the form of preparation of positions and processing of documents by the competent authorities of the Republic of Slovenia and the European Union, as well as co-ordination of access to treaties and of implementation of the EU's regulations into the national legal order.

European Regional Development Fund

Tea Pirih

The aim of the Ministry of Economic Development and Technology for the upcoming programming period is to support further enhancement of the competition of Slovenian companies and proactively change the structure of Slovenia's economy towards global economic trends. The areas in which the Ministry performs these tasks are, primarily, entrepreneurship, competitiveness and technology, tourism, internationalisation and internal regional development.

One of the main sources of financing for these areas is the European Regional Development Fund (hereinafter: ERDF), as a financial instrument of the EU's Cohesion Policy, which is intended for strengthening the economic and social cohesion and providing assistance in the elimination of the most severe developmental discrepancies in the Community regions.

The ERDF funding is managed in three strands:

- convergence (technological research and development, innovation and entrepreneurial spirit),
- regional competitiveness and employment, and
- European territorial co-operation.

The areas in which the Ministry pursues these objectives are mainly entrepreneurship, competitiveness and technology, tourism, etc.

The irregularities which the Ministry of Economic Development and Technology found in the area of the ERDF in the year 2014 included mainly uneconomic management, failure to carry out activities or achieve set objec-

tives, non-earmarked use of resources and non-eligible expenditure. Further irregularities found by the Ministry were reporting and information irregularities, insufficient evidence and compensation of unverifiable content.

The difference between the old and the new financial perspectives lies in the fact that the new perspective (2014–2020) focuses on smart, sustainable and all-encompassing growth. The perspective covers 11 topical areas, e.g. research and innovation, combat against climate change, employment, and mobility. In the new perspective, the breakdown of funds follows the requirements of the regulations for focusing on key thematic objectives. In this period, one operational programme has been prepared for the ERDF, the European Social Fund and the Cohesion Fund. This operational programme is not based on a sectoral approach, and there is no priority axis for regional projects as in the previous programming period 2007–2013. Currently, there are five structural and investment funds which co-operate and supplement each other. Common provisions for the structural and investment funds are laid down in the Regulation (EC) No. 1303/2013. The Regulation newly specifies ex-ante conditionalities, which require Member States to operate suitable strategies for the areas in which they wish to invest.

Investigating suspicions of fraud to the detriment of the EU

David Antolovič

One of the most striking cases of fraud to the detriment of the European Union relating to ERDF funds in the Republic of Slovenia is the reconstruction of a 'spa'. Police received a criminal complaint against the responsible person of the 'spa' and the responsible person of the construction company 'X' for committing the criminal offence of abuse of position or trust in economic activity, which was filed with the prosecutor's office by the newly appointed management of the facility. The criminal complaint specified considerable material damage to the 'spa' company on the one hand, and property benefits to the construction company 'X' on the other, since the construction works were not performed despite the payments having been made on the basis of interim valuations.

According to the police findings, the responsible person from the 'spa' company acquired for the company, property benefits of more than EUR 3 million from the general budget of the European Union by filing, on behalf of the 'spa' company, several co-financing requests for investment in the 'spa' with the Ministry of Economic Development and Technology, made false statements concerning total expenditure for the construction project, and submitted as proof interim valuations of the construction work done, as well as fictitious proof of payment of these interim valuations. The key person in such projects is the Quantity Surveyor, who must be appointed for each construction project under the Construction Act. In this case, the authorised Quantity Surveyor made

One of the most striking cases of fraud to the detriment of the European Union related to ERDF funds in the Republic of Slovenia is the construction of a 'spa'.

a false declaration that the works specified in the false interim valuations were true and real. Additionally, the Surveyor falsely confirmed that the works were carried out in the specified quantities and that the types and quantities of works, arising from the construction log book, were carried out, although this was not the case.

In order to prove this criminal offence, it was necessary to ensure and confiscate all the submitted co-financing requests as well as the falsified evidence enclosed thereto. The main proof that the submitted interim valuations had been falsified was found in the construction log books and construction journal of the investment project.

Prosecuting cases of fraud to the detriment of the EU

Matej Mavrič

The criminal offence of ‘fraud to the detriment of the European Union’ is criminalised with the aim of safeguarding funds of the EU budget, or of the budgets managed by the European Union, or managed on its behalf. In practice, the issue refers mainly to funds acquired from the structural, cohesion and social funds and regional development fund. The criminal offence of ‘fraud to the detriment of the EU’ is perpetrated by any person who avoids expenses or acquires property benefits by way of using or submitting false, incorrect, or incomplete statements or documents, or does not reveal data, and thus, in way of engaging in an executory form of a criminal offence, misappropriates, or unlawfully withholds or uses inappropriately, funds of the general budget of the European Union, or of the budgets managed by the European Union or managed on its behalf.

One of the most notorious cases in the field of ‘fraud to the detriment of the European Union’ and absorption of ERDF funds to be prosecuted by the State Prosecutor’s Office was the case of the ‘spa’. The case was classified as a ‘substantive criminal offence’

because the entire activity of the accused was aimed at the acquisition of funds from the ERDF call (*dolus coloratus*), and because the accused were granted the funds on the basis of their request containing false information. The company facing a criminal charge acquired and used property benefits although the works were executed at a later date. In deliberating on the complaint concerning the seizure of property benefits in a material criminal case, the Higher Court found that a subsequent agree-

The request contained false statements of executed activities and expenditure, as well as two interim valuations with falsified content.

ment between the injured person and the legal entity facing the criminal charge for the early payment of works performed at a later date is a civil law matter and cannot affect the existence of a criminal offence and the nature of the property benefit acquired through such criminal offence. In this matter, a request for the protection of legality was filed with regard to the seizure of property benefits by the responsible person of the 'spa' company. The grounds of the judgement of the Supreme Court of the Republic of Slovenia disclose that the acquisition of property benefits by the legal entity is common ground, but the Supreme Court found that on account of a misinterpretation of assets that can be confiscated, the Court of First Instance failed to investigate the circumstances that could affect the value of recovered assets. For the above given reason, the Supreme Court annulled the contested judgement in the part concerning the recovery of unlawfully acquired property benefits and referred the case back to the Court of First Instance for deliberation.

Similarly, in another 'mansion' case, the co-financing request relating to the investment into the 'mansion revival' project was filed on the basis of falsified construction books. The request included false statements on the works executed and expenses made, as well as interim valuations with false content. After receiving a request for completion, two false construction log books were submitted to the Ministry. Using such documents, the defendants were able to mislead the Ministry of Economic Development and Technology into disbursing ERDF funds.

The grounds for the decision by the Higher Court in this matter disclose that in the case of the criminal offence 'fraud to the detriment of the European Union' it does not matter whether the perpetrator acquired property benefits for his/her or another person. Furthermore, the Court stressed the relevance of identification of the fact whether all the funds acquired by the company 'mansion' were from European funds. The conclusions of the case state that the Court estimates that this is a single criminal offence even in the case when the perpetrator induces two persons to commit the same criminal offence.

Corruption of foreign public officials

Romana Berčič

The Republic of Slovenia is a member of the OECD Working Group on Bribery in International Business Transactions. The Working Group has already implemented three phases of the OECD's Convention Combating Bribery of Foreign Public Officials in International Business Transactions. The fourth phase is currently in preparation. All countries need to undergo a detailed assessment carried out by at least two member states of the Working Group (the Republic of Slovenia is being assessed by Luxembourg and the Netherlands). Once a year each Working Group member state reports on active cases (with the police, state prosecutor or court) of bribery in international business transactions.


The Republic of Slovenia was criticised for not paying enough attention to combating bribery in international business transactions, as it only prosecuted four cases of foreign bribery since the Convention came into force. The OECD Convention Combating Bribery of Foreign Public Officials defines the offence of bribery of foreign public officials as containing the following elements:

- the criminal offence is intentional,
- the criminal offence is committed directly or through intermediaries,
- the criminal offence may be an act to offer, promise or give any undue pecuniary or other advantage to a foreign public official, for that official or for a third party, and
- the criminal offence is committed by an official who acts, or refrains from acting, in relation to the performance of his/her official duties, in order to obtain or retain business or improper advantage in the conduct of international business.

The Working Group's first report concerning the implementation of the Convention was adopted in February 2005, the second in June 2007, and the third in June 2014. Since 2007 the Working Group has been closely monitoring the measures of the Republic of Slovenia regarding the raising of awareness in the public and private sectors, and recommends:

- awareness-raising initiatives concerning the Convention and the criminal offence
- awareness-raising initiatives among Slovenian business associations and companies
- reminding public officials of their duty to report bribery of foreign public officials
- measures aimed at promoting the mechanisms protecting the reporters of bribery
- ukrepa v smeri promoviranja mehanizmov za zaščito prijaviteljev korupcije

Attention is also paid to the detection and prosecution of suspicions of foreign bribery, which may form part of other criminal offences, in particular those of international relevance, which often include fraud to the detriment of the European Union.



Attention is also paid to the detection and prosecution of suspicions of foreign bribery.



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