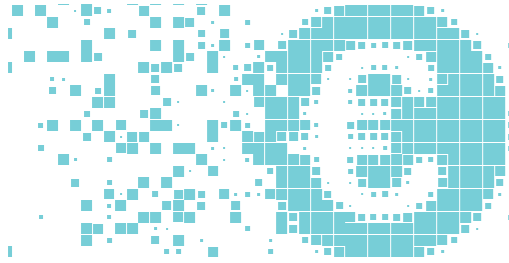




**MAPPING  
CORRUPTION SCHEMES  
INVOLVING EU FUNDS**

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The publication is based on the presentations of speakers and discussions of the conference "Mapping corruption schemes involving EU funds", organised on 26-27 April 2018 in Bucharest, Romania. The list of speakers is available at the end of the publication. Speakers were credited for their contributions in the text of the publication.

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Bucharest, December 2018

# 1. CORRUPTION AS A THREAT TO THE UNION'S FINANCIAL INTERESTS

According to the EU Directive 2017/1371, „the protection of the Union's financial interests concerns not only the management of budget appropriations, but extends to all measures which negatively affect or which threaten to negatively affect its assets and those of the Member States”.

Corruption is thus defined as a “particularly serious threat to the Union's financial interests, which can in many cases also be linked to fraudulent conduct”. Corruption breaks impartiality and objectivity principles in the exercise of public or private duties. Corruption is usually broadly defined as abuse of power for private gain<sup>1</sup> and it can take many forms from bribery to trading in influence, abuse of power, conflicts of interest, or revolving doors. Corruption is related to fraud as complex schemes of fraud at the expense of the general budget of the European Union require aid or participation of different kinds of officials involved in the management of EU funds.

Sometimes such schemes are not confined to a single country and are committed by networks of companies, organised crime, politicians and white-collars. Corruption cannot be confined as a behaviour specific to public organisations as private persons (such as contractors) are increasingly involved in the management of EU funds. Thus, public official definition by the EU Directive 2017/1371 is very board

comprising “any person assigned and exercising a public service function involving the management of or decisions concerning the Union's financial interests in Member States or third countries”.

**Passive corruption** is the action of a public official who, directly or through an intermediary, requests or receives advantages of any kind, for himself or for a third party, or accepts a promise of such an advantage, to act or to refrain from acting in accordance with his duty or in the exercise of his functions in a way which damages or is likely to damage the Union's financial interests.

**Active corruption** is the action of a person who promises, offers or gives, directly or through an intermediary, an advantage of any kind to a public official for himself or for a third party for him to act or to refrain from acting in accordance with his duty or in the exercise of his functions in a way which damages or is likely to damage the Union's financial interests.

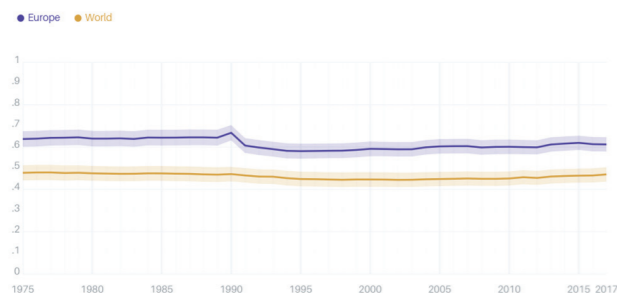
**Misappropriation** is the action of a public official who is directly or indirectly entrusted with the management of funds or assets to commit or disburse funds or appropriate or use assets contrary to the purpose for which they were intended in any way which damages the Union's financial interests

<sup>1</sup>Transparency International's definition of corruption

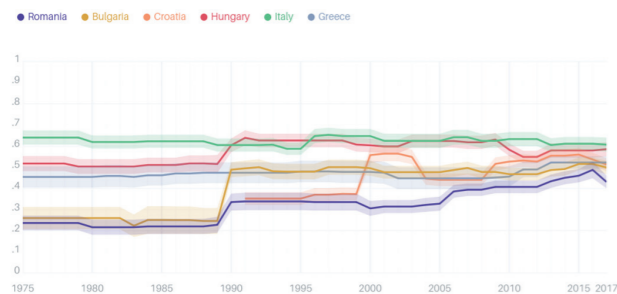
<sup>2</sup> www.idea.int

**Source:** The Global State of Democracy indices website

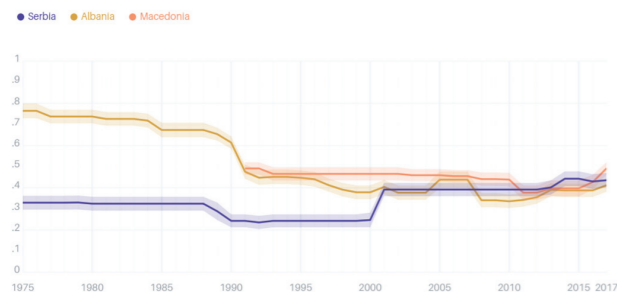
**Figure 1.** Absence of corruption attribute Europe vs. World



**Figure 2.** Comparison between Bulgaria, Croatia, Hungary and Romania



**Figure 3.** Comparison between Serbia, Albania and North Macedonia



Corruption is very hard to curb as it is deep-rooted in countries' social, political and economic system. International IDEA's new Global State of Democracy (GSoD)<sup>2</sup> report examines the global state of democracy and the challenges to democracies in 155 countries around the world, in the period 1975 - 2017.

According with GSoD, one attribute of democracy is impartial administration and one subattribute of impartial administration is absence of corruption. While analysing 1975-2017 period, GSoD finds that "corruption is as big a problem today as they were in 1975", in spite of more efforts being made to curb this development. (Figure 1). The GSoD conclusions are that implementing the rule of law in public administration is a difficult task in the short and medium terms and corruption scandals affect perceptions of democracy because they cause citizens to lose trust in politics and institutions.

While considering the Member States and candidate countries targeted by the conference, the struggle for integrity had ups and downs, corruption being as relevant as ever for these societies (Figure 2 and Figure 3). Bulgaria, Croatia, Hungary and Romania had improve their integrity performance between 1990 and 2010 but this trend seems to reverse in the last years. Italy and Greece are mostly constant during the period.

However, candidate countries present contradictory dynamics in control of corruption. While Serbia exhibits minor improvements, especially after 2000, Albania is in a constant search for equilibrium, after a major backslide during '90s. North Macedonia also has more challenges in the progress against corruption.

<sup>2</sup> www.idea.int

## 2. PROGRESS AGAINST CORRUPTION AND FRAUD

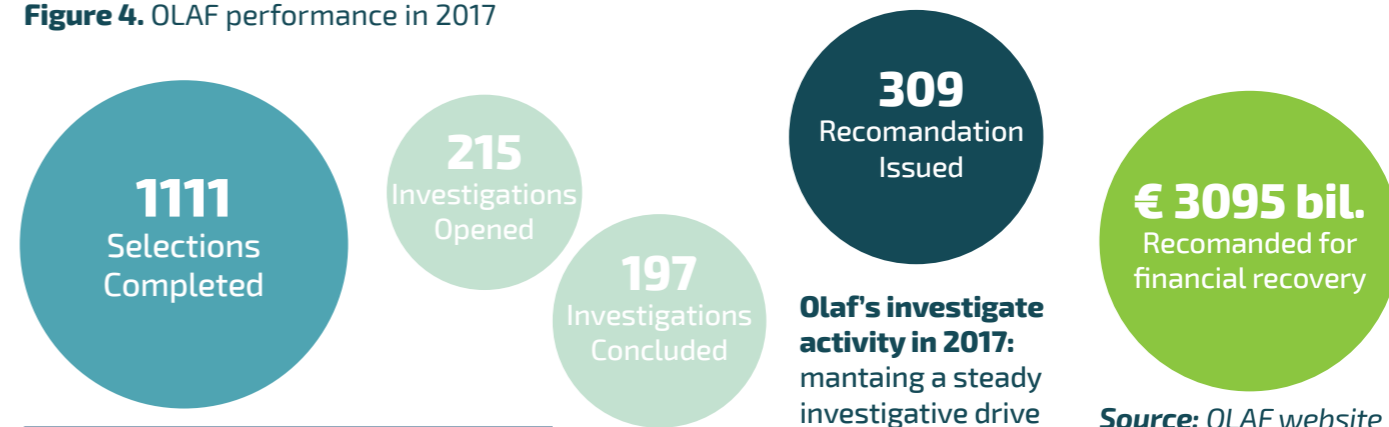
European Anti-Fraud Office (OLAF)<sup>3</sup> has the mission to detect, investigate and work towards stopping fraud with EU funds. OLAF mandate is to conduct independent investigations into fraud, corruption and irregularities involving EU funds so as to ensure that EU taxpayers' money reaches projects that can stimulate the creation of jobs and growth in Europe; to investigate serious misconduct by EU staff and members of the EU institutions, thus contributing to strengthening citizens' trust in the EU institutions; to develop EU policies to counter fraud. OLAF acts only under administrative law, its recommendations being either financial, judicial (only to national authorities) or disciplinary (only to EU institutions).

OLAF sends its reports and its recommendations to the competent authorities: national and/or EU. It

is under OLAF's remit to investigate cases of fraud and corruption involving EU funds. These can be internal cases, involving EU staff or external cases, involving EU funds. For instance, 14% of the EU GDP, about 48% of the ESI Funds, EUR 352 billion, is spent through public procurement, cases of corruption in public procurement is under OLAF's remit. European Public Prosecutor's Office (EPPO)<sup>4</sup>, once operational, will conduct criminal investigations and prosecutions of offences against EU's financial interests, while OLAF will continue administrative investigations.

Olaf's investigative performance 2010-2017<sup>5</sup>: 1800 investigations concluded, 2300 recommendations issued and it recommended the recovery of over €6.6 billion to the EU budget

**Figure 4.** OLAF performance in 2017



<sup>3</sup> [https://ec.europa.eu/anti-fraud/home\\_en](https://ec.europa.eu/anti-fraud/home_en)

<sup>4</sup> [https://ec.europa.eu/anti-fraud/policy/european\\_public\\_prosecutor\\_en](https://ec.europa.eu/anti-fraud/policy/european_public_prosecutor_en)

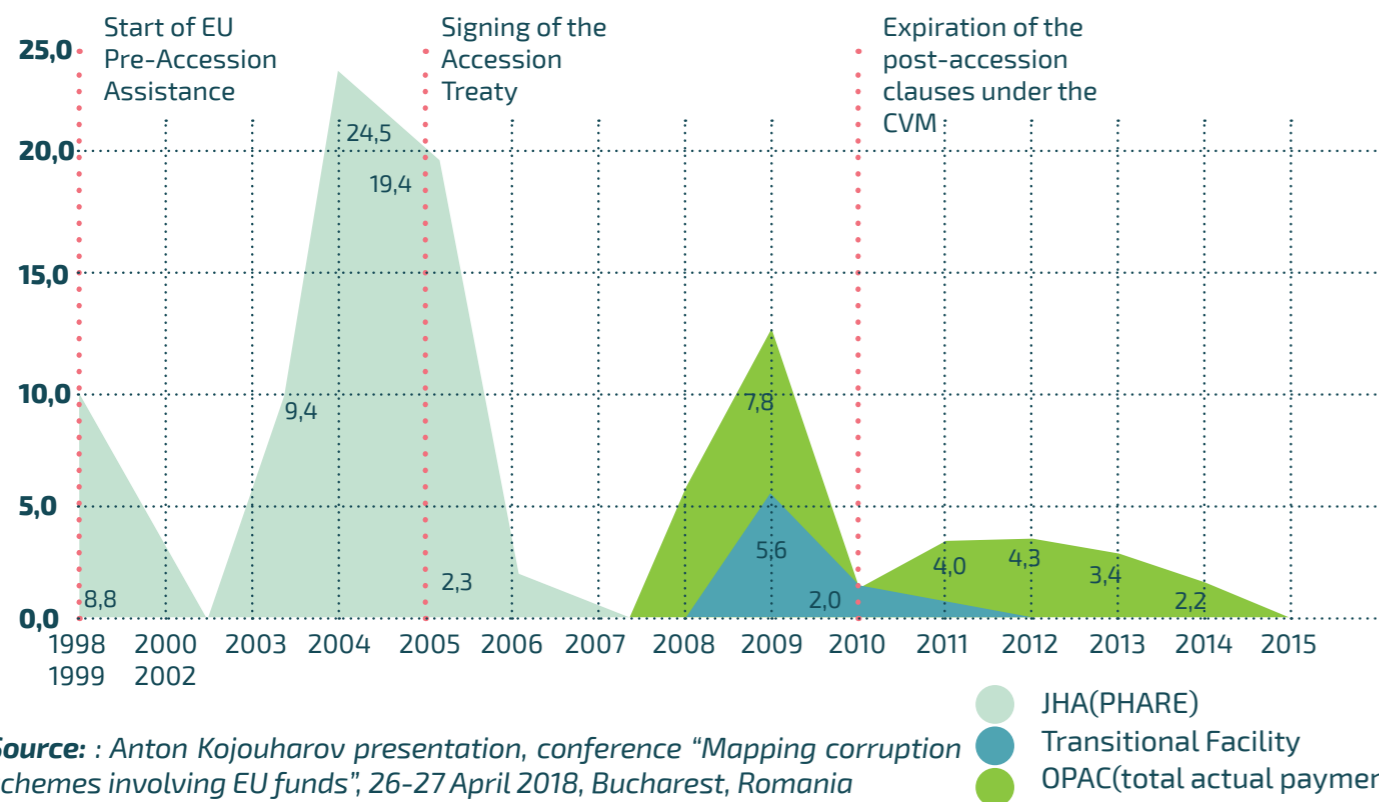
<sup>5</sup> OLAF website and reports

The Treaty (325 TFEU) also requires close and regular cooperation between Member States and the Commission to counter fraud and corruption in order to provide equivalent and effective protection of the EU's financial interests. In this respect, each Member State established an Anti-Fraud Coordination Service (AFCOS) in order to facilitate effective cooperation and exchange of (operational) information with OLAF.

Also Member States invested in anticorruption-related actions. An overview of the provided EU financial support for anticorruption-related actions since the beginning of the PHARE programme in

Bulgaria in 1998 reveals a telling trend. Irrespective of the actual amount of financial support through the years, Bulgaria seems to devote attention and resources to anti-corruption commitments only when approaching a major milestone towards EU accession or other related conditionality. Pre-accession, the allocation of anti-corruption-related support grew on two such occasions – at the very beginning of the PHARE programme and just before signing the Treaty of Accession in 2005. Post-accession, action through OPAC and the 2007 Transitional Facility peaked just prior to 2010, which coincided with the expiration of the CVM's safeguard clauses (see Figure 5).

**Figure 5.** Dynamics of the overall provided support for anticorruption-related actions (actual EC payments, EUR mln.)



**Source:** : Anton Kojouharov presentation, conference "Mapping corruption schemes involving EU funds", 26-27 April 2018, Bucharest, Romania

### 3. CORRUPTION SCHEMES INVOLVING EU FUNDS

According to 2018 ACFE Report to the nations on fraud and abuse<sup>6</sup>, corruption is the second most common form of occupational fraud (38% of the case). Industries with highest proportion of corruption cases are energy, manufacturing and public administration, while 70% of corruption cases were perpetrated by someone in a position of authority and 82% were committed by males. ACFE report found that top red flags in corruption cases are: living beyond means (43%), unusually close association with vendor/customer (34%), financial difficulties (23%), and "wheeler-dealer" attitude (21%). On average, ACF report found that a corruption scheme lasts 22 months and corruption is particularly likely to be detected by tips/inside reports (50%).

**Table 1.** Actors in corruption schemes involving EU funds

Corruptors	Intermediaries	Corrupted
Beneficiaries	Politicians	Managing authority
Contractors	Consultants	Oversight bodies
Subcontractors	Lawyers	Investigative bodies
Organised crime	former employees	Judicial authorities
White-collar	Politicians	

Thus, protection of EU whistleblowers is a particularly relevant policy against corruption. Regarding the exposure to corruption, ACF report found that "small businesses typically have fewer anti-fraud controls than larger organizations, leaving them more vulnerable to fraud".

Corruption is a scheme in which an employee misuses his or her influence in a business transaction in a way that violates his or her duty to the employer in order to gain a direct or indirect benefit. 2018 ACFE Report

Corruption schemes may be identified by assessing the process and corruption opportunities in each EU programming phase: planning, preparing,

**Source:** : Philip Gounev presentation, conference "Mapping corruption schemes involving EU funds", 26-27 April 2018, Bucharest, Romania

<sup>6</sup> <https://www.acfe.com/report-to-the-nations/2018>

procurement/contracting, execution and monitoring /evaluation/sustainability.

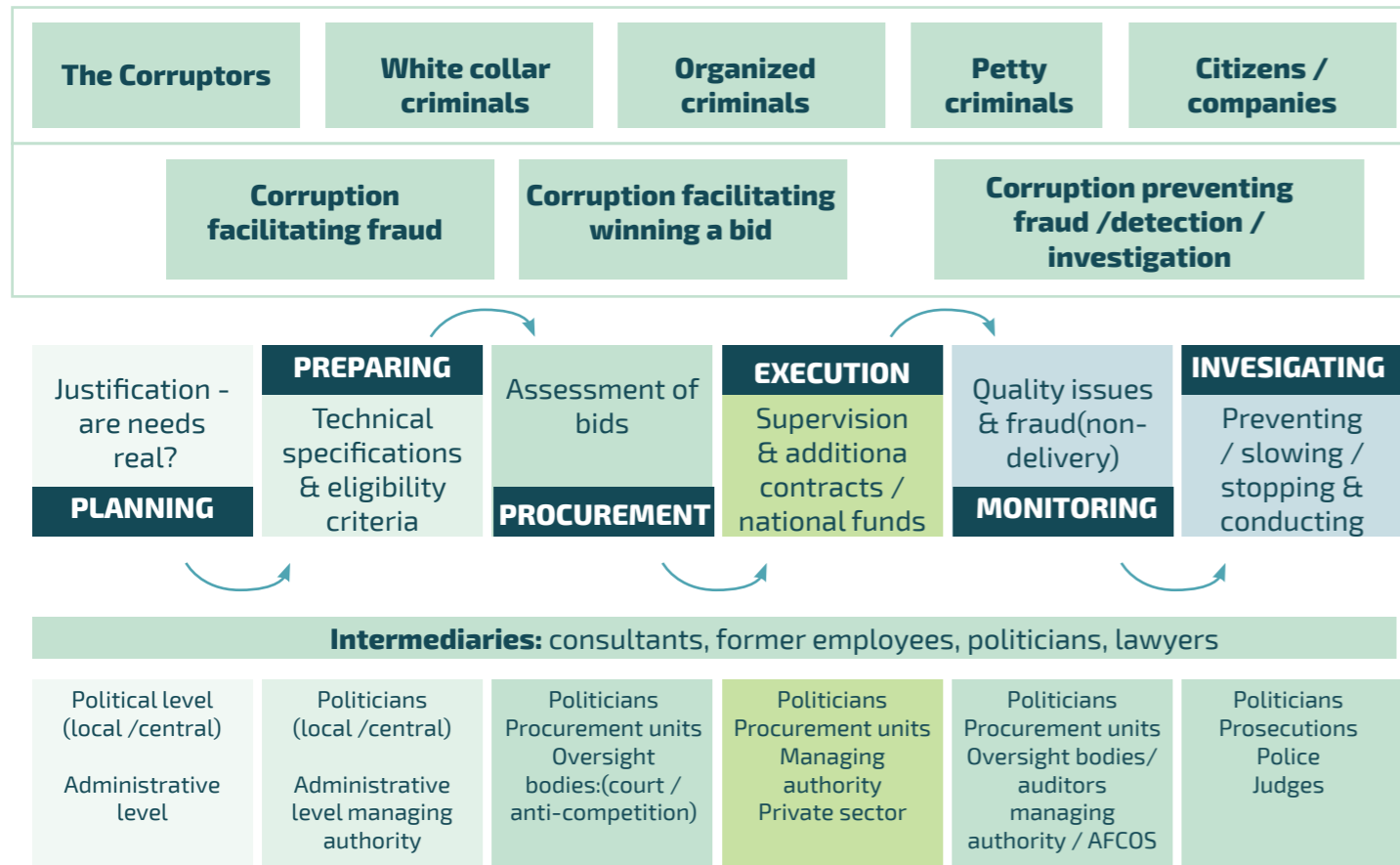
Corruption pressure may come from beneficiaries, intermediaries or officials.

Planning phase may be affected by corruption in order to falsify needs or favour certain investments. In this case, political level and high administrative level may be involved. During preparing phase, corruption may be used for favouring certain beneficiaries or companies in the process of defining

technical specifications or eligibility criteria. The procurement process has several corruption risks, especially during the process of assessment of bids.

During the execution phase, supervision may be loose or the amounts may be supplemented as a result of a corrupt scheme. In the monitoring/evaluation phase, fraud / non-delivery or poor quality may be overlooked also as a result of a corrupt scheme. In the end, even investigations may be affected by corruption.

**Figure 6.** Corruption risks during programme cycle



**Source:** Philip Gounev presentation, conference "Mapping corruption schemes involving EU funds", 26-27 April 2018, Bucharest, Romania

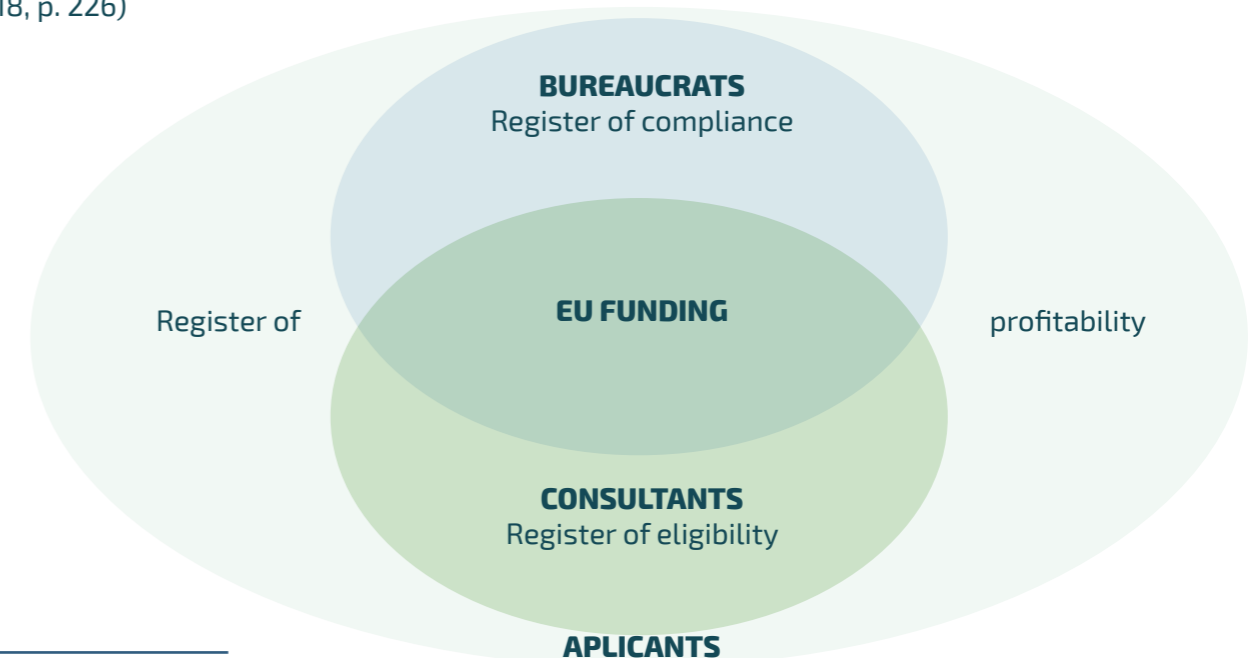
Bratu<sup>7</sup> builds a comparable framework for analysing corruption related to EU funding: "process of EU funding puts in relationship three generic actors - applicants/beneficiaries (people who want and/or access the funding), consultants (people who assist the applicant in accessing the funding) and bureaucrats" (p. 225).

According to Bratu, each generic actor works in a different register of behaviour: consultants focus on the register of eligibility, applicants work in the register of profitability, while bureaucrats rely on a register of compliance, "based on an overwhelming number of verifications, controls, inspections and monitoring" (p. 227, see also Figure 7). In this framework, a new actor emerged at national level to control defrauding of EU budget: "anti-corruption

and antifraud establishments", called by Bratu "elite squads" because of their superior social status, sustained by high level of financial and symbolic capital, such as higher salaries and direct contact with Brussels (p. 226). This landscape of transnational control through resources, rules and elite organisations combined with local context ("such as reliance on old solidarity networks, favour and gift exchange, informal arrangements") generates paradoxes, according to Bratu: anti-corruption simultaneously deters breaking the law and accessing funds, anti-corruption institutions are highly dependent on the political factor, and proliferation of rules and controls create the very conditions for carrying out simultaneously licit and illicit activities.

**Source:** Roxana Bratu presentation, conference "Mapping corruption schemes involving EU funds", 26-27 April 2018, Bucharest, Romania (from Bratu, 2018, p. 226)

**Figure 7.** The process of accessing EU funding in Romania: a stylised representation



<sup>7</sup> Corruption, Informality and Entrepreneurship in Romania, Palgrave Macmillan, 2018



One major element of analysis in explaining the corruption schemes involving EU funds is the national context, characterised in several EU member states by societal capture. In his presentation during the conference “Mapping corruption schemes involving EU funds”, 26-27 April 2018, Bucharest, Romania Munir Podumljak made the distinction between what is traditionally known as state capture and a new emerging form of societal capture characterized by a) high level of politicization of the public sector (especially criminal justice system, law enforcement, public administration, and State Owned Enterprises), b) absent or weak accountability mechanisms,

c) low transparency and confusing public data management systems; d) capture of the private sector (through privatization, concessions, public procurement and subsidies), e) significant presence and influence of PONGOs (political party organized, or influenced, non-governmental organizations), f) media clientelism (non-transparent interest based relationships between the political elites/governments and media owners), and g) lack of effective political integrity instruments. In such national contexts, according to Munir Podumljak, EU financial assistance is an accelerator of already present corruption.

**State capture** occurs when the ruling elite and/or powerful businessmen manipulate policy formation and influence the emerging rules of the game (including laws and economic regulations) to their own advantage. (World Bank)

**Societal Capture** is state of governance where elites engage in strategic endeavour to capture external control mechanisms (private sector, civil society and media) in addition to control of traditional state capture actors. (Partnership for Social Development)

Fazekas et al.<sup>8</sup> found that EU funding impacts institutionalised grand corruption in CEE in two ways: first, by providing additional public resources available for corrupt rent extraction; second, by increasing the controls of corruption for the additionally allocated funding. Their preliminary calculations indicate that the first effect increases the value of particularistic resource allocation in the three countries up to 1.21% of their GDPs, while the second effect decreases the value of particularistic resource allocation by up to 0.03% of GDP. However, the latter beneficial effect is entirely driven by Slovakia, which has a high national corruption risk

level; while in Czech Republic and Hungary this impact is even negative. Four types of corruption & fraud schemes involving EU funds were analysed during the conference “Mapping corruption schemes involving EU funds”, 26-27 April 2018, Bucharest, Romania

**• Corruption and fraud during the planning, application and contracting phase**

In the planning phase, according to Munir Podumljak, in captured societies, the process is reduced to a particularistic distribution of resources, setting

preconditions for accelerating-corruption role of the EU funds. According to Constantin Lica, in the application and contracting phase fraud schemes involve use of false statements in order to meet eligibility criteria (eg. false bank statements, fake contracts to prove previous experience, fake tax certificates).

**• Corruption in public procurement**

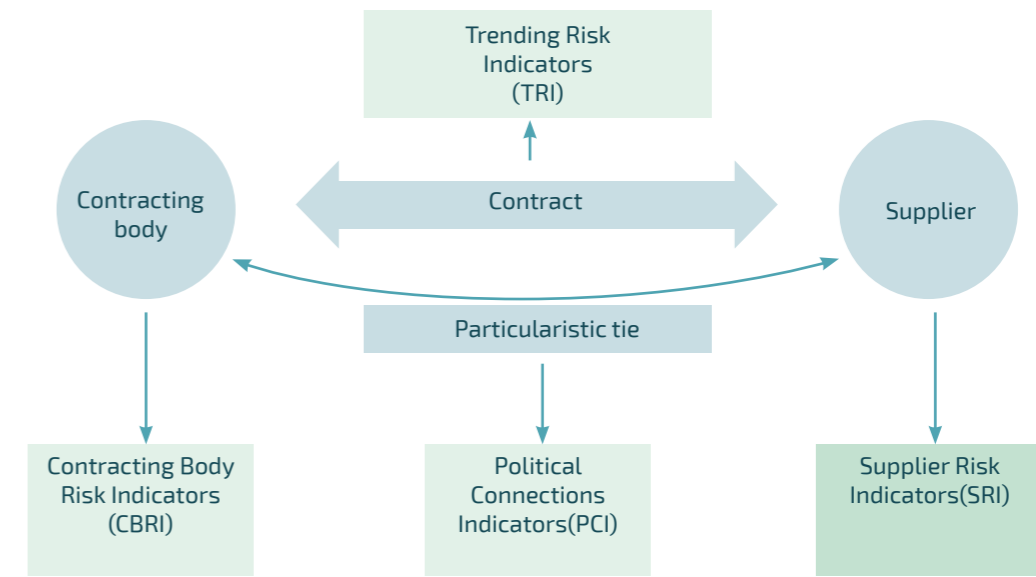
According to OLAF's experience<sup>9</sup>, public procurement is still the most attractive marketplace for perpetrators of fraud, who use corruption and off-shore accounts as fraud facilitators, many procurement fraud/corruption cases are transnational (e.g. contracting authority from one

Member State and bidders from several other Member States who subcontract in different countries), unlawful splitting of contracts, situations of Conflict of Interests, fraud at procurement level leads to fraud at the implementation level (false invoices, product substitution, etc.)

*One of the main common features of the OLAF cases concluded in 2017 was the collusion between the winner of a tender and either a consultant or the beneficiary of the funding. Conflict of interest also featured prominently in many of OLAF's cases, sometimes involving political figures and large public procurement projects. Source: OLAF 2017 report*

**Figure 8.** Conceptualising public procurement corruption indicators

**Source:** Ágnes Czibik presentation, conference “Mapping corruption schemes involving EU funds”, 26-27 April 2018, Bucharest, Romania



<sup>8</sup> Mihály Fazekas, Jana Chvalkovska, Jiri Skuhrovec, István János Tóth, and Lawrence Peter King - Are EU funds a corruption risk? The impact of EU funds on grand corruption in Central and Eastern Europe, Working Paper series: CRCB-WP/2013:03, November 2013, Budapest, Hungary

<sup>9</sup> Maria NTZIOUNI-DOUMAS presentation, conference “Mapping corruption schemes involving EU funds”, 26-27 April 2018, Bucharest, Romania

Ágnes Czibik tested corruption risks in public procurement using big data, four major types of corruption risks being defined (see Figure 8)

In public procurement, the aim of corruption is to steer the contract to the favoured bidder without detection through avoiding competition, tailoring technical specifications and/or sharing inside information.

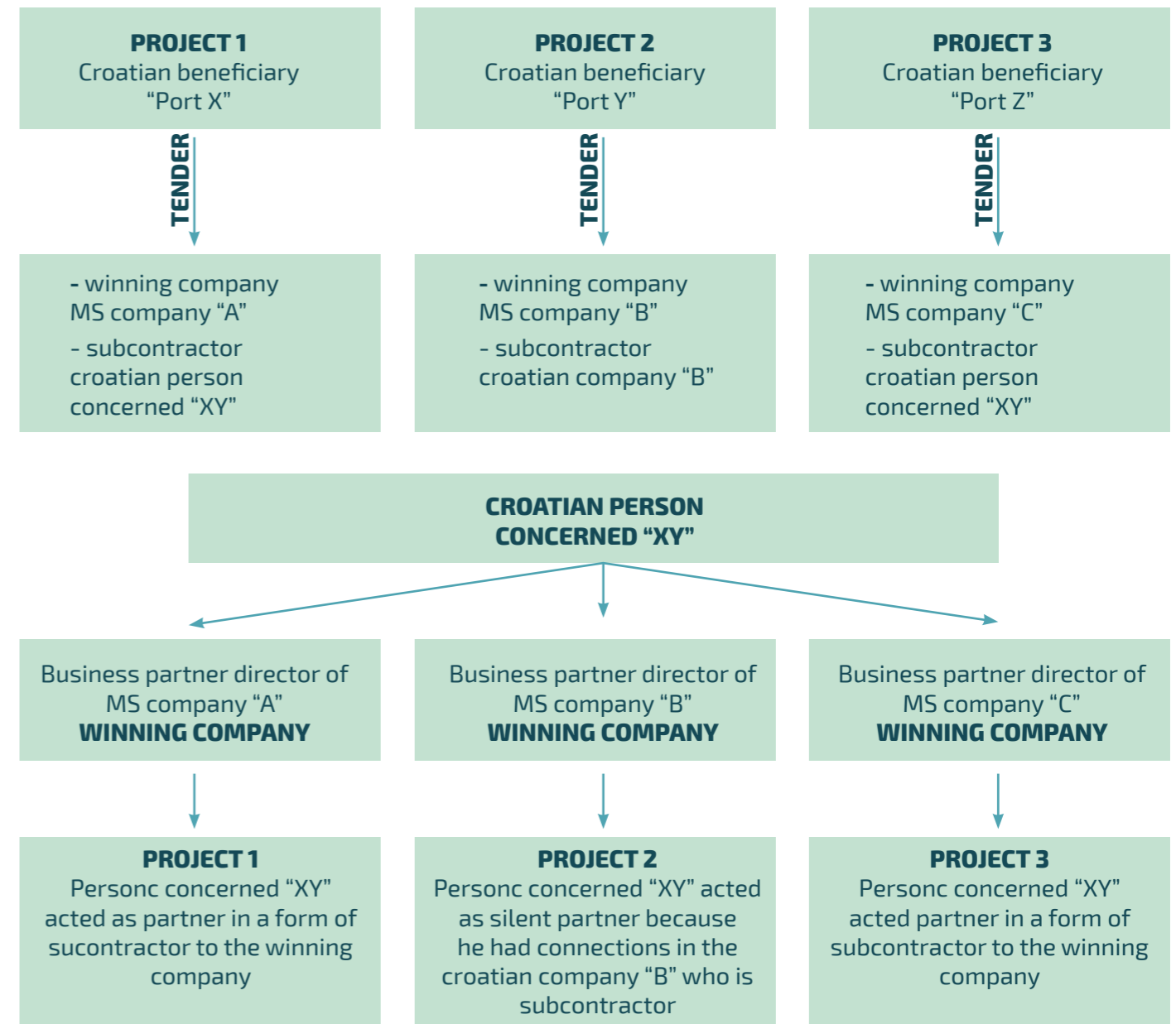
Constantin Lica presented real-life examples of procurement schemes such as falsification of unsuccessful bids to favour a particular bidder (similarities between the documents issued by different bidders), fictitious acquisition of software to justify transfers up to EUR 50,000, claiming reimbursements using forged document of origin in order to hide a prohibited "second hand" equipment

purchase (price differences: 22,000 USD real cost of second-hand equipment and 200,000 EUR reimbursement claim for the "new" equipment), unjustified increase of equipment price (between 200% and 500%) through multiple selling cycles between companies under the control of EU funds beneficiary, falsifying work situations (works not performed, construction materials not used), favouring a particular bidder through illegal disqualification of the economic operator who filed the most advantageous offer (costs increased by EUR 1,000,000), favouring a particular bidder through restrictive technical specifications. Ivana Trajceva presented similar real-life schemes from Republic of North Macedonia involving procurement of second-hand agricultural equipment and declaring it as new equipment in order to claim higher EU reimbursements.

## CASE STUDY: PROJECTS „INLAND WATERWAYS“

New director „XX“ of Croatian company „A“ by checking the documentation and e-mails discovered that previous director „XY“ had access to confidential tender documentation before the projects were published for tender (e.g. ToR of the projects). „XY“ received those documentation from someone in the Ministry of Transport and from the Beneficiary port „Y“. Furthermore, previous director „XY“ shared this information with his business partners, namely Member States company „A“, „B“ and „C“ with a view to divide the market among these three companies. By having access to the confidential information companies A, B, C steer the outcome of the tenders and get the contracts awarded to them and XY was subcontractor, directly and indirectly, in all the projects (see Figure 9). In that sense, A, B, C had time to draft technical specifications of their proposal and find key experts in accordance with the ToR of the projects.

Figure 9. Inland waterways project scheme



Source: Mirjana Jurić presentation, conference "Mapping corruption schemes involving EU funds", 26-27 April 2018, Bucharest, Romania

## CASE STUDY: OLAF REPORT ON CONSTRUCTION OF THE M4 SUBWAY LINE IN BUDAPEST

A Hungary Government spokesman<sup>10</sup> said the irregularities in the implementation of the M4 subway line project, the most expensive EU funded project implemented in Hungary, include fees paid to various agents for inside information, payment for services not actually rendered and various conflicts of interest, including instances where the same individual acting on behalf of the state when verifying the completion of work was also employed as an advisor to the contractor in question. The Government spokesman said the report cites examples of valid, lawful and cheaper offers being rejected during the public procurement phase in favour of those demonstrably possessing inside information. "Friendly companies were helped," he asserted, implying that this involved official malfeasance and abuse of power, conflicts of interest and bribery. OLAF report on this case is now public<sup>11</sup>.

<sup>10</sup> <https://budapestbeacon.com/europes-biggest-case-corruption-took-place-budapest-says-government-spokesman/>

<sup>11</sup> [http://www.kormany.hu/download/4/24/f0000/final\\_report.pdf#!DocumentBrowse](http://www.kormany.hu/download/4/24/f0000/final_report.pdf#!DocumentBrowse)

### • Conflicts of interests

Anca Tomulescu presented cases from Romania of high-level decisions-makers which took decisions regarding the administration or implementation of programs and projects funded by European Union that produced benefits for themselves, husband/wife, and close relatives: a) a rector of a state university signed individual employment contracts relating to his own employment and his daughter employment as experts in projects implemented by the university and funded by European Union; c)

a procurement contract co-financed by European Union was awarded by a public institution to a company in which the husband of the public institution's director had significant stocks.

Filip Stefan presented conflicts of interests related to EU Funds cases from Croatia: a) a project manager was also a co owner of the company that was selected for the procurement of equipment for the project, b) the winning bidder of the secondary public procurement also participated in the preparation of the public tender documentation.

## CASE STUDY: CONFLICT OF INTEREST

"Croatian Bank for Reconstruction and Development (CBRD) approved and signed a contract for a credit loan of approx. 4.000.000 € with a low interest rate (2%) to a company that was partly owned (20%) by the Assistant Minister in the Ministry of finances, where he was the head of the Sector for financial revision of budget spending. The credit was approved through a program designed to assist new investment projects in tourism. In the program rules it was explicitly stated that the credits cannot be granted for projects of refinancing older bank loans. The Commission for the Resolution of Conflicts of Interest in Croatia determined that the particular credit loan was approved by



the Supervisory board of CBRD although the project was tagged as risky and although this particular credit was to be used for refinancing older bank loans with higher interest rates that the company was not able to liquidate in due time. The Commission for the Resolution of Conflicts of Interest in Croatia also determined that the Assistant Minister was himself the guarantor for the approved credit through mortgage on his real estate. Because of this fact the Commission concluded that he had to come familiar with the terms and the program in which the credit was approved.

**Source:** Filip Stefan presentation, conference "Mapping corruption schemes involving EU funds", 26-27 April 2018, Bucharest, Romania

**• Corruption and fraud during sustainability phase**

Constantin Lica presented real-life examples of corruption and fraud after the implementation of projects: a) falsification of the minutes of on-spot verification through certification of unrealistic data on project output indicators, b) submission of false data on vulnerable people employed after the implementation of the project as part of sustainability obligations.

Organised crime is also an important threat against EU financial interests. The 2017 OLAF report highlights mafia involvement in defrauding EU Agricultural Funds<sup>12</sup>. A study commissioned by the European Parliament<sup>13</sup> found that organised crime is involved in VAT fraud, public procurement fraud and excise good fraud.

<sup>12</sup> OLAF 2017 report, p. 20

<sup>13</sup> PriceWaterhouseCoopers, How does organised crime misuse EU funds?, 2011, commissioned by European Parliament's Committee on Budgetary, Control

## CONFERENCE SPEAKERS "MAPPING CORRUPTION SCHEMES INVOLVING EU FUNDS", 26-27 APRIL 2018, BUCHAREST, ROMANIA:



**Maria NTZIOUNI-DOUMAS**, Advisor, OLAF, Directorate D – Policy

**Philip GOUNEV**, Anti-Corruption Expert, Former Deputy Minister of Interior of Republic of Bulgaria

**Roxana BRATU**, London School of Economics and Political Science, visiting research fellow

**Irena BJELOS**, Deputy Higher Prosecutor, Higher Public Prosecutor's Office in Belgrade, AFCOS contact point for Serbia

**Filip ŠTEFAN**, adviser, Conflict of Interest Commission, Croatia

**Anca TOMULESCU**, Integrity Inspection Chief, National Integrity Agency, Romania

**Constantin LICA**, Control Unit, Fight against Fraud Department (DLAF), Romania

**Melinda SZABO**, Prosecutor, Head of Section at the Metropolitan Chief Prosecution Office, Hungary

## CONFERENCE SPEAKERS “**MAPPING CORRUPTION SCHEMES INVOLVING EU FUNDS**”, 26-27 APRIL 2018, BUCHAREST, ROMANIA:



**Mirjana JURIC**, Head of Service for combating irregularities and fraud, Ministry of Finance, Croatia

**Andon TASHUKOV**, Anti-Fraud Coordination Service, Ministry of Interior Bulgaria

**Ened NAKUCI**, Prosecutor, Serious Crimes Prosecutor's Office, Albania

**Munir PODUMLJAK**, Executive Director, Partnership for Social Development, Croatia

**Florin ORBAN**, Association for Preventing and Combating Fraud, Romania

**Marius VASILIU**, Ministry of Regional Development and Public Administration, Romania

**Ivana TRAJCHEVA**, Public Prosecutor, Prosecutor's Office for Combating Organized Crime and Corruption, Republic of North Macedonia (former FYROM)

**Anton KOJOUHAROV**- Analyst, Center for the Study of Democracy, Bulgaria

**Ágnes CZIBIK**, Government Transparency Institute, Hungary

**Bart SCHEFFERS**, Open Society Foundations

**Cosmin ȘERBĂNESCU**, National Internal Control Institute, Romania

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