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*Committee on Budgetary Control*

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## **WORKING DOCUMENT**

on the Hercule III programme to promote activities in the field of the protection of the European Union's financial interests [PART 2]

Committee on Budgetary Control

Rapporteur: Iliana Ivanova

After the release of a first Working document on the Commission's proposal for the continuation of the Hercule programme to promote activities in the field of the protection of the EU financial interests there are several outstanding questions that are mainly related to the implementation of the programme and to the estimated allocation of resources under Hercule III. This second Working document aims to examine these aspects in order to substantiate the Rapporteur's amendments to the legislative proposal.

### ***Tobacco's money implementation and future allocation under Hercule:***

#### **A. Need for better coordination between Member States (MS) and the Commission?**

On the basis of the agreements with four major Tobacco's manufacturers<sup>1</sup>, between 2004 and 2030 more than USD 2 billion are to be paid to the EU budget and to the national budgets with the objective to fight against cigarette smuggling and counterfeiting. The MS are allocated 90,3% of the funds from the manufacturers during this timeframe, while the Commission receives the remaining 9.7%. In the context of Hercule III, EUR 44,815 million, equivalent to almost 41% of the envisaged financial envelop of the Hercule III programme covering the period 2014-2020, is to be allocated to the fight against cigarette smuggling and counterfeiting. In addition, this money will contribute to the funding of projects and initiatives through grants and procurement contracts, mainly signed between the Commission (OLAF) and the competent national authorities, the same which are also direct beneficiaries under the "tobacco's agreements".

The Rapporteur has already stressed, in her first Working document, the importance of assessing how the resources were spent since the adoption of Hercule I until now and how the resources will be allocated in the future, in particular regarding the fight against cigarette smuggling and counterfeiting<sup>2</sup>.

The recent Commission's documents on the implementation of the Programme<sup>3</sup> did not provide a clear answer to the issue of the coordination between the MS and the EU spendings

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<sup>1</sup> See Working document - PE486.153, page 2.

<sup>2</sup> See Working document - PE486.153

<sup>3</sup> The most recent analysis of the Community programme implementation is offered by the Commission Staff Working Document – Impact Assessment – accompanying document to the proposal on the Hercule III programme SEC(2011) 1610 final of 19 December 2011, which takes into account data until 2010.

(which is linked to the question of the possible overlaps between these two levels of implementation). Also the Court of Auditors (ECA), in its recent opinion on the proposal, pointed out the same issue<sup>1</sup>. To the knowledge of the Rapporteur, information by the MS on the use of “tobacco’s funds” allocated for the fight against cigarette smuggling and counterfeiting is still lacking and, when it is available, OLAF considers this information to be confidential.

In the absence of relevant information on how the revenues from the Tobacco’s agreements have been spent by the MS, some of the Rapporteur’s fundamental questions remain unanswered. For instance, it would have been very useful to understand how and to which extent, when implementing the Community programme, the vulnerability of the national markets to the contraband of illicit and counterfeit cigarettes was taken into account. It would also have been extremely helpful to know in advance and assess national or local initiatives in order to ensure the maximum impact of the Community programme at a national level.

### **The implementation of the programme<sup>2</sup>**

Most of the spending concerning the fight against cigarette smuggling and counterfeiting has been done under the “technical assistance” (TA) sector of the programme. As a general remark, the Rapporteur notes that, from Hercule II to Hercule III, the percentage of the programme’s financial envelop devoted to this sector has been increased from 50% to 79%<sup>3</sup>. Furthermore, the Rapporteur notes that among the MS receiving the most important portion of the Hercule financial envelop devoted to TA , one can find:

*TABLE 1 Top 5 Grant beneficiaries Technical Assistance (from 2004 until 2010) in EUR*

Country	TA except scanners	Scanners	Hercule II (2007-2010)	Hercule I (2004-	TOTAL

<sup>1</sup> See ECA Opinion No 3/2012, OJ C 201/1 of 7.7.2012.

<sup>2</sup> According to selected data from the Intermediate review on the achievement of the objectives of the Hercule II programme and from the Commission Informal note (Room document) transmitted by OLAF to the Council and to the EP.

<sup>3</sup> See Legislative financial statement of the Proposal for a Regulation on Hercule.

				2006)	
Germany	1 427 000	1 500 000	<b>2 927 000</b>	1 105 000	<b>4 032 000</b>
Finland	547 000	1 300 000	<b>1 847 000</b>	541 000	<b>2 388 000</b>
Spain	631 000	700 000	<b>1 331 000</b>	1 278 000	<b>2 609 000</b>
Poland	1 007 000	680 000	<b>1 687 000</b>	475 000	<b>2 162 000</b>
Hungary	1 375 000	-	<b>1 375 000</b>	768 000	<b>2 143 000</b>

In the field of the fight against cigarette smuggling and counterfeiting, the purchase of X-ray scanners has been preferred under Hercule II. Between 2007 and 2010, 21 scanners have been purchased by 16 MS, for a total amount of EUR 12,5 million. However, OLAF indicates the effectiveness of these scanners only in two cases (Ireland and Malta).

In addition, interesting data are those showing where the Hercule resources have been allocated (total grants and procurements, under TA, Training and IT).

*TABLE 2 Percentage of annual commitments per MS (2007-2011)  
[100% = 57,163,475 €]*

<b>0,1% - 1,9%</b>		<b>2 % - 4,9%</b>		<b>5% - 9,9%</b>		<b>10% - 15%</b>	
CY	1,8%	ES	4,1%	PL	5,4%	DE	12,7%
IT	1,7%	HU	4,1%	UK	5,0%	BE	11,9%
CH	1,6%	CA	4,0%			FR	11,6%
IE	1,5%	PT	3,9%				
LU	1,3%	SL	3,8%				
EE / LV	1,2%	NL	3,7%				
AT	1,0%	FI	3,5%				
LT	0,8%	EL	2,8%				

BG	0,7%	EC-JRC	2,8%		
CZ	0,4%	SK	2,3%		
DK	0,4%	RO	2,2%		
SV	0,2%	MT	2,1%		
PRC	0,1%				
Hong Kong	0,1%				
IN	0,0%				

On the basis of the “Project Star” research carried out by KPMG<sup>1</sup>, the Rapporteur notes that, in the context of cigarette smuggling and counterfeiting, one of the highest risks of vulnerability can be found at the Eastern borders of the EU. Eastern border countries are recognized to be a concern at EU level<sup>2</sup>.

The increase of the share of illicit cigarettes consumption in the last years, confirms the seriousness of the problem. Therefore, the Rapporteur reiterates her support to the continuation of the programme and considers necessary to devote enough resources to tackle the issue of illegal trafficking over the EU territory, especially for Eastern European borders which seem to be most vulnerable. The Rapporteur understands that illicit trafficking needs joint efforts not only inside the EU but also with third countries. In this regard, she would like to get further clarifications regarding the spending outside the EU (for instance, Canada received an important part of Hercule funds).

Due to lack of relevant information from MS, it is difficult to assess the impact of the EU funds at national level in the fight against cigarette smuggling and counterfeiting.

<sup>1</sup> See KPMG “Project Star 2010 results” of 22 August 2011 at [http://www.pmi.com/eng/tobacco\\_regulation/illicit\\_trade/documents/Project\\_Star\\_2010\\_Results.pdf](http://www.pmi.com/eng/tobacco_regulation/illicit_trade/documents/Project_Star_2010_Results.pdf)

<sup>2</sup> The Rapporteur acknowledges the Council conclusions on the “3133<sup>rd</sup> Competitiveness (Internal Market, Industry, Research and Space)”, of 5-6 December 2011. In the framework of the European Neighbourhood Policy, the Eastern Partnership and the EU-Russia Partnership for Modernisation, the Council invites “the Commission and the MS to cooperate with the East neighbouring countries with a view to [...] promote risk management and the fight against fraud in particular by: [...] organising joint actions targeting risks area and/or identified illicit trade routes in the region; stepping up actions to fight against smuggling of cigarettes and alcohol along the EU Eastern border; [...]”.

Consequently, the Rapporteur calls OLAF to provide, by December 2014, an extensive assessment of the Programme implementation in conformity with Article 7 of the Decision establishing Hercule II<sup>1</sup>. This assessment shall also take into account the impact of the programme and the link with the spending by MS in this field. The Rapporteur's amendments will allow a certain degree of flexibility, which will cover any major output of this evaluation.

### **B. Need for better coordination between the Commission's services?**

The Rapporteur congratulates OLAF and the national authorities for the results obtained in the fight against illegal activities detected by using specialised databases and scanners funded by the Hercule programme.

Information provided by OLAF on the use of scanners funded under the programme indicates that a variety of illicit goods has been seized during the past years: counterfeited cigarettes, tobacco, alcohol, wine, drugs and many other counterfeited items<sup>2</sup>. Information provided by FRONTEX<sup>3</sup> indicates that smuggling of migrants is carried out more frequently together with cigarettes on specific routes, mainly the Eastern Mediterranean Route. National law enforcement agencies' reports suggest that organised crime use trafficking routes for a variety of illicit activities.

The Rapporteur would like to understand which steps have been taken to avoid any risk of overlapping between Hercule and other programmes. OLAF, DG HOME, DG TAXUD and DG JUST all pay for technical assistance to MS (including scanners, training and access to database). Information should be provided about the efficiency of the coordination among the Commission's services. In particular, between TAXUD and OLAF funded activities when it comes to the fight against cigarettes smuggling and counterfeiting. The Rapporteur shares the ECA consideration in this respect.

### **Conclusions**

The Rapporteur recognises the importance of joint actions between EU and national level to protect in an efficient way the EU financial interests, in particular in this period of financial

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<sup>1</sup> Decision (N° 878/2007/EC) of the EP and of the Council of 23 July 2007.

<sup>2</sup> See Commission Staff Working Paper Impact Assessment – Accompanying document to the Hercule III proposal (SEC(2011) 1610 final), of 19.12.2011, page 24.

<sup>3</sup> See FRONTEX Annual Risk Analysis 2012.

crisis. She considers that all support should be given to the MS to protect EU financial interests. The Hercule programme provides the legal basis for this kind of support.

Yet, the Rapporteur is concerned about misspending of public money. In particular, it arises when needs and priority areas have not been fully assessed, and when there is a lack of clear evidence of coordination among all stakeholders involved. Concerning Hercule, she deems it important to evaluate in a proper manner the impact of EU spending before committing the resources available. In the context of the programme this imperative is particularly true with regards to the fight against cigarettes smuggling and counterfeiting and to the purchase of scanners in the field of technical assistance.

The Rapporteur welcomes the initiative of the Commission to continue the Community programme Hercule until 2020. At the same time, she agrees with the ECA about the need to ensure that the legal basis should take into account the results and the assessment of Hercule II. A specific provision in the Regulation should take it into account accordingly.

The Rapporteur also considers it very important to ensure that Hercule III will be assessed on the basis of clear and measurable performance indicators. The recent ECA opinion shares, on this point, the Rapporteur's view. She will therefore ensure that these indicators are clearly reflected in the proposal.

The cooperation between the MS and the Commission is a fundamental element in the protection of the EU financial interests. Given the importance of the financial envelop devoted to the fight against cigarettes smuggling and counterfeiting, the MS and the Commission should establish a systematic exchange of data about the use of funds relating to this sector. The Rapporteur would like to make sure that in the future relevant information is gathered by the Commission for assessment and review purposes.

The Rapporteur takes the view that the level of co-financing<sup>1</sup> as proposed by the Commission is justified given the current budgetary difficulties experienced by most MS. Going even further, she considers necessary a certain degree of flexibility in case of specific problematical situations especially when vulnerable MS cannot afford sufficient co-financing. The Rapporteur is also of the opinion that clear performance indicators will allow to assess the impact of the Hercule programme and the impacts of other Commission or national initiatives.

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<sup>1</sup> 80% of eligible costs for grants and up to 90% in exceptional and duly justified cases, defined in the annual work programme

The Rapporteur considers that the Commission's services' coordination should be further improved. Law enforcement tools, like scanners, are funded by several DGs of the Commission. The Rapporteur invites the Commission to transmit a comprehensive description of technical equipment used by national law enforcement authorities which are funded or partly funded by the Commission, and – whenever available – the impact of such spending in the fight against illicit activities.

Finally the Rapporteur, considers that the question of the “earmarking” is still open. In addition, she would like to receive further clarifications of the reasons why the management of the Hercule programme should remain within OLAF and not, as suggested several times by the ECA, to be transferred to another DG not in charge of anti-fraud investigations.

Since several questions remain unanswered, the Rapporteur intends to organise a Public hearing to gather the opinions of the different stakeholders.