

Evolution of System for Protection of EU Budget – Part I

Fight Against Fraud in the EU Funds

European funds, due to their significant volume, enable harmonious development, implementation of important reforms and reduction of economic disparities between Member States. In the new financial perspective 2021–2027, Poland will remain the largest beneficiary of the cohesion policy as it will receive over EUR 75 billion (at current prices), which means that every fifth euro will reach Poland¹. Besides cohesion policy funds, Poland will also receive support under, among others, the Recovery and Resilience Facility (EUR 23.9 billion in grants and EUR 34.2 billion in loans), to be spent by the end of 2026². The Facility is aimed at mitigating direct economic and social damage resulting from the coronavirus pandemic. Such a large amount of the allocation creates tremendous opportunities and can leverage the economy and bring social benefits. It is, however, indispensable to program these funds in an appropriate manner, firstly – so that the set development goals can be met, and secondly – so that they will be spent in an efficient manner, in full compliance with the law, and – most importantly – free from fraud. Every fraud related to implementation of EU projects affects negatively implementation of set goals, and may also damage reputation of the cohesion policy as such, which in consequence can result in reducing European support in the area in the future.

¹ The total amount of funding for the cohesion policy for 2021-2027 is EUR 372.6 billion (in current prices). Regulation of the Council 2020/2093 of 17 December 2020 on multiannual financial framework for 2021–2027, OJ EU L 433 I/11. Breakdown of allocation in current prices: <https://ec.europa.eu/info/files/mff-2021-2027-breakdown-cohesion-policy-allocations-member-state-current-prices.pl>

² Adopted on the basis of the Regulation by the Council 2020/2094 of 14 December 2020 establishing a European Union Recovery Instrument to support the recovery in the aftermath of the COVID-19 crisis, OJ L 433 I/23. To use these funds, ratification is necessary of the decision on own resources by all Member States in accordance with their constitutional requirements.

MARCIN SZYMAŃSKI**Introduction**

For many years, European institutions have been taking steps to protect the Union's financial interests. Also, Member States, on the basis of the Treaties' provisions, are obliged to combat fraud, which is of special importance, within the so called shared management, i.e. co-responsibility of Member States and the European Commission (EC) for proper execution of the EU budget, implemented through, among others, the cohesion policy. In order to improve protection of the Union's financial interests, since 2021 provisions set forth that availability of European financial support and refunds on expenditure are linked to compliance with the rule of law, principles have been in place. This requires not only focusing on concrete law breaches, but above all means the necessity to ensure constant implementation of the rule of law principles as a kind of guarantee protecting European funds against corruption and embezzlement. A particular challenge is to safeguard sound implementation of funds in the current crisis situation triggered by the COVID-19 pandemic, which resulted in unprecedented financial support for Member States and, simultaneously, in flexibility of rules, procedures and principles governing its use. Moreover, this support has to be used in a relatively short time perspective.

Considering the above, fight against fraud poses a great challenge, and calls for actual engagement and cooperation among all entities that spend public funds (including those from the EU budget) and

law protection bodies that have appropriate investigation tools at their disposal. Efforts must focus not only on detection, but also – or even more so – on prevention mechanisms that should reduce opportunities and possibilities to commit fraud. It is also necessary to increase the level of awareness of potential risks and consequences of fraud, and to establish a culture of integrity and ethical conduct, as well as to engage civil society organisations in public money spending monitoring. Systems designed to combat fraud must also be complemented with procedures enabling fast recovery of unduly paid funds, as well as with sanctions having a deterrent effect on potential perpetrators.

Since combating fraud is a very broad area, this article focuses on solutions related to expenditure of EU funds within the framework of the cohesion policy, and it has been divided into two main parts. The first part emphasises negative results of corruption in its broad sense, as well as presents EU legal regulations that provide the basis on which Member States perform their duties related to combating fraud. The article also elucidates the basic terms in the area of fight against fraud, i.e. the notion of “the Union's financial interests”, as well as the difference between “an irregularity” and “fraud”. Moreover, the paper aims to present the evolution of the system to protect the Union's financial interests, and anti-fraud initiatives of the EU institutions, especially the European Commission that sets directions in the area in the form of strategic documents. Moreover, the first part of the article presents an appraisal of the activities by the EC and Member States that has been developed

by the European Court of Auditors (ECA), as well as an evaluation of the solutions set forth in the *Regulation on a general regime of conditionality for the protection of the Union budget*, which has been in force since the beginning of 2021. The second part of the article, presents, in turn, examples of specific anti-corruption tools used in Poland while implementing programmes financed from the Union's funds, including e.g. the mechanism for whistle-blowers, and the innovative instrument to prevent fraud, i.e. the so called integrity pact. Examples included in this part of the article refer to highest risk areas, and are related to prevention and detection of suspected fraud. The measures discussed can be also successfully applied by all entities that use public money, and their implementation should improve the internal control system in the area of prevention and detection of illegal activities, and consequently enhance the effectiveness of public policies implemented.

Effects and scale of fraud in the EU

Subsidies granted to a friendly entity as a result of a biased assessment of a project application, a contract awarded under an EU project in exchange for material or personal gains, refunds on assignments that have never been carried out declaring the same expenditure in several projects,

or untrue certification of results achieved within a project – these are just a few out of numerous potential frauds³, examples that may occur in EU funded projects. On the basis of the data of the European Anti-Fraud Office (OLAF⁴), the most common examples of fraud against EU spending within the framework of the cohesion policy are related to:

- public procurement awarding procedures and contract execution, including collusive bidding;
- false documentation to certify expenditure (invoice, documents to certify that work has been delivered), or lack of such documentation;
- doubled declaration on the same expenditure;
- failure to disclose a conflict of interests;
- opening fictitious business only in order to receive a subsidy.

The areas where fraud is most frequently detected include:

- infrastructure;
- research and development;
- environment;
- information technology (IT) investments.

Fraud in an EU project, or broadly understood corruption⁵, related not only to Union's funds implementation, but to the public sector as such, results in, for instance:

³ Fraud examples are discussed e.g. in European Anti-Fraud Office's *Compendium of anonymised cases structural actions* of 2011 available at: <https://ec.europa.eu/sfc/sites/sfc2014/files/sfc-files/OLAF-Intern-2011.pdf>

⁴ From the French name of the office: L'office européen de lutte anti fraude.

⁵ The broader approach defines corruption as abuse of power (office) for private benefits (also covering private sector activity). Still, corruption is a multidimensional aspect, variously defined by the law and literature. More details: Waldemar Walczak. 2019. „Nadużycie władzy publicznej elementem korupcji - Próba szerszego ujęcia zjawiska”. *Kontrola Państwowa* 3.

- waste of public resources that could have been used in a more effective manner (e.g. excessive costs of public investments, lower quality, high maintenance costs);
- non-optimal implementation of policies' goals. In the case of the EU cohesion policy – delayed economic growth in the regions subject to support;
- deepening inequalities, poverty and negative impact on income division⁶;
- negative perception and reduced trust in institutions. In case of EU funds – lost trust in the EU institutions and Member State's institutions responsible for funds management⁷;
- honest entities' reluctance to take initiative, to apply for support, and to submit public procurement bids – due to the negative reputation of policies, and the feeling that bids are “fixed” and unavailable for fair market players⁸;
- obtaining undue benefits by entities that commit fraud. In the case of EU funds, these benefits come – ultimately – from taxpayers' purse, i.e. citizens of EU Member States;

- decreased interest and willingness of foreign companies to invest in corrupt markets, since their legal and administrative rules are considered insecure and depending on discretionary decisions of officials⁹;
- lowered level of public and private investments, and decreased gross domestic product (GDP)¹⁰.

Reduction of corruption prone phenomena is a huge challenge, mainly due to the fact that corruption is by its nature well veiled. Most often there is no concrete fraud victim, and consequently such fraud is hard to detect. In addition to that, fraud is usually hard to prove, therefore confirming fraud by the court and punishing perpetrators is not always possible. The actual scale of corruption is also unknown. Some information about fraud is provided on the basis of the data related to the cases presented in the EC's annual reports on protection of the Union's financial interests and fight against fraud. Only in 2019, EU Member States reported to the EC on 939 fraud cases amounting to EUR 461 million¹¹.

⁶ OECD, Recommendation of the Council on Public Integrity, 26 January 2017 – C(2017)5, p. 2, <https://www.oecd.org/gov/ethics/OECD-Recommendation-Public-Integrity.pdf>.

⁷ European Commission: Joint Anti-Fraud Strategy 2015-2020, Ref. Ares(2015)6023058 – 23/12/2015 (JAFS 2015-2020) <https://ec.europa.eu/sfc/sites/sfc2014/files/sfc-files/JOINT%20ANTI-FRAUD-STRATEGY2015-2020.pdf>

⁸ For instance, the lack of assurance as for fairness in selecting the best offer was indicated by contractors as the reason for little interest in public procurement proceedings. On the basis of: *Raport z badania dotyczącego niskiej konkurencyjności w zamówieniach publicznych*, Urząd Zamówień Publicznych, Warszawa, October 2019, <https://www.uzp.gov.pl/aktualnosci/wyniki-badan-dotyczacych-konkurencyjnosci-w-zamowieniach-publicznych>

⁹ Tomasz Grzegorz Grosse. 2000. *Działania antykorupcyjne w państwach członkowskich OECD*, Florencja, <https://www.antykorrupcja.gov.pl/download/4/5337/DzialaniaantykorupcyjnewpanstwachczlonkowskichOECD.rtf>

¹⁰ P. Mauro. 1997. “The Effects of Corruption on Growth, Investment, and Government Expenditure: A Cross-Country Analysis”. In: *Corruption in the Global Economy*, K. Elliott (ed.), Washington, Institute for International Economics.

¹¹ Report from the Commission to the European Parliament and the Council, 31st Annual Report on the protection of the European Union's financial interests – Fight against fraud – 2019 (3.9.2020 COM(2020) 363 final), p. 13, https://ec.europa.eu/anti-fraud/sites/antifraud/files/pif_report_2019_en.pdf

For comparison, in the years 2013–2017 the total of over 4,000 irregularities – potential fraud cases were detected. They were related to the European support amounting to almost EUR 1.5 billion, and 72 percent of this amount was cohesion policy funds. The cohesion policy constitutes only ca. one-third of the EU budget, but almost three-quarters of the total value of funds where fraud occurs are cohesion policy funds¹². Nevertheless, it needs to be emphasised that this data refers only to the cases that have been detected and reported by Member States. At this point it is worth paying attention to the fact that even the scale of identified cases is not fully known, since the ways in which Member States report on them vary significantly¹³, due to various interpretations of legal regulations. For example, some states notify about suspected fraud only after a legally binding court verdict, while other states – at earlier stages of criminal proceedings (e.g. once after preparatory proceedings have started). Therefore the exact number and value of all fraud cases that could have been committed when EU funds spending is impossible to estimate. The

study commissioned by the EC in 2013 indicated that direct corruption costs related to the EU procurement amounted to from 2.9 percent to 4.4 percent of the total value of public procurement¹⁴. For Poland, this implies losses at the level of several billion of Polish zloty a year¹⁵. In its 2014 anti-corruption report¹⁶, the EC indicated that corruption costs in EU Member States were as much as EUR 120 billion a year, which is comparable with the annual amount of the EU budget.

Legal grounds to fraud combatting

EU citizens should receive assurance that their contribution to national budgets and the EU budget (mainly coming from taxes they pay) is used adequately. A significant part of the EU budget is spent through funds that include the cohesion policy aimed at investments in creating jobs, sustainable economy development and environmental protection. Member States are accountable for appropriate spending of these funds within the shared management scheme, i.e. under supervision of the EC that, on the basis of Article 317 of the Treaty on the Functioning of

¹² ECA press release of 16 May 2019: <https://www.eca.europa.eu/en/Pages/DocItem.aspx?did=49940>

¹³ Item 25 of the special report of the European Court of Auditors on the fight against fraud in EU funds spending – it is necessary to take measures of the special report (No 01/2019). Polish version: https://www.eca.europa.eu/Lists/ECADocuments/SR19_01/SR_FRAUD_RISKS_PL.pdf

¹⁴ Report by PwC and Ecorys for the European Commission: *Identifying and Reducing Corruption in Public Procurement in the EU*, 2013, https://ec.europa.eu/anti-fraud/sites/antifraud/files/docs/body/identifying_reducing_corruption_in_public_procurement_en.pdf

¹⁵ For instance, the value of the public procurement market in 2019 stood at PLN 198.9 billion – based on the Report by the President of the Public Procurement Office on the functioning of the public procurement system in 2019, <https://www.uzp.gov.pl/baza-wiedzy/analizy-systemowe/sprawozdania-o-funkcjonowaniu-systemu-zamowien-publicznych>

¹⁶ Report from the Commission to the Council and the European Parliament EU Anti-corruption report, COM(2014)38 of 3 February 2014.

the European Union (TFEU)¹⁷, remains primarily responsible for the UE budget implementation.

EU funds spending is based on clearly defined principles stemming from the EU regulations. The basic law in the area, equivalent to the Polish Act on Public Finance, is the EU financial regulation¹⁸ and the Treaty¹⁹ principle of sound financial management²⁰ it comprises. It requires that EU funds spending is economical, effective and efficient. The assumption behind and the objective of the new version of the EU financial regulation, which was issued in 2018, include, among others, increased transparency and accountability of the EU expenditure, and ensuring better focus on the results of the EU policies implemented. The provisions of the regulation are horizontal in nature (they are related to all EU policies), and they require introduction of internal controls for budget execution, at all management levels, that should provide for fraud and irregularities prevention, enable their detection, ensure correction and follow-up, as well as appropriate risk management.

The principles that strictly relate to EU funds spending in the financial framework 2014–2020 were set forth in sectoral provisions, i.e. in the Regulation of the European Parliament and of the Council (EU) No 1303/2013²¹. These provisions indicate a desirable management and control system shape, which comprises authorities with defined duties and responsibilities, as well as procedures for funds spending and their verification²². These provisions, compared with the regulations for the previous EU financial frameworks, increased the responsibility of Member States for appropriate use of EU funds, and for reaching clear and measurable objectives. Moreover, they expanded the scope of responsibilities of managing authorities liable for implementation of operational programmes under which projects are carried out and EU funds are spent.

Fight against fraud and other illegal actions that breach financial interests of the European Union is an obligation of every Member State, and it stems directly from Article 325 of the TFEU. What is more, Member States must introduce

¹⁷ O J C 115/49 of 9 May 2008.

¹⁸ Regulation of the European Parliament and of the Council (EU, Euratom) 2018/1046 of 18 July 2018 on the financial rules applicable to the general budget of the Union, amending regulations (EU) No 1296/2013, (EU) No 1301/2013, (EU) No 1303/2013, (EU) No 1304/2013, (EU) No 1309/2013, (EU) No 1316/2013, (EU) No 223/2014 and (EU) No 283/2014, and decisions No 541/2014/EU, and repealing regulation (UE, Euratom) No 966/2012. (O J U EU L No 193 of 30 July 2018).

¹⁹ Article 310(5) TFEU.

²⁰ More details: Justyna Łacny. 2014. „Zasada należytego zarządzania finansami Unii Europejskiej”. *Kontrola Państwowa* 3.

²¹ Regulation (EU) No 1303/2013 of the European Parliament and of the Council of 17 December 2013 laying down common provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund, the European Agricultural Fund for Rural Development and the European Maritime and Fisheries Fund and laying down general provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund and the European Maritime and Fisheries Fund and repealing Council Regulation (EC) No 1083/2006 (Regulation 1303/2013).

²² More details: Marcin Szymański. 2014. „System wdrażania i kontroli projektów polityki spójności 2014–2020”. *Kontrola Państwowa* 5.

such measures to combat fraud as when protecting their own financial interests²³ (principle of assimilation). It means that funds coming from the EU budget must be protected at least in the same way in which the given state's budget is protected, both on the part of revenues and expenditure. Under the shared management, in accordance with Article 63 of the EU financial regulation, Member States should take steps (including legislative, executive and administrative) in order to protect the Union's financial interests. To this end, Member States should establish competent bodies, prevent irregularities and fraud, as well as identify cases thereof, collaborate with appropriate services, such as, e.g. the EC, OLAF and the ECA. Moreover, Member States are obliged to undertake control activities in order to recover unduly paid funds, as well as impose effective, proportionate and deterring sanctions. Every year, by 15 February, the Member States are obliged to submit to the EC accounts on the expenditure that was incurred, an annual summary of the final audit reports and of controls carried out, as well as a management declaration to confirm that:

- information has been presented in an appropriate manner, is complete and accurate;

- expenditure has been incurred for its intended purposes set out in sector-specific regulations;
- the control systems put in place ensure the legality and regularity of the underlying transactions.

Member States are also obliged to protect the Union's financial interests directly on the basis of the horizontal regulation of the Council (EC, Euratom) No 2988/95 of 18 December 1995 on the protection of the European Communities financial interests²⁴ (Regulation No 2988/95). Another important legal act in the area is the directive on the fight against fraud to the Union's financial interests by means of criminal law²⁵ of 2017 (the PIF Directive²⁶), which replaced the Convention on the protection of the European Communities' financial interests²⁷.

It is worth emphasising that the above legal acts oblige Member States to protect "Union's financial interests". The notion was defined in the provisions of the PIF Directive. In accordance with Article 2 of the Directive, "Union's financial interests" means all revenues, expenditure and assets covered by, acquired through, or due to the Union budget. A similar definition is comprised in the provisions of the regulation concerning investigations conducted by OLAF²⁸, according to which "Union's

²³ Article 325(2) TFEU.

²⁴ OJ EU of 23 December 1995.

²⁵ Directive (EU) 2017/1371 of the European Parliament and of the Council of 5 July 2017 on the fight against fraud to the Union's financial interests by means of criminal law.

²⁶ PIF – from the French 'protection of financial interests' (*protection des intérêts financiers*).

²⁷ Act of the Council of 26 July 1995 establishing the Convention on the protection of the financial interests of the European Communities, OJ 316 of 27.11.1995, p. 48-57.

²⁸ Regulation (EU, Euratom) No 883/2013 of the European Parliament and of the Council of 11 September 2013 concerning investigations conducted by the European Anti-Fraud Office (OLAF) and repealing Regulation (EC) No 1073/1999 of the European Parliament and of the Council and Council Regulation (Euratom) No 1074/1999 (OJ C 248/1).

financial interests” means revenues, expenditure and assets covered with the budget of the EU and the budgets of institutions, bodies, offices and agencies, as well as the budgets that they manage or monitor. Therefore protection of the Union’s financial interests against irregularities and fraud actually means – within the scope of the cohesion policy – protection of budget funds, so on one hand – ensuring appropriate proceeds to the EU budget, and on the other hand – due diligence in spending that prevents from charging the budget of the Union with an unjustified item of expenditure provisions for the financial perspective 2014–2020 (Regulation 1303/2013) – for the first time – directly oblige managing authorities to introduce effective and proportionate measures to combat fraud²⁹, taking into account risks identified. Managing authorities must therefore not only ensure that the expenditure declared for refund by the EC has been incurred in compliance with the law, but also guarantee that the risk of fraud in the programmes implemented has been reduced to the lowest acceptable level. This obligation has resulted from intense efforts of the European institutions aimed at implementing a systematised and effective anti-fraud system. It should cover all institutions whose activities redound to preventing, detecting and appropriate dealing with illegal actions that affect the Union’s financial interests. Despite a series of initiatives taken by Member States and

the EC, described every year in reports on protection of the Union’s financial interests and fight against fraud³⁰, there is still a lot of room for improvement. It was discerned by the ECA in its audit missions conducted in the area in 2018, which will be discussed later in this article.

Notion of fraud versus notion of irregularity

Regulations at the EU level oblige Member States to prevent, detect and correct irregularities and counteract fraud. Both irregularity and fraud have clear definitions in the EU regulations, different from the common understanding of these notions (in-compliance with the laws or norms, and financial crime, respectively). Also, there are strictly defined relations between the two. It is worth mentioning that the Act on the Supreme Audit Office³¹ also uses the notion of irregularity (e.g. Article 51(4)), which, however, has not been defined in the Act. Therefore an irregularity identified in NIK’s audits, as well as in other audits outside the EU funds management and audit system, does not necessarily denote an irregularity in the way it is understood in the Union’s regulations. So media information about “irregularities” found in European projects will not always mean that there has been an irregularity or fraud as understood by the EU provisions, which would require corrective measures. At this point, it is also important to remind that the premises for

²⁹ The obligation was introduced in the communication on the Commission Anti-Fraud Strategy – final version of 24 June 2011; COM (2011) 376.

³⁰ Report submitted to the European Parliament and the Council on the basis of Article 325(5) of the EU Financial Regulation.

³¹ Act of 23 December 1994 on the Supreme Audit Office (Dz.U. 2020.1200 with later amendments).

recovery of funds, set forth in the Act on Public Finance³² (Article 207) do not relate, in any way, to the definition of irregularity and premises for its occurrence set forth in the EU regulations³³. The requirement to demand recovery of funds stems from one of the circumstances listed in Article 207(1), in accordance with which funds must be returned if they have not been used in accordance with their purpose, if procedures have been breached, if funds have been obtained unduly, or in an excessive amount.

Whereas a definition of irregularity is provided in Article 1(2) of Regulation 2988/95, which is still in force, and simultaneously in sectoral provisions – for the financial perspective 2014–2020 this means Article 2 item 36 of Regulation 1303/2013³⁴. The definitions included in the above legal acts are almost identical, with the only difference being that the definition from the sectoral regulation – since it is related to the Union's funds spending – is limited to the impact on the EU budget at the expenditure side only, and not at the revenue side, as it is the case in the general regulation. The Court of Justice of the European Union, in the verdict of 26 May

2016, emphasised that these notions, in spite of being regulated in separate acts, call for a unified interpretation³⁵.

1. Bearing in mind the definitions provided in the above legal acts, an irregularity is a situation when all the presumptions listed below are met: Breach of law. It may be related to both the EU law and national provisions, including the provisions of a grant agreement concluded with a project beneficiary³⁶.

2. Act or omission on the part of a perpetrator. It is not important, however, whether it was intentional or not. It means that an unintentional action is sufficient to state an irregularity. It was confirmed in the thesis included in item 65 of the verdict of the Court of Justice of 1 October 2020 No C 743/18 stating that it is not necessary to prove an intention or negligence on the part of a beneficiary for an irregularity to occur.

3. Stating that it is due to an economic operator. In accordance with the legal definition, adopted for the purposes of the EU funds implementation, an economic operator means any natural or legal person or other entity taking part in the implementation of assistance from the ESI

³² Act of 27 August 2009 on public finance (Dz.U.2021.305 with later amendments).

³³ See also: Marcin Szymański. 2010. „Zwrot środków nieprawidłowo wykorzystanych przy realizacji programów Unii Europejskiej - Na podstawie przepisów ustawy o finansach publicznych”. *Kontrola Państwowa* 2.

³⁴ An irregularity means any breach of Union law, or of national law relating to its application, resulting from an act or omission by an economic operator involved in the implementation of the ESI Funds, which has, or would have, the effect of prejudicing the budget of the Union by charging an unjustified item of expenditure to the budget of the Union. Importantly, the Act of 11 July 2014 on the rules for implementation of programmes within the cohesion policy in the financial perspective 2014–2020 (Dz.U. 2014 item 1146 with later amendments) refers to the definition of an irregularity set forth in Regulation 1303/2013.

³⁵ Judgment of 26 May 2016, *Județul Neamț i Județul Bacău*, C-260/14 and C-261/14, EU:C:2016:360, item 34.

³⁶ Chapter 5 item 2 of the Guidelines of the Minister of Investments and Development on correcting and recovering undue spending and reporting on irregularities within operational programmes of the cohesion policy for 2014–2020, Warszawa, 3 December 2018.

Funds, with the exception of a Member State exercising its prerogatives as a public authority. So in the first place, an entity that may commit an irregularity is a beneficiary responsible for project implementation, or, also, an entity that on behalf of a beneficiary incurs eligible expenditure within the project, a public procurement contractor, or any other person involved in the project. It means that despite the lack of an illegal deed on the part of a beneficiary, this very beneficiary will take the consequences, because the ineligible expenditure will not be settled within the project, and in case it has already been refunded – the beneficiary will have to return it, being the party to the grant agreement. An irregularity will not occur in the case of a public authority prerogative of a given Member State. This exception must be, however, compliant with the judicature of the Court of Justice³⁷, narrowly interpreted, and it will not comprise situations when, e.g. an administration body within its responsibilities related to the road infrastructure development implements a European project, or the administration's activities related to the implementation of a technical assistance project supporting the effectiveness of an operational programme implementation.

4. Indicating a damaging impact on the EU budget, through at least a threat to burden

it with ineligible expenditure. This premise makes the definition of irregularity applied in the funds implementation different from the common understanding of the term. The very occurrence of a breach of law and assigning responsibility for it to a given entity is not sufficient to identify an irregularity as understood in the EU regulations, since it is also necessary to demonstrate that the breach has or may have a negative impact on the EU finances. Thus it is sufficient to identify the very risk of financing of an ineligible expenditure, i.e., e.g., a situation when a breach has been identified during the beneficiary's payment claim verification (potential damage). When such a breach was not detected, it would result in declaring an ineligible expenditure to the EC, which would cause – if the refund was made – damage to the EU budget (actual damage). In such a situation, a Member State is obliged to make financial corrections, applying the proportionality principle, i.e. adjusting financial consequences to the nature and gravity of the breach and its impact on the EU budget³⁸. Estimating a damage value is usually troublesome, particularly in the case of breaches in the public procurement area. That is why the EC adopted, upon its decision³⁹, guidelines setting the rates of corrections depending on a breach type, and its impact

³⁷ Item 4 of the Handbook on Reporting of irregularities in shared management (2017), developed by OLAF in cooperation with Member States experts, <https://www.eu-skladi.si/sl/dokumenti/navodila/handbook-irregularity-reporting-final.pdf>.

³⁸ Article 143(2) of Regulation 1303/2013.

³⁹ Commission Decision of 14 May 2019 laying down the guidelines for determining financial corrections to be made to expenditure financed by the Union for non-compliance with the applicable rules on public procurement (C(2019) 3452final).

on fair competition and equal treatment of contractors. It is worth observing that, in accordance with the judicature of the Court of Justice, an obligation to return an unduly paid amount is not a sanction, but just a consequence of stating that the requirements for its obtaining have not been met, which resulted in an unduly paid amount⁴⁰.

The definition of fraud is yet more complex⁴¹. Currently it is included in Article 3(2) of the PIF Directive. Previously, a fraud was defined in a similar way in Article 1 of the Convention of 1995 on the protection of the European Communities' financial interests, which was replaced with the PIF Directive. The definition indicates which situations are regarded as fraud, separately for expenditure and separately

for EU budget revenues. In addition, the expenditure part, despite identical types of breaches, is divided into expenditure related and unrelated to public procurement. For instance, fraud in relation to expenditure occurs if false documents have been submitted in order to embezzle funds, or if funds have been used for other purposes than those for which they have been allocated. All the cases discussed in the definition must be treated by Member States as criminal offences if they have been intentional. Recital 11 of the PIF Directive emphasises that provisions of the Directive are applied only with regard to offences that require intention. Article 4 of the PIF Directive gives an equal status to several categories of criminal offences if they breach the Union's financial interests,

⁴⁰ Judgment of 26 May 2016, *Județul Neamț i Județul Bacău*, C-260/14 and C-261/14, EU:C:2016:360, item 50, and the judicature referred to therein.

⁴¹ For the purposes of this Directive, the following shall be regarded as fraud affecting the Union's financial interests: in respect of non-procurement-related expenditure, any act or omission relating to: (i) the use or presentation of false, incorrect or incomplete statements or documents, which has as its effect the misappropriation or wrongful retention of funds or assets from the Union budget or budgets managed by the Union, or on its behalf; (ii) non-disclosure of information in violation of a specific obligation, with the same effect; or (iii) the misapplication of such funds or assets for purposes other than those for which they were originally granted; in respect of procurement-related expenditure, at least when committed in order to make an unlawful gain for the perpetrator or another by causing a loss to the Union's financial interests, any act or omission relating to: (i) the use or presentation of false, incorrect or incomplete statements or documents, which has as its effect the misappropriation or wrongful retention of funds or assets from the Union budget or budgets managed by the Union, or on its behalf; (ii) non-disclosure of information in violation of a specific obligation, with the same effect; or (iii) the misapplication of such funds or assets for purposes other than those for which they were originally granted, which damages the Union's financial interests; in respect of revenue other than revenue arising from VAT own resources referred to in point (d), any act or omission relating to: (i) the use or presentation of false, incorrect or incomplete statements or documents, which has as its effect the illegal diminution of the resources of the Union budget or budgets managed by the Union, or on its behalf; non-disclosure of information in violation of a specific obligation, with the same effect; or (iii) misapplication of a legally obtained benefit, with the same effect; in respect of revenue arising from VAT own resources, any act or omission committed in cross-border fraudulent schemes in relation to: (i) the use or presentation of false, incorrect or incomplete VAT-related statements or documents, which has as an effect the diminution of the resources of the Union budget; (ii) non-disclosure of VAT-related information in violation of a specific obligation, with the same effect; or (iii) the presentation of correct VAT-related statements for the purposes of fraudulently disguising the non-payment or wrongful creation of rights to VAT refunds.

including money laundering, passive and active corruption and misappropriation.

Interestingly, the Commission Delegated Regulation No 1970/2015 on the reporting of irregularities concerning the cohesion policy⁴² contains a definition of “suspected fraud”. In accordance with Article 2 letter a of the said regulation, it means an irregularity that gives rise to initiating administrative or judicial proceedings at the national level in order to confirm intentional behaviour, in particular fraud⁴³. Therefore, this provision directly relates the notion of fraud to the notion of an irregularity. Thus, the construction of the provision assumes that fraud means an irregularity that requires intention. In this way, intention is a distinctive feature that differentiates an irregularity from fraud. OLAF indicates that fraud is an intentional offence committed for own benefit or for the other party’s losses⁴⁴. Therefore it can be said that fraud is an aggravated form of an irregularity, to be identified when intention is stated. At the same time, in accordance with the requirement of the PIF Directive, such fraud must be considered a criminal

offence in accordance with national criminal provisions (Article 3 point 1).

Considering the above, one can say that fraud – in national criminal regulations, i.e. mainly in penal codes – will be understood as an intentionally committed offence related to depletion of EU finances⁴⁵. These include officials’ venality, bribery, negligence, power abuse, offences against information protection, offences related to documents reliability, disturbing public procurement. Such offences are mostly related to undue benefits and, if they risk the Union’s financial interests, will be regarded as fraud. In conclusion, each fraud is also an irregularity, whereas not every irregularity is fraud, since it is less possible to confirm that it has been committed in an intentional and purposeful manner.

Protecting the Union's financial interests

Over the last decades, a gradual development of legal regulations and mechanisms aimed to protect the Union’s financial interests has been observed⁴⁶. Institutions

⁴² COMMISSION DELEGATED REGULATION (EU) 2015/1970 of 8 July 2015 supplementing Regulation (EU) No 1303/2013 of the European Parliament and of the Council with specific provisions on the reporting of irregularities concerning the European Regional Development Fund, the European Social Fund, the Cohesion Fund, and the European Maritime and Fisheries Fund L 293/1 of 10 November 2015.

⁴³ A suspected fraud with regard to expenditure of the cohesion policy incurred in the financial perspective 2007–2013 was defined in the same way (Article 27 letter (c) of the Regulation of the EC 1828/2006 of 8 December 2006 setting out rules for the implementation of Council Regulation (EC) No 1083/2006 laying down general provisions on the European Regional Development Fund, the European Social Fund and the Cohesion Fund and of Regulation (EC) No 1080/2006 of the European Parliament and of the Council on the European Regional Development Fund.

⁴⁴ <https://ec.europa.eu/anti-fraud/olaf-and-you/report-fraud.pl>

⁴⁵ JAFS 2015–2020, p. 10.

⁴⁶ See also: Summary of the most important initiatives indicating crucial moments in the area of the fight against fraud presented in the 30th jubilee annual report on the protection of the financial interests of the European Union and the fight against fraud for 2018: https://ec.europa.eu/anti-fraud/sites/default/files/pif_report_2018_pl.pdf.

and task forces have been established to deal with the issue and with international cooperation in the area. Horizontal regulations are binding regardless of the EU financial frameworks, and are applied to various programming periods in which cohesion policy objectives are implemented. Provisions of Regulation 2988/95 can serve as an example here – these have been in force (since 1995), and so have been throughout Poland's presence in the EU. Fight against fraud has become one of the priorities of the EC, which is obliged to implement the EU budget in an appropriate manner. The breakthrough in the area was the establishment, within the EC, of the Anti-Fraud Coordination Unit (UCLAF⁴⁷) in 1988. UCLAF was tasked with supervising the EC's activities related to fight against fraud, in cooperation with national bodies, and with coordinating fight against organised financial crime. The Treaty of Maastricht⁴⁸, which entered into force in 1993, in Article 209a obliges Member States to coordinate – with the EC – their activities aimed to protect the EU financial interests, as well as – for the first time – emphasises that Community funds should be protected in the same

way in which Member States protect their own finances.

In 1994, the Advisory Committee for the Coordination of Fraud Prevention (COCOLAF)⁴⁹ was established, composed of representatives of Member States, and was tasked with advising the EC on the matters related to:

- fraud prevention,
- cooperation between Member States and the Commission, and prosecuting fraud, and other matters related to legal protection of the Union's financial interests.

At the same time, an obligation was introduced to inform the EC on irregularities detected and to recover funds paid unduly⁵⁰. A year later, a Convention on Protection of the European Communities' financial interests was signed, which – as has been already stated – defined the notion of fraud. Later, the horizontal acts were adopted that are still binding, i.e. Regulation 2988/95 and Regulation 2185/96⁵¹, which state, among others, that the measures applied to fraud combating should be effective, proportionate and deterring. Provisions of the regulations set out the principles for EU's audits in Member States, aimed at fighting fraud.

⁴⁷ From the French name of the Unit: *Unité de coordination de la lutte antifraude*.

⁴⁸ OJ C 191, 29.7.1992.

⁴⁹ Decision of the Commission of 23 February 1994 establishing the Advisory Committee for the Coordination of Fraud Prevention (94/140/EC), OJ L 061, 04/03/1994 P.0027–0028 – COCOLAF, from the French name of the Committee: *Le comité européen pour la coordination dans le domaine de la lutte contre la fraude*.

⁵⁰ Commission Regulation (EC) No 1831/94 of 26 July 1994 concerning irregularities and the recovery of sums wrongly paid in connection with the financing of the Cohesion Fund and the organisation of an information system in this field OJ L 191, 27.7.1994, p. 9–12 and Commission Regulation (EC) No 1681/94 of 11 July 1994 concerning irregularities and the recovery of sums wrongly paid in connection with the financing of the structural policies and the organisation of an information system in this field OJ L 178, 12.7.1994, p. 43–46.

⁵¹ Council Regulation (Euratom, WE) No 2185/96 of 11 November 1996 w concerning on-the-spot checks and inspections carried out by the Commission in order to protect the European Communities' financial interests against fraud and other irregularities, OJ L 292, 15/11/1996.

Regulation 2185/96 provides for an opportunity to check all contractors of final beneficiaries, and it is a basic tool for detecting fraud. In 1997, a revision of the EU Treaty took place, and the changes to Article 209a of the Treaty of Maastricht led to the current wording of Article 325 of the Treaty of Lisbon. This regulation obliges the EC to annually present the European Parliament and the Council with reports on the implementation of obligations related to ensuring effective protection of the Union's financial interests.

European Anti-Fraud Office Group of States Against Corruption (GRECO)⁵²

Another milestone in the fight against fraud was the establishment, in 1999, of OLAF⁵³ that took over the competence of UCLAF. The creation of OLAF was related to the financial scandal within the very EC, resulting in the demission of all Commissioners headed by Jacques Santer⁵⁴. In the aftermath, the European Parliament – for the first time – did not discharge the EC's budget. OLAF is an investigation service of the European institutions, and it is functionally independent of the

EC. It has the right to have insight into all the matters related to EU funds management, financing of EU institutions and the Union's revenues. OLAF protects the Union's financial interests mainly through administrative investigations in Member States, or in EU institutions, units, offices and agencies.

It is worth noting that in May 1999 the Council of Europe (that gathers, among others, all EU Member States) established the Group of States Against Corruption (GRECO)⁵⁵. The group takes measures aimed at corruption combating. The group members are subject to mutual checks and evaluations that decide whether the members' activities are compliant with anti-corruption standards of the Council. GRECO also administers an internet platform of good practices with regard to corruption prevention and detection. Twenty leading principles for the fight against corruption were set in the Resolution of the Council of Europe No (97) 24⁵⁶. National authorities should apply them in everyday practice and legislature. The latest report on evaluation of the anti-corruption standards implementation in Poland was adopted on 7 December 2018⁵⁷.

⁵² From French: *Groupe d'Etats contre la corruption*

⁵³ Commission Decision of 28 April 1999 r. establishing the European Anti-Fraud Office (OLAF) (notified as SEC(1999) 802), OJ L 136, 31.5.1999.

⁵⁴ The case was judged by the Court of Justice, judgment of 11 July 2006 C-432/04, in which the Court confirmed the fraud committed by former Commissioner Edith Cresson, however financial consequences were not applied (pension reduction).

⁵⁵ Resolution of the Council of Europe No (99) 5 establishing the Group of States Against Corruption (GRECO), adopted by the Council of Ministers on 1 May 1998 at 103th Session.

⁵⁶ <https://rm.coe.int/CoERMPublicCommonSearchServices/DisplayDCTMContent?documentId=09000016806cc17c>

⁵⁷ <https://www.coe.int/en/web/greco/evaluations/poland>

Further challenges after EU enlargement

In the years 2004–2007, the biggest enlargement of the EU in the history took place with twelve new members admitted, including Poland, which implied a significant increase in the budgetary expenditure. Several years back, the majority of Member States of the so called old EU adopted the new euro currency, while the year 2007 marked the beginning of a worldwide economic crisis. All these posed a great challenge as for protection of financial interests and prompted the need to increase coordination and efforts on the part of both European institutions and Member States aimed at safeguarding effective protection of the Union's budget, in accordance with the requirements set forth in the Treaty of Lisbon, in force since 2009.

In 2004, the EC launched the “Hercule” programme for Member States to financially support all activities aimed at fighting irregularities, fraud and corruption that have an impact on the EU budget. The funds can be used, e.g. on specialist training and exchange of information and best practices among bodies responsible for law enforcement with regard to fraud combating in the whole of Europe. For the financial perspective 2021–2027 the pool of funds of the programme amounts to EUR 181 million⁵⁸. It is also worth mentioning that it is possible to finance anti-corruption

activities from other sources. In the financial perspective 2014–2020, an opportunity was created to support such activities from the Technical Assistance Operational Programme, as well as from technical assistance components of other programmes implemented within the cohesion policy. Activities of anti-corruption nature related, e.g. to the rule of law, can also be financed from the Technical Support Instrument managed by the EC. The budget of the Instrument for 2021–2027 amounts to EUR 864 million. Other sources to support anti-corruption activities are the EEA Financial Mechanism and the Norwegian Financial Mechanism.

Reform of OLAF and public procurement system

The last decade has witnessed a significant intensification of the measures related to the Union's budget protection. It started with the adoption, in 2011, of the ambitious Commission Anti-Fraud Strategy (CAFS 2011)⁵⁹. It emphasises the importance of engaging all entities that manage European funds in irregularities prevention, especially through establishing effective systems for management and control, which should also provide for the risk of irregularities. The strategy encourages to increase transparency in funds spending, as well as emphasises the necessity to comply with the highest standards of ethical conduct. One of the

⁵⁸ https://ec.europa.eu/commission/presscorner/detail/en/IP_18_3967

⁵⁹ Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee, and the Commission of the Regions and the Court of Auditors on the Commission Anti-Fraud Strategy, 24 June 2011, COM(2011) 376.

strategy priorities is to include, in sectoral provisions related to EU funds spending, issues related to fraud combating, increasing the role of OLAF, and simplification of the provisions in the area of public procurement.

The result of the first priority implementation was the introduction, in the provisions of Regulation 1303/2013, of the obligation for managing authorities to put in place anti-fraud measures. It was supplemented with the designation procedure which is a kind of accreditation of institutions that manage EU funds by independent auditors, tasked with certifying that the requirements related to establishing a robust internal control system are met, and also taking into account activities related to prevention and detection of fraud⁶⁰. Interestingly enough, in Poland the legislation foresees a non-obligatory participation of the President of NIK, the Head of the Central Anti-Corruption Bureau and the Head of the Internal Security Agency in the designation committee. Also, provisions of Regulation 1303/2013 introduce the system for annual settling of expenditure and a related instrument that allows the EC to impose net financial

corrections that imply irretrievable loss of part of the funds assigned to Member States for operational programmes implementation. This applies when the control system in a Member State does not function properly, which leads to systemic irregularities. This makes a significant disciplinary element, which is reflected in the substantial number of the so called doubtful expenditure indicated by Member States, for which full regularity cannot be confirmed⁶¹ (e.g. due to criminal proceedings in progress). Such activities demonstrate appropriate management of expenditure by Member States and allow for avoiding the EC's net corrections.

In order to enhance fight against fraud through OLAF investigations, a reform of the institution was introduced, and OLAF started operating on the basis of Regulation 883/2013⁶². The operations of units that coordinate fight against fraud (AFCOS⁶³), which every Member State has to establish, have also been reformed. The main task of AFCOS is to ensure effective cooperation and exchange of information with OLAF, including operational information⁶⁴. In Poland, the functions of AFCOS are performed – on behalf of

⁶⁰ Annex XIII to Regulation 1303/2013: Designation criteria for the managing authority and certifying authority.

⁶¹ Dr Lothar Kuhl, *Implementation of Effective Measures against Fraud and Illegal Activities in Cohesion Policies. An Analysis of Current Structures, a Discussion of Reform Ideas and a Look Towards Changes by the European Public Prosecutor's Office*. Eucrium 2/2020 THE EUROPEAN CRIMINAL LAW ASSOCIATIONS' FORUM, <https://eucrim.eu/issues/2020-02/>

⁶² Regulation of the European Parliament and of the Council (UE, Euratom) No 883/2013 of 11 September 2013 concerning investigations conducted by the European Anti-Fraud Office (OLAF) and repealing Regulation (EC) No 1073/1999 of the European Parliament and of the Council and Council Regulation (Euratom) No 1074/1999.

⁶³ Anti-fraud coordination service.

⁶⁴ Detailed tasks of AFCOS were set out in the Guidance note on main tasks and responsibilities of an Anti-Fraud Coordination Service (AFCOS), 13 November 2013, Ares (2013) 3403880.

the Government's Proxy for Fight Against Irregularities to the detriment of Poland or the EU Financial Interest – the Head of the National Revenue Administration – an organisational unit at the Ministry of Finance (currently the Department of Public Funds Auditing)⁶⁵.

In 2014, new directives were also adopted in the area of public procurement, taking into account the EC Anti-Fraud Strategy of 2011, related to, among others, increasing transparency of bids, mainly through digitisation of the procurement process, and prevention of conflict of interests in public procurement through providing a definition of the concept.

EC's report on fight against corruption

At the beginning of 2014, the EC published, for the first time in the history, a report related to fight against corruption in the EU. For the purposes of the report, corruption is understood in a very broad way, i.e. as all sort of abuse of power for private gain. The value of the document is high, as it presents the state of fight against corruption separately for each Member State, indicates best practices, as well as weaknesses and areas where improvements should be made. The report shows that Member States have made significant efforts in fighting corruption, but still these are not sufficient. The report indicates several issues being common challenges to all Member States. The most corruption prone area, according to the report, is public procurement, where

about one-fifth of GDP is spent. The document also draws attention to the political dimension of corruption, including deficiencies related to e.g. financing of political parties. The report emphasises the role of independent courts for effective implementation of anti-corruption policies. It also draws attention to the problems resulting from conflict of interests, and the lack of sufficient mechanisms to prevent risks in the area. As for Poland, attention is drawn to the lack of a strategic and comprehensive approach to fight against corruption. In the opinion of the EC, efforts should be made to prevent the Central Anti-Corruption Bureau from being politically involved, as well as to strengthen anti-corruption measures in the area of public procurement, supervision of State owned companies, and with regard to corruption risks in the health sector. As an example of a corruption issue, collusive bidding in the road infrastructure sector is recalled, which resulted, at the end of 2012, in the EC suspending EU funds refund in the amount of almost EUR 1 billion. While the only good practice in Poland, according to the report, is the activity of the Supreme Audit Office, which not only identifies irregularities, but proposes taking systemic regulatory measures, aimed at introducing improvements. The report was supposed to be updated every two years, yet it failed to continue. The only exception was the inclusion of the issue of corruption fighting within the European Semester in 2018, which will be discussed later in this article.

⁶⁵ Article 14(1)(18) of the Act on the National Revenue Authority (Dz.U.2021.422 with later amendments).

Joint Anti-Fraud Strategy 2015–2020

At the end of 2015, three Directorates-General of the EC⁶⁶ responsible for implementation of structural and investment funds, in cooperation with OLAF, developed the Joint Anti-Fraud Strategy 2015–2020 (JAFS 2015)⁶⁷, which focused on protection of the funds spent, among others, within the cohesion policy. The strategy is an operational document serving the implementation of the general strategy of the EC (CAFS 2011). The document comprises specific measures to be implemented by the EC's Directorates-General that manage EU funds. JAFS 2015 focuses on two fundamental priorities. Firstly, it indicates the necessity to conduct an analysis of the way in which Member States meet the requirement to systematically analyse fraud risks. The analysis was made through a survey on a sample of 50 operational programmes and system audits of the EC in selected Member States, aimed to examine how their authorities meet the designation criteria, especially with regard to implementation of the measures for fighting fraud⁶⁸. The other priority is increasing the use of information technology tools in order to improve fraud detection. In this area, the EC's efforts were supposed to focus on promoting and encouraging the

use of the ARACHNE IT tool, developed by the EC with an objective to better select projects to be audited, and to assist identification, prevention and detection of fraud (ARACHNE system will be discussed in the second part of this article). In addition, JAFS 2015 sets three goals. The first goal addresses the services of individual Directorates-General, and comprises measures related to strengthening cooperation with academics, increased dissemination of information related to corruption, and making the EC's officials more sensitive to fight against fraud issues. The second goal is supposed to be implemented with regard to Member States, and to focus, among others, on ensuring that they are equipped with appropriate guidance, recommendations and manuals associated with fraud prevention and detection, as well on strengthening cooperation within thematic working groups. The third goal focuses on ensuring implementation of OLAF's recommendations comprised in reports that conclude fraud related investigations.

In 2015, Directorate-General for Regional and Urban Policy of the EC, together with Transparency International, decided to launch a pilot project related to the use of the so called integrity pact in projects financed from EU funds. This was, in the

⁶⁶ DG Regional and Urban Policy, DG Employment, Social Affairs and Inclusion, DG Maritime Affairs and Fisheries.

⁶⁷ <https://ec.europa.eu/sfc/sites/default/files/sfc-files/JOINT%20ANTI-FRAUD-STRATEGY2015-2020.pdf>

⁶⁸ *Preventing fraud and corruption in the European Structural and Investment Funds – taking stock of practices in the EU Member States – Study on the implementation of Article 125(4)(c) of the Regulation (EU) No 1303/2013 laying down the common provisions on the European Structural and Investment Fund in Member States.* https://ec.europa.eu/regional_policy/en/information/publications/studies/2019/preventing-fraud-and-corruption-in-the-european-structural-and-investment-funds-taking-stock-of-practices-in-the-eu-member-states

first place, aimed at increasing transparency of the public procurement process, and at engaging society in monitoring of public funds spending. The initiative will be discussed in more detail in the second part of this article.

Harmonisation of criminal provisions to fight fraud

The pace of applying anti-fraud measures in the last decade has been maintained, which resulted in the adoption of two important legal acts that strengthened the protection of the EU budget with the use of criminal law. The first act is the PIF Directive, which has already been referred to in this article. The Directive harmonises the definitions, sanctions and the statute of limitations for the crimes that breach the Union's financial interests. The Directive is also the basis for the activity of the European Public Prosecutor's Office that was established (also in 2017) under another legal act⁶⁹, tasked with investigating and prosecuting fraud. The establishment of the European Public Prosecutor's Office has also been an embodiment of the decision included in Article 86 of TFEU. Participation in this initiative is not obligatory, and currently 22 states are involved in the programme (excluding Poland)⁷⁰. The European Public Prosecutor's Office has the same investigation mandate in the whole EU, and operates on the basis of

national legal systems of Member States, within their structures. The introduction of the European Public Prosecutor's Office has also triggered some changes in the operations of OLAF, currently at the stage of legislative proceedings⁷¹.

In mid-2018, the so called Omnibus regulation was adopted, consisting of changes to some legal acts related to implementation of European funds, especially Regulation 1303/2013 and the EU Financial Regulation. The objective of amendments was to simplify implementation principles, to make them more flexible, to eliminate the so called bottlenecks, and to increase expenditure policy's focus on results. The amendments include the expanded scope of simplified methods for expenditure settlement, which replaced detailed analyses of individual costs. As for fraud, the key changes were related to redefining of and a new approach to the issue of conflict of interests, which should result in increased transparency in budget expenditure.

Regulation on the general conditionality system

Simultaneously with the Omnibus regulation, the EC proceeded with a proposal for adopting a regulation on the protection of the Union's budget in case of generalised deficiencies as regards the rule of law in Member States⁷², based on the assumption that compliance with the principles of the

⁶⁹ Regulation of the Council (EU) 2017/1939 of 12 October 2017 implementing enhanced cooperation on the establishment of the European Public Prosecutor's Office OJ UE L 283/1.

⁷⁰ Austria, Belgium, Bulgaria, Croatia, Cyprus, Czech Republic, Estonia, Finland, France, Germany, Greece, Italy, Latvia, Lithuania, Luxembourg, Malta, the Netherlands, Portugal, Romania, Slovakia, Slovenia and Spain.

⁷¹ https://www.europarl.europa.eu/doceo/document/TA-8-2019-0383_PL.html#title1

⁷² Proposal of EC of 2 May 2018 COM(2018) 324 final.

rule of law is a prerequisite for sound financial management. In accordance with the proposal, the EU should have a possibility to suspend, on the basis of proportionality, the access to financing in case the principles of the rule of law have been breached. The proposal was well received by the ECA⁷³ that, however, pointed at some shortcomings, mostly related to the lack of clear and specific criteria to judge what should be regarded as a “deficiency” in the rule of law that may threaten sound financial management. Ultimately, the proposal was adopted through the Regulation of the European Parliament and of the Council 2020/2092 on a general regime of conditionality for the protection of the Union budget (Conditionality Regulation⁷⁴), in force since 1 January 2021.

The provisions of the Regulation allow the EC to apply for suspension of European funds for a Member State that, in the opinion of the EC, breaches the principles of the rule of law. A decision on suspension of payments can be taken by the Council of the European Union with a qualified majority⁷⁵. It should be observed that already in the sectoral provisions related to implementation of funds within the cohesion policy (e.g. Regulation 1303/2013), the EC can on its own take a decision on interrupting a payment deadline, on suspending a payment, or on imposing a financial correction on an operational programme (reduce

commitments within the programme). Such decisions can be taken mainly in cases when deficiencies have been identified in the management and control system of the given programme, or when a serious irregularity has been detected in the expenditure declared to the EC – if these have not been corrected by the respective Member State. It is worth noting that sanctions relate only to a specific operational programme where deficiencies have been found. While in the case of the Conditionality Regulation:

- firstly, the portfolio of disciplinary measures that may be implemented is broader and covers, e.g. possibility to suspend programme approval, or to suspend advance payments for a Member State;
- secondly, a lot of freedom is left as for the scope of the measures implemented. Measures must indeed be proportionate and adequate to the nature and gravity of a breach, yet in fact they may cover all programmes and support instruments financed from the EU budget;
- thirdly, the portfolio for implementing sanctions is much wider, yet a breach of the rule of law must at least create a risk of affecting sound financial management, or the protection of the Union’s financial interests. The EC will then have to demonstrate a relation (sufficiently direct) between deficiencies and their negative impact on EU funds spending. What is more, a breach must be related to at least

⁷³ Opinion No 1/2018 concerning the proposal of 2 May 2018 for a regulation of the European Parliament and of the Council on the protection of the Union’s budget in case of generalised deficiencies as regards the rule of law in the Member States (2018/C 291/01).

⁷⁴ Regulation on a general regime of conditionality for the protection of the Union budget of 16 December 2020, L 433 I/1.

⁷⁵ Supported by 55 percent of Member States, representing at least 65 percent of the EU population.

one out of the eight premises enumerated. A breach may be related not only to inappropriate activities of bodies that directly manage and control EU funds, but also e.g. to the activity of law enforcement bodies that conduct investigations related to fraud, the activity of courts that supervise those bodies, as well as cooperation with OLAF. The most broad-ranging and unclear is the latest condition (Article 4(2)(h) of the Regulation) which relates to “other situations or conduct of authorities that are relevant to the sound financial management of the Union budget or the protection of the financial interests of the Union”.

Interestingly, sanctions cannot cause damage to beneficiaries and final recipients of support, which means that a Member State has to bear its liabilities even if, e.g. a financial correction has been imposed on the given operational programme. European financing will in this way have to be replaced with national financing.

Measures are lifted by the Council of the EU, yet upon motion by the EC that, at its own discretion, decides whether breaches have been eliminated by the Member State or not.

The adoption of the provisions related to conditionality was accompanied with the conclusions, issued by the Council⁷⁶, which are not binding, but provide a desired way of interpretation and application of the Regulation’s provisions. The document

emphasises that the Union’s budget must be protected against any fraud, corruption and conflict of interests. Moreover, the mechanism must be applied in an objective, fair, unbiased and facts-based manner, in order to ensure procedural fairness, non-discrimination and equal treatment of Member States. The conclusions also oblige the EC to issue guidance that will determine the mode of the Regulation application. It is aimed to prevent arbitrariness of the EC in the application of the conditionality mechanism.

It needs to be emphasised, that the provisions of the Regulation directly state (Article 4(1)) that a breach of the rule of law principle itself does not suffice for imposing sanctions. It is necessary to identify potential negative impact of the breach on the funds spent from the EU budget. Furthermore, the provisions set a catalogue of breaches categories. The EC is also obliged to, in accordance with the procedure set forth in the Regulation, appropriately justify its decision and to indicate concrete reasons for the decision. What is more, the EC must also consider the information and comments received from Member State to be subject to sanctions, and take a position on them. All these clearly differentiate the conditionality mechanism from other provisions and procedures serving to discipline Member States and to make them compliant with the EU laws⁷⁷.

⁷⁶ <https://www.consilium.europa.eu/media/47337/1011-12-20-euco-conclusions-pl.pdf>

⁷⁷ Compare with: Procedure of application of Article 260 of TFEU aimed to execute implementation by Member States of the judgments by the Court of Justice, presented in the article by Łukasz Augustyniak. 2020. “Financial Sanctions for EU Member States - Execution of Supervision Function by the Court of Justice of the EU”. *Kontrola Państwowa* 1, pp. 34-59.

Therefore, the provisions of the Regulation refer primarily to breaches that are not necessarily considered an offence in the meaning of criminal regulations. These breaches are related to corruption in a broad understanding of the term, and may relate to abuse of power or position aimed at particularistic interests that favour one specific group only⁷⁸. This means, e.g. establishing organisational structures and legal regulations to favour a specific group of beneficiaries, and simultaneously fail to allow for appropriate control and accountability. Such activities are referred to as “legal corruption”, which is embedded in the system. At this point, we can refer to the concept of Robert Klitgaard⁷⁹, according to whom corruption means monopoly of authorities and discretionary decisions, with simultaneous lack of accountability. In EU funds implementation, such dangerous situations may comprise e.g. setting such funds disbursement procedures that favour a specific group of recipients, or lack of appropriate measures and control on the part of, e.g. law enforcement bodies in the case of suspected fraud with regard to the privileged group. From this perspective, it seems justified to introduce a tool to discipline Member States, under the condition that full objectivity, impartiality and proportionality are ensured with regard to application of measures related to the rule of law principles, set forth in

Article 2 letter (a) of the Conditionality Regulation are not adhered to, i.e.:

- principle of legality, which means a transparent, accountable, democratic and pluralistic law-making process,
- legal certainty,
- prohibition of arbitrariness of the executive powers,
- effective judicial protection, including access to justice, by independent and impartial courts, also as regards fundamental rights,
- separation of powers.,
- non-discrimination and equality before the law.

The very fact that this issue has been regulated should work as a deterrent, and discourage activities that breach the above principles.

Matters related to the mechanisms for suspending EU funds payments due to the rule of law principles breaches triggered public debates and numerous controversies, especially in Poland. What is more, in March 2021, Poland filed a complaint to the Court of Justice of the European Union as for the mechanism’s in compliance with the TFEU, claiming, e.g. that such solutions have no legal basis in the Treaties, that they interfere with Member States’ competence, and breach the law of the European Union⁸⁰. The Polish party emphasised that the mechanism for imposing sanctions for breaching the rule of law

⁷⁸ Compare with: Waldemar Walczak. 2019. “Abuse of public authority as a corruption element – a broader perspective attempt”. *Kontrola Państwowa* 3, p. 110 and Grzegorz Makowski. 2019. *Preparing the ground for “great corruption”*. (Anti)corruption activity of the authorities in the years 2015–2019, pp. 4-11.

⁷⁹ Concept presented in: Robert Klitgaard. 1988. *Controlling corruption*, University of California Press.

⁸⁰ <https://www.gov.pl/web/premier/skarga-do-trybunalu-sprawiedliwosci-ue>.

principles has already been set forth in Article 7 of the TFEU, and it should form the only grounds for assessing Member State's compliance with the values set forth in Article 2 of the Treaty. It seems that the EC's intention was to provide complementarity of the provisions with sectoral and financial regulations. Both the EC and the Council have declared that the provisions of the Regulation will be included, at the earliest convenience, in the EU financial regulation. So the basic objective of the mechanism is not the very assessment of compliance with the rule of law principles, but the protection of financial interests from undue spending from EU budget funds. As it has been previously stated, possibilities for imposing financial sanctions are set forth in sectoral provisions, and the EC has many times applied the mechanisms related to suspension of payments to Member States⁸¹, or imposing net financial corrections⁸². However, considering the importance of the issue and existing legal doubts, an opinion by the Court of Justice, i.e. the body relevant for interpreting and enforcing the EU law, is highly desired. The Court's decision should indicate whether it will be possible to use the conditionality mechanism, which has

not been explicitly based on the provisions of the Treaty.

Prevention of European support concentration

In 2018, in a resolution⁸³ the European Parliament expressed the expectation of Member States to collect and send to the EC the data on actual beneficiaries who receive the highest support from the Union (beneficial owners). The objective is to prevent support concentration in the hand of a potentially privileged group or oligarchic structure. Requirements in the area are expected to be introduced, among others, in sectoral provisions on EU funds implementation in the financial perspective 2021–2027.

Corruption related matters in European Semester⁸⁴

In 2018, fight against corruption was also identified as a priority for the economy management process within the European Semester. A vast part of national reports comprised an evaluation of the anti-corruption legal, political and institutional environments. Several Member States also received recommendations related to strengthening their anti-corruption

⁸¹ For instance, suspension of payments related to suspected conflict of interests of the Prime Minister of the Czech Republic: <https://www.euractiv.pl/section/instytucje-ue/news/ke-zamraza-unijne-dotacje-dla-firm-zwiazanych-z-premierem-czech/>

⁸² More details: Justyna Łacny. 2015. "Korekty finansowe nakładane na państwa członkowskie UE". *Kontrola Państwowa* 1.

⁸³ Item 26 of the European Parliament resolution of 14 May 2018 with observations forming an integral part of the decisions on discharge in respect of the implementation of the general budget of the European Union for the financial year 2018, Section III – Commission and executive agencies (2019/2055(DEC)).

⁸⁴ European Semester, since 2011, a procedure of the European Commission to coordinate economic and budget policy in the EU. An element of the EU economic management. The basic objective of the European Semester is to better consider the European perspective in planning national economic strategies.

measures, eliminating deficiencies in their public procurement procedures, and increasing accountability of the prosecutor's office and police⁸⁵.

ECA Audits on anti-fraud measures

In 2019, the European Court of Auditors (ECA) finalised its works on the results of two audits related to the EC's activities (January, report No 1/2019), and to those of Member States (May, report No 6/2019) related to meeting obligations regarding fight against fraud. Despite numerous initiatives and efforts, the ECA identified a number of weaknesses, and concluded that fight against fraud must be significantly intensified.

In its 1/2019 report⁸⁶ – on the audit of performance of tasks by the EC, the ECA stated that the Commission did not have complex and comparative comparable data on the scale of fraud in European resources spending, which significantly reduced the usability of strategic documents developed in the area.

The report also indicated that the EC did not estimate the scale of “undetected fraud” at all. Moreover, the ECA criticised the value of OLAF's investigations and stated that they are not effective, as being highly time-consuming, which could lead, among others, to the failure in punishing perpetrators, as well as to the failure to recover unduly spent funds. The Court

judged that persons suspected of committing fraud were charged only in less than a half of OLAF's investigations, and only one-third of unduly paid EU funds were recovered. Surprisingly enough, financial recommendations of OLAF addressed individual directorates of the EC are not binding⁸⁷. Additionally, OLAF informs national bodies of suspected crime usually not earlier than three years after this alleged crime⁸⁸. Therefore, the Court stated that it was necessary to increase determination and to strengthen the Commission's efforts, in cooperation with Member States, to make anti-fraud measures more effective. The ECA's recommendations include:

- introducing a reliable system for reporting on fraud cases, which will allow for providing, in the first place, information on the reasons for fraud;
- adopting a new comprehensive anti-fraud strategy;
- link the adoption of programmes for the financial perspective 2021–2027 with fraud risk analysis;
- convincing all Member States to apply the ARACHNE tool in order to improve the fraud detection system.

They are to redefine the role and responsibilities of OLAF, especially in the context of establishing the European Public Prosecutor's Office. In its special ECA 6/2019 report⁸⁹, the Court evaluated in turn the effectiveness of the activity of operational

⁸⁵ https://ec.europa.eu/info/publications/2018-european-semester-country-reports_pl

⁸⁶ <https://www.eca.europa.eu/pl/Pages/DocItem.aspx?did=48858>

⁸⁷ Item 92 of the ECA special report 01/2019.

⁸⁸ Item 103 of ECA report 01/2019.

⁸⁹ <https://www.eca.europa.eu/en/Pages/DocItem.aspx?did=49940>

programmes managing authorities in the area of fighting fraud. An evaluation supplemented the report on the EC's activity. The Court stated that Member States had not made significant progress as for active fraud detection. At the same time, the ECA observed that managing authorities had improved their risk assessment as for fraud, and improved fraud prevention measures, yet it also emphasised that those analyses were superficial, routine and not very innovative, which reduced their value. The Court judged that anti-fraud measures should be subject to regular evaluations in order to confirm their effectiveness, and identified some significant weaknesses as for measures with regard to detected fraud cases, also related to meeting the requirement to provide regular information on fraud. Moreover, the ECA observed that managing authorities did not use, in a sufficient manner, their potential for advanced analyses to detect fraud, and identified important differences in the structures, competences, roles and responsibilities of AFOCS units in individual Member States, which had a negative impact on their actual function to coordinate the activities of other anti-fraud bodies. Increased efforts with a view to fighting fraud should comprise, in the opinion of the ECA:

- appropriate development of anti-fraud strategies and policies, covering in the first place funds monitoring and implementation mechanisms, and monitoring of results;

- engaging competent entities with necessary experience in risk assessment, mainly law enforcement bodies;
- using the potential of new technologies in data analysis, to facilitate fraud detection;
- monitoring mechanisms for reacting to fraud, including through ensuring a unified approach to reporting on fraud cases;
- increasing the role of AFCOS in order to improve coordination.

EC's new anti-fraud strategy (CAFS 2019)

On 29 April 2019, the EC adopted a new anti-fraud strategy⁹⁰, which included the recommendations formulated by the ECA in its report 1/2019. The main goal of the new strategy is to increase coherence and better coordination of the fight against fraud in individual Directorates-General of the EC. The strategy is also intended to pave the way to fighting fraud, based – to a larger extent – on reliable data. The strategy also identifies OLAF as the main body responsible for elaborating and developing a European policy in the area of fraud fighting. The fundamental priority of the strategy is to equip the EC with full data analysis capacities, in order to prevent and detect fraud. It was deemed necessary to ensure completeness and quality of the data, especially the data gathered within the Irregularities Management System (IMS)⁹¹, which is definitely a correct recommendation, regarding the weaknesses of the reporting system and

⁹⁰ Communication from the Commission Anti-Fraud Strategy: enhanced action to protect the EU budget of 29 April 2019, COM(2019) 196 final.

⁹¹ Irregularity Management System (IMS) – an IT system launched by the European Commission in order to allow Member States meet their obligation to inform about irregularities.

varying approaches to responsibilities in the area adopted by Member States, which also was emphasised by the ECA in its special 6/2019 report. The sources of data may include results of audits, OLAF's investigations, other available databases and scientific research. The data is to be closely analysed with the use of modern intelligent technologies of data scanning. Such analyses are to lead to better understanding of fraud risks and designing their schemes, identification of risk factors, systemic weaknesses, and elaborating the profile of a given Member State.

Harmonisation of the whistleblowing system

In October 2019, a directive was adopted aimed to protect whistleblowers⁹², i.e. persons who report or disclose irregularities in good faith, including such breaches that endanger the Union's financial interests. The directive obliges introduction of solutions for channels for reporting irregularities in the Member States that have not regulated this area yet, and it is supposed to lead to harmonisation and unification of procedures in the field across the whole EU. Considering that the systems for reporting on irregularities are the basic source of detecting breaches, adoption of provisions in the area at the EU level can make a significant breakthrough in the fight against fraud. A more detailed analysis of this issue will be presented in the second part of the article.

New Joint Anti-Fraud Strategy

Following the EC's Strategy (CAFS 2019), in December 2019 an operational plan of the Commission's Directorates dealing with, i.e. spending of funds within the cohesion policy in the form of the Joint Anti-Fraud Strategy 2020–2025⁹³, was redeveloped. In the document, the EC services indicate concrete measures which have been formulated on the basis of the experience in implementing new legal requirements. These measures, at the same time, complement the CAFS 2019, and follow the ones on the basis of JAFS 2015–2020. The measures have been divided into two groups. Obligations to support the efforts of Member States, which are the main responsible parties for combating fraud, constitute the first group. To the other belong the ones to be implemented within the EC itself. The measures related to supporting Member States foresee the necessity to develop an e-learning platform for officials of national institutions, and a tool comprising cases of concrete frauds and ways of combating them. Moreover, guidelines are to be issued on preventing conflict of interests, understood in accordance with its new definition provided in the EU Financial Regulation. In this area, the EC's audits have also been foreseen, aimed to evaluate the effectiveness of the measures to prevent conflicts of interests. The Commission is also to support the use of IT systems, especially ARACHNE,

⁹² Directive (EU) 2019/1937 of the European Parliament and of the Council of 23 October 2019 on the protection of persons who report breaches of Union law, L 305/17.

⁹³ <https://ec.europa.eu/sfc/sites/default/files/jointanti-fraudstrategyforsharedindirectmanagement2020-2025.pdf>.

for detecting fraud by Member States. Among the tasks to be performed by the structures of EC directorates-general, are strengthening cooperation with OLAF and ensuring ongoing information exchange.

Financial framework 2021–2027

During implementation of projects in the new financial perspective 2021–2027, Member States, their managing authorities included, will be responsible for fighting fraud. The provisions related to both the cohesion policy and other instruments will directly indicate responsibilities in the area. Considering the initiatives undertaken and how important it is for all European institutions to protect their financial interests, as well as the experience that Member States gained while implementing programmes during the financial perspective 2014–2020, they will be expected to be more engaged and proactive. Pressure on ensuring an effective anti-fraud system will be strengthened with the provisions of the Conditional Regulation, aimed in its very nature to protect the Union's financial interests. Therefore, not only the system for a given operational programme implementation

will have to be effective and efficient, but the system for law protection in the given state will have to guarantee appropriate protection of funds paid from the Union budget. Fight against fraud will be a challenge due to the high volume of the funds to be allocated in a relatively short period of time. A significant simplification of the rules for European funds implementation will undoubtedly contribute to more efficient settlements of the EC's spending, but on the other hand, it will increase the risk of fraud, therefore emphasis will have to be placed on developing systemic solutions, safeguarding effective prevention and detection of actions that endanger the Union's financial interests. Examples of and proposals for applicable tools in the area will be presented in the second part of the article.

MARCIN SZYMAŃSKI

Deputy Director
Department for Infrastructural Programmes
(Managing Authority for the Infrastructure
and Environment Operational
Programme), Ministry of Development
Funds and Regional Policy

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