The Approximation of National Substantive Criminal Law on Fraud and the Limits of the Third Pillar

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OLAF is the only Community body whose tasks include administrative investigations on behaviour detrimental to the financial interests of the EU that may have "criminal" and "trans-national" aspects simultaneously. Trans-national European crime requires new solutions to be found in what is commonly referred to as European criminal law. For this reason the protection of financial interests has been the motor of the emerging European criminal law and continues to play a vital role.[1] Even before the existence of OLAF, its predecessor, the unit charged with the protection of the financial interests within the Commission (UCLAF), put forward first instruments on an approximation of national substantive criminal law, namely in the field of protecting the financial interests.[2] These instruments are the so-called PFI-instruments, consisting of the PFI-Convention of 26.7.1995, the First Protocol of 27.9.1996, the ECJ Protocol of 29.11.1996 and the Second Protocol of 19.6.1997,[3] all adopted under Title VI TEU. Protection of financial interests through criminal law began and has remained in the third pillar. This paper sets out to briefly outline the future outlook on the PFI-instruments and how OLAF could utilise these instruments in order to step up the fight against economic crime.

I. State of Affairs

The PFI-instruments cover a part of substantive criminal law, where the harmonisation of national law of EU Member States was considered necessary.[4] They require a number of offences to be incorporated in national criminal law, such as a variety of different forms of fraud concerning both EU expenditure and income, passive and active corruption and money laundering. Moreover, they also require the incrimination of attempt and even of preparatory acts, of complicity and the association to commit the relevant crimes. The PFI-Convention itself sets out the criminal liability of "heads of businesses" and the Second Protocol foresees, for the first time and in an innovative way, the criminal or administrative liability for legal entities. The Second Protocol also contains provisions on information exchange and assistance by the Commission (OLAF) to national judicial authorities.

However, the PFI-instruments pose two difficulties to the Commission in terms of enhancing the level of protection of the EU's financial interests through national criminal law:

–– Firstly, the Commission has struggled with the purely *formal aspects* of these instruments. They were devised as international law conventions and before the directive-like framework decisions were introduced in the TEU; their entry into force depends on national ratification. Ratification procedures only accelerated when the Commission proposed an alternative first-pillar instrument, namely a Directive on the criminal-law protection of the financial interests on the basis of Article 280 TEC, the so-called PFI-Directive.[5] Although the subsequent case-law of the Court revealed that the proposal for the directive was based on the right assumption that the TEC would also allow to introduce criminal law measures,[6] it was never adopted, but remained as a stick for the Commission to insist on compliance with the PFI-instruments. Only now – more than 10 years after signature –, the Second Protocol has entered into force due to the late Italian ratification.[7] Further, all of the instruments still wait for ratification by the new EU Member States (the Czech Republic, Hungary and Malta), which seem in no hurry in that regard.[8]

–– Secondly, the *material compliance* of Member States' legal systems with the requirements of the PFI-instruments has still not been achieved. The Commission issued two reports on the Implementation of the PFI-instruments[9] and, although these reports limit themselves to review the Member States' compliance on paper,[10] they both come to a damning conclusion: Loopholes in the national legislations allow offences covered by the PFI-instruments to go unpunished. The Commission even had to scale down its approach from the first report to the second report, in which it threatens to limit its follow-up only to "serious

shortcomings" in some of the 15 Member States that were already subject to the first report and thus alerted on the Commission's views.

Both, formal and material issues are also at stake for each enlargement negotiation in that the availability of EU monies for each newly acceding country also requires the adequate protection of financial interests through criminal law.[11]

II. Future Challenges in Relation to the PFI-Instruments

OLAF, as the Commission service in charge of the PFI-instruments, has to cope with these challenges. However, the TEU only offers very limited third-pillar tools to OLAF to deal with the PFI-instruments in their present state.

On the formal side, the TEU does not contain a mechanism to trigger national ratifications. Past experience of enlargement indicates that the ratification process may be even more cumbersome with the new Member States. For this reason, a mechanism was devised for Bulgaria and Romania whereby the accession of these countries was automatic on a date fixed by the Council and no longer depended on national ratification procedures.[12]

Regarding material compliance, the TEU does not provide a monitoring mechanism for the implementation as is foreseen under the first pillar. The Commission stated its intention to consider proceedings under Article 35(7) TEU in its second report on the implementation of the PFI-instruments. That provision is essentially different from an infringement procedure set out in Article 226 TEC reflecting also the intrinsic dichotomy between the Community legal order and intergovernmental cooperation as under the third pillar. Article 35 TEU states that the dispute may only concern the interpretation or the application of conventions, yet not the failure to comply with the obligations under the conventions. The Court of Justice is only authorized to pass judgment if the dispute cannot be settled amicably by the Council. How the judgment is supposed to be dealt with subsequently is specified in the TEU. It will be interesting to see how the Commission will tackle the "serious shortcomings" in implementation as identified in its second report. However, it has not been ruled out that such a "serious shortcoming" by a Member State in complying with the PFI-instruments, including even an inadequate implementation or enforcement practice, may also be pursuable under Article 280 TEC. Such a procedure would put the onus on the Commission to show that the concerned Member State's behaviour amounts to an actual failure in countering "fraud and illegal activities affecting the financial interests", whereby the Member State concerned no longer affords "effective protection" or protects the EU's financial interests in the same way as its own financial interests. For such a procedure, the Commission would have to produce a proof that goes beyond the mere review of Member States' compliance on paper as done by the Commission's implementation reports.

Additionally, the issue of reforming the legal set-up of the criminal-law protection of the financial interests as such remains unresolved. The Commission has not withdrawn its proposal for a PFI-Directive yet. The advantage of such a Directive remains to be that it offers the benefits that go with first-pillar Community legislation, in particular the supervisory mechanism not available under the third pillar. Even so, a directive cannot, of itself and independently of a national implementation law adopted by a Member State, have the effect of determining or intensify the criminal liability of persons acting in contravention of the provisions of that directive.[13] Furthermore, the proposal dates back to 2001. In the meantime, while European legislation on criminal law has evolved, OLAF has also had the opportunity to accumulate experience on what is further needed. Any new proposal would need to take these elements into account.[14]

In the future, the novelties introduced by the Treaty of Lisbon may make a balanced combination of the reform of the PFI-instruments and a better enforcement mechanism possible. Article 10 of the Protocol (No 36) on transitional provisions[15] extends the supervisory mechanism of the Community to previously existing third pillar acts, such as the PFI-instruments, but only five years after the date of entry into force of the Treaty of Lisbon. Even then it remains open whether the instruments still first need ratification by a Member State in order for that Member State to be subject to an infringement procedure.

Instead, the full set of measures to enforce implementation will be immediately available for any new acts adopted under the Treaty of Lisbon. The Commission could try to propose a newly revised legal act on the criminal-law protection of the financial interests as soon as the Treaty of Lisbon comes into force. Thereby, the OLAF experience in this field would prove valuable to justify new and advanced elements in such a proposal. This way of proceeding firstly requires finding out whether the appropriate instrument under Article 325 (ex-Article 280) of the future Treaty on the Functioning of the European Union is a directive or a regulation.[16] Additionally, the Commission faces another choice, namely whether it would be better to insist on establishing the European Public Prosecutor's office competent for offences affecting the financial interests as foreseen in the future Article 86 of the mentioned Treaty. All of these options, pursued separately or combined, may be met with political resistance by some Member States insisting further on a necessity test in order to exercise these future competences, even though the Treaty of Lisbon does not at any point hint at a need for such a test and although the two implementing reports seem to convincingly confirm that it is necessary to act regarding the protection of the EU financial interests through criminal law.

III. Outlook on OLAF's Role in Fostering the PFI-Instruments

The future perspectives on an improved protection of the financial interests through criminal law remain vague in the light of political uncertainties surrounding the Treaty of Lisbon. The problem of enhancing the protection of the financial interests, however, is an immediate concern and cannot wait. As an operational service, OLAF also has an interest to ensure that compliance is not just limited to the texts of the national provisions, as evaluated by the Commission reports, but also covers adequate implementation and enforcement practice of these national provisions in the Member States.

The practical work with the actual application of national criminal law puts OLAF in a good position to verify whether national courts are able to sanction all the different forms of fraud, corruption and money laundering, committed to the detriment of the EU budget, in an effective, proportionate and dissuasive way. The Second Protocol complements the national provisions[17] allowing national judicial authorities to collaborate with OLAF as a European layer reinforcing this co-operation. In practice, OLAF has close contact with national judicial authorities that receive OLAF reports of suspected criminal behaviour. In fact, national courts may be in a good place to promote compliance of national law with the PFI-instruments, since they have two powerful tools in their hand, both available under the present legal framework and without need to wait for the Treaty of Lisbon: conform interpretation of national criminal law with European law and the possibility of asking preliminary questions in case of doubts on the scope of European law.

–– *Conform interpretation* of national criminal law may be exploited more efficiently. Conform interpretation is applicable to criminal legislation regardless of whether the European act, with which conformity is sought, was enacted under the first or third pillar.[18] Conform interpretation ensures that formal compliance matches with material compliance: an example are national corruption offences, which leave the qualification of "official" or "public function" open so that these legal terms could cover not only national officials but also European officials in line with the assimilation principle.[19] However, conform interpretation is limited, since it

must respect the principle that criminal law may not be applied extensively to the detriment of the defendant, with the effect that it may not lead so far as to allow bringing criminal proceedings in respect of conduct not clearly defined as culpable by national law.[20]

–– *Preliminary questions* lead to correct application of existing European provisions. Although the so-called ECJ Protocol allows such preliminary questions with regard to the PFI-instruments, no national jurisdiction has yet taken advantage of this possibility. Still, the European Court of Justice already had to pronounce itself on cases concerning materially offences falling under the PFI-Convention, namely smuggling which is fraud to the detriment of the EU own resources. The relevant preliminary questions explored the scope of the notion of intra-EU *ne bis in idem* as enshrined in Article 54 of the Convention implementing the Schengen Agreement.[21] Interestingly enough that the provision of the Schengen *acquis* inspired Article 7 of the PFI-Convention; the basis for the procedure on the preliminary question used was Article 35 TEU, which on its side was inspired by the ECJ Protocol. Thus, the European Court of Justice could have decided the cases – with the same outcome – with reference to the PFI-instruments as well. Given that criminal procedures need to be swift in particular in view of protecting fundamental rights, it is understandable that national jurisdictions were not eager to put forward preliminary questions in the past. This justified concern led to the introduction of a new fast-track procedure for preliminary questions in the field of criminal law in 2008.[22] One may hope that the urgency procedure raises national judges' awareness of this way of promoting European criminal law.

In raising awareness for these tools, OLAF has a role to play in fostering the PFI-instruments in their practical application. However, there should be no doubt, that neither conform interpretation nor a preliminary question enable court judgements on the conformity of national measures with European law and are thus no substitute for an enforcement mechanism.

IV. Conclusion

More than ten years of PFI-instruments and ten years of OLAF still leave a situation whereby the protection of financial interests through criminal law is not ensured equally EU-wide. The tools of the third pillar provide direct measures to ensure compliance with the PFI-instruments, such as reports and litigation on interpreting their provisions, as well as indirect ones, such as conform interpretation or preliminary questions. However, these tools are limited in their impacts and ultimately unsatisfactory.

The challenge to come with the Treaty of Lisbon is what to do with these instruments and how far to push any reform of the set-up of the criminal-law protection of the financial interests. OLAF will have to face the choice on what to propose to the Commission, ranging from the European Public Prosecutor's office or a new legal act on the PFI to keeping the old set-up but taking advantage of new and improved enforcement mechanisms as soon as available. No doubt, interesting developments lie ahead in the next ten years as to OLAF's role in the approximation of national substantive criminal law on fraud.

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1. *Sieber*, Editorial to the first eucrim, eucrim 1-2/2006, p. 1.↩
2. See *Van Den Wyngaert*, Protection 'PIF' et espace judiciaire européen : bilan et perspectives à l'aube du 3ème millénaire, AGON 25/1999, p. 10 and *Kuhl*, The Criminal Law Protection of the Communities' Financial Interests against Fraud, The Criminal Law Review 1998, pp. 259 und 323.↩
3. Convention on the protection of the European Communities' financial interests: OJ C 316, 27.11.1995, p. 49; Protocol to the Convention on the protection of the European Communities' financial interests: OJ C 313, 23.10.1996, p. 2; Protocol on the interpretation, by way of preliminary rulings, by the Court of Justice of the European Communities of the Convention on the protection of the European Communities' financial interests: OJ C 151, 20.5.1997, p. 2; Second Protocol to the Convention on the protection of the European Communities' financial interests: OJ C 221, 19.7.1997, p. 12. Except for the ECJ Protocol the Council approved an explanatory report for each of the PFI instruments, to be found in OJ C 11, 15.1.1998, p. 5; OJ C 191, 23.6.1997, p. 1 and OJ C 91, 31.3.1999, p. 8.↩
4. Note the "whereas-clause" of the PFI-Convention reading that the PFI-instruments are "*necessary … to improve the effectiveness of protection under criminal law of the European Communities' financial interests*." The PFI-instruments draw inspiration essentially from the study of *Delmas-Marty*, In-compatibilities between legal systems and harmonisation measures: Final report of the working party on a comparative study on the protection of

the financial interests of the Community" in *Commission* (Editor), The legal protection of the financial interests of the Community: Progress and prospects since the Brussels seminar of 1989, Brussels, 25 and 26 November 1993, p. 59.↩

5. COM(2001) 272 final of 23.5.2001, OJ C 240 E, 28.8.2001, p. 125, as amended by COM(2002) 577 final of 16.10.2002, OJ C 71 E, 25.3.2003, p. 1.↩
6. See *Kuhl/Killmann*, The Community Competence for a Directive on Criminal Law Protection of the Financial Interests, eucrim 3-4/2006, p. 100.↩
7. The Second Protocol entered into force on 19 May 2009 after Italy had notified ratification on 18 February 2009. See also the news part of eucrim in this issue.↩
8. See on the Czech Republic and Hungary *Fenyk*, eucrim 1-2/2007, p. 51 and *Farkas*, eucrim 1-2/2007, p. 55.↩
9. (First) Report on the Implementation of the Convention on the Protection of the European Communities' financial interests and its protocols, COM(2004)709 final, and Second Report, COM(2008) 77 final. The detailed evaluation of all Member States' legislation is to be found in the Commission staff working papers associated with the reports, namely SEC(2004) 1299 and SEC(2008) 188. See also *Killmann*, eucrim 1-2/2007, p. 48.↩
10. See this critique for all third-pillar implementation reports in *Borgers*, Implementing Framework Decisions, Common Market Law Review 44/2007, p. 1361.↩
11. On OLAF's role in this context *Hamdorf*, The Role of the European Anti-Fraud Office in the Process of EU-Enlargement, AGON 31/2001, p. 8.↩
12. Article 3(3) of the 2005 Act of accession, OJ L 157, 21.6.2005, p. 203, provides simply that Bulgaria and Romania accede to the PFI-instruments by virtue of the Act of Accession itself. The related Council decisions were published in OJ L 9, 12.1.2008, p. 23 for Bulgaria and in OJ L 9, 12.1.2008, p. 23 for Romania.↩
13. See Joined Cases C-387/02, C-391/02 and C-403/02, Berlusconi and others [2005] ECR I-3565, paragraph 74 and the case-law cited there.↩
14. See for instance the proposal for offences such as market-rigging (Article 2), conspiracy (Article 4), abuse of office (Article 7) and disclosure of secrets pertaining to one's office (Article 8) of the *Corpus Juris 2000*, as contained in Annex III of Part I, *Delmas-Marty/Vervaele* (eds.), The Implementation of the *Corpus Juris* in the Member States, 2000, Volume I, p. 189.↩
15. The citation refers to the consolidated versions of the Treaty on European Union and the Treaty on the Functioning of the European Union, as published in OJ C 115, 9.5.2008, p. 1.↩
16. *Picotti*, La perspective de réforme des traités européens et la lutte contre la fraude, eucrim 1-2/2008, p. 64.↩
17. See for instance *Desterbeck,* The Added Value of OLAF, A few thoughts on the evidential value of OLAF reports in criminal investigations and for the criminal justice authorities in Belgium, Speech given at the formal inaugural sitting of the Court of Appeal in Ghent on 1 September 2005 (available at http://ec.europa.eu/anti_fraud/partners/tribune/others_en.html).↩
18. For the first pillar ever since Case 14/86, Pretore di Salò, [1987] ECR 2545 and Case 80/86, Kolpinghuis Nijmegen [1987] ECR 3969; for the third pillar since Case C-105/03, Pupino [2005] ECR I-5285, setting out also the limits to conform interpretation in criminal law.↩
19. See for example *Killmann/De Moor*, De assimilatie van communautaire ambtenaren met nationale ambtenaren bij de bestraffing van ambtenarenmisdrijven, Rechtskundig weekblad, 12/2007-2008, p. 482.↩
20. As clearly expressed for the first time in Joined Cases C-74/95 and C-129/95, Criminal proceedings against X [1996] ECR I-6609, paragraph 25.↩
21. See Case C-467/04, Gasparini and others [2006] ECR I-9199 and Case C-288/05, Kretzinger [2007] ECR I-6441.↩
22. See *Wahl*, eucrim 3-4/2007, p. 78f.↩

* Author statement

The views expressed are purely those of the authors and may not in any circumstances be regarded as stating an official position of the European Commission or the European Anti-Fraud Office (OLAF).

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