

Practice Name:

**EC-recommended red flags integrated into management verifications**

Country:

**Croatia**

Practice category:

- Red flags



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**Fraud risk(s) countered**

- Conflict of interest
- Avoidance or manipulation of public procurement procedures
- Double funding
- Collusion
- Manipulation of project costs

**Context and objective(s)**

The Croatian Ministry of Regional Development and EU Funds and the Ministry of Labour and Pension System have set the requirement for Managing Authorities (MAs) for Operational Programme (OP) Competitiveness and Cohesion and OP Efficient Human Resources and their Intermediary Bodies (IBs) to use red flags for carrying out their management verification procedures. More specifically, the EC's Information Note of Fraud Indicators for ERDF, ESF, and CF (COCOF 09/0003/00-EN) has been transposed into the Common National Rules (CNR) for Management and control system of MAs for OP Competitiveness and Cohesion.

The MA for OP Competitiveness and Cohesion uses ARACHNE but does not have other additional sophisticated IT tools for the identification of red flags. Instead, at the national level, the Managing Authority for OP Competitiveness and Cohesion developed the Common National Rules summarising anti-fraud and anti-corruption measures taken by MAs and IBs.

The MA for OP Competitiveness and Cohesion set up the CNR in order to address several goals:

- To ensure efficient procedures are in place at the OP Competitiveness and Cohesion level, as the MAs have a shared responsibility at the EU level for managing EU funds
- To have a proper safeguard to limit the risks of fraud and corruption at the MA and national level
- To prevent potential fraudulent and corrupt activities involving EU Funds
- To raise awareness among practitioners involved in managing and implementing Operational Programmes (OPs).

Annexes 8 and 9 to the CNR No.10. (Risk management) detail the use of EC-recommended red flags and tailored red flags for management verifications. The Annexes were set up to comply with the Key Requirements 4 and 7 on the specific anti-fraud measures (red flags, fraud risk self-assessment) to be put in place by the Managing Authority. These annexes are available for consultation and use by employees of the MA and IBs. The MA also sees the Annexes 8 and 9 as awareness-raising and capacity-building instruments for IBs of the first and second levels involved in management verifications. Both MAs and IBs are using the red flags list as an up-to-date comprehensive list of risk indicators in anti-fraud work.

## Description of the practice

CNR were developed by the MA with the help of the technical assistance. The CNR were developed on the basis of the similar set of regulations for the EU Structural funds developed by the MA for the 2007-2013 programming period. With the transition to the structural funds in the new programming period (2014-2020) the MA need to ensure that all the IBs are following the same rules and procedures from the CPR and EU regulation. CNR was a tool to ensure standardisation and consistent application of rules and procedures regarding management of EU funds and anti-fraud activities.

The framework of anti-fraud work is distributed over two layers of procedures: Common National Rules and organisations' manual of procedures (MoP). CNR includes procedures on the horizontal topics (e.g. risk assessment), as well as prevention and detection of fraud and reporting of irregularities. Currently, the MA has 15 different CNR covering different topics of the management and control system set up and implementation. Apart of the CNR, each authority and IBs in the system have their own manual of procedures, that detail and specify the procedures and rules from the CNR related to daily functions of these authorities. Internal manuals of procedures details specific tasks, responsibilities and deadlines for activities for each organisation and team members.

Application of CNR in the part of red flags is done through implementation of **EC-recommended fraud risks indicators, tailored fraud risks indicators or by using ARACHNE IT tool.**

The MA uses EC-recommended list of red flags, which is a list taken from to EC guidelines on fraud risks assessment<sup>1</sup>. Basically Annex 8 of the CNR on risk management reflects the template from the EC Guidelines on the fraud risk assessment. Annex 9 to the CNR on specific risk indicators was developed in 2017. Based on the analysis performed with the help of the technical assistance, as well as on the feedback received from the IBs and results of the MA controls performed during the verification of delegated functions, the MA found a set of additional fraud risk indicators that were specific to the context of Croatia and were not included in the EC template and in the Annex 8 of the CNR. With the help of colleagues from Latvia providing technical assistance, the MA developed a set of tailored risk indicators in additional to EC-recommended indicators.

## Unique features

The fraud risk indicators (red flags) in the Annex 9 are merged into three groups depending on the area of fraud risks:

- Public procurement
- Forgery of documents
- Labour costs and consulting services

Each group of fraud risks contains specific fraud risk indicators and practical examples on how such fraud indicators would look like in practice. For instance, the corruption risk indicators include 12 practical examples of corrupt behaviour. It makes it much easier to understand the specific fraud indicator and “detect” such fraudulent behaviour. In addition to this, the main terms as fraud, corruption etc. are also defined and standardised to avoid misinterpretation and misunderstanding among IBs.

The type, degree and frequency of the verifications using those red flags depend on the assessed level of risk for the project. Hence, the higher the perception of fraud risks for a specific project, the stricter the verifications will be. For instance, a project assessed with a high degree of riskiness could be subject to more

<sup>1</sup> European Commission, Fraud Risk Assessment and Effective and Proportionate Anti-Fraud Measures, Guidance for Member States and Programme Authorities. June 2014, [https://ec.europa.eu/regional\\_policy/sources/docgener/informat/2014/guidance\\_fraud\\_risk\\_assessment.pdf](https://ec.europa.eu/regional_policy/sources/docgener/informat/2014/guidance_fraud_risk_assessment.pdf)

frequent on-the-spot checks, involving more targeted verifications. In this way, Annexes 8 and 9 are used by practitioners as an additional tool during the check-ups to detect suspicious behaviour, documents or patterns.

Following the new EC guidelines establishing bid rigging<sup>2</sup> as a type of irregularity to be corrected, the MA has organised a network meeting for all IBs to raise awareness on bid rigging as a fraud risk and how to detect such a risk. Following an interest from the IBs, the MA has included bid rigging in the risk of fraud risk indicators.

To follow up on the implementation and monitoring of fraud risks, the MA has designated **risk coordinators** in charge of coordinating with project managers of IBs on the use of red flags in their management verifications. Each authority (MA, IBs) has a designated risk coordinator that is responsible for anti-fraud work. Risk coordinators are forming a network of experts that meet at least two times per year to exchange good and bad practices, sharing knowledge and fraud risks. In addition, risk coordinators are involved in three operational networks, discussing issues around state aid, public procurement and irregularities. Following the meetings, risk coordinators are distributing relevant information across their organisations.

## Outcomes and results

Requirement of integration of red flags into the management and control system in Croatia ensured a high standard for risk control and verification for ESI Funds operation. Implementation of the CNR has reinforced the use of red flags and identification of fraud risks for OPs under ESI Funds.

The MA generally recognises the improved efficiency and consistency in anti-fraud prevention and detection as a result of developing CNR and its Annexes 8 and 9. The risk indicators are also included in the MA's checklist on public procurement, therefore it is difficult to measure the impact of introduction of Annexes 8 and 9 separately. The MA has seen the positive outcomes of implementation of CNR and fraud risk indicators based on the statistics of reported irregularities and suspected fraud by the IBs. The latest statistics on reported irregularities prove better response to risk, but also **better awareness and capacity** of IBs to detect fraud risks. The Annex 9 has proved to be an excellent **prevention tool** and increase the alert of IBs for potentially fraudulent activities. The reported irregularities and suspected fraud, however, relate mostly to the conflict of interest and fraud in general.

## Key success factors

- The development of the Common National Rules should be a common task between MAs, IBs and consultants. MAs have an extensive knowledge of the system and internal processes that should be considered, once IBs help tailor the procedures to better fit into the existing environments.
- Involvement of the IBs in the development of the CNR ensured the consistency of CNR with the individual manual of procedures of each IB.

<sup>2</sup> Annex to the Commission decision 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, May 2019, <https://ec.europa.eu/transparency/regdoc/rep/3/2019/EN/C-2019-3452-F1-EN-ANNEX-1-PART-1.PDF>

## **Challenges encountered & lessons learned**

- When implementing all the requirements from the regulation into a local or national system, the MA should aim to put all information together in a practical and simple way. Heavy and complex procedures lead to low uptake by the IBs and a high number of errors.
- EC's self-assessment tool was useful for the MA to ensure that all necessary procedures are foreseen in the CNR and IBs' manuals of procedures.
- CNR are constantly evolving, and updates reflect the changes in the EU and national regulation, fraud risk trends (taking into account the feedback from IBs as well as the recommendations of audits and controls of delegated functions performed by MAs).
- The MA views personal visits to the IBs and running self-assessments to be a key to understanding the knowledge gaps of the IBs, to better assessing the local environment and fraud risks and to tailoring the CNR to the needs of IBs.

## **Potential for the transferability**

- The CNR and Annexes 8 and 9 can be easily replicated and transferred to other MS.
- To ensure smooth setup of the practice, MAs should work in collaboration with IBs, and raise awareness on the existing procedures and rules.