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# From UK customs fraud to Danish money laundering: lessons for Brexit and the EU

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Serious lapses by national authorities have recently come to the fore, ranging from customs fraud in the UK to money laundering through Danish banks operating in Estonia. These incidents are symptoms of a wider issue which needs to be tackled.

The discovery of customs fraud would not normally merit wider attention. But if the extraordinary extent of the UK-based undervaluation scheme has made headlines and has important ramifications for Brexit, the story also points to a systemic problem in the way the EU operates.

OLAF uncovered the enormous scale of the fraud in a 2016 joint customs operation with French customs authorities (OCTOPUS), which targeted criminal networks importing textiles and footwear from China via the UK. By only declaring a small fraction of the true value of the goods, the fraud was generating billions of losses in customs revenues and VAT income for the countries where the goods ended up. However, despite repeated warnings dating back to 2007, the UK authorities have failed to prevent the fraud. Now the European Commission is demanding the UK government pay a €2.7 billion shortfall directly into the EU budget.

In the Brexit context, the widespread fraud uncovered by this investigation makes it even more difficult to believe that a hard 'customs' border can be avoided in Ireland if the UK does not remain in the Customs Union. The 'trusted trader' scheme proposed by the UK seems unlikely to work in practice.

Beyond Brexit, it highlights a broader issue. From the start of the integration process, the general approach has been that 'Brussels' would only set general rules, which would then be implemented through national legal and administrative systems. 'European integration light' might have worked in a community of six countries with a similar level of development and administrative capacity and within a group small enough that peer pressure was direct and personal. But to what extent is it feasible for a much larger EU to leave important functions in

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the hands of member states when their interests are not always aligned with those of the Union?

Customs duties go to the EU budget, except for 25% retained by member states to defray their expenses. This does not give them sufficient incentive to catch this type of fraud: for every euro collected through national efforts, national authorities only pocket 25 cents. Moreover, as seen in this case, if national authorities are lax in checking customs declarations, this also generates losses of VAT revenue in the destination countries. Why should national customs authorities invest resources in protecting the interests of other member states? The principle of sincere collaboration in the Treaty is unlikely to be a decisive factor when national authorities have to decide how much money to allocate to fighting customs fraud.

Something similar happened in the area of money laundering where huge gaps in enforcement have become apparent recently, with one branch of a Danish bank reportedly facilitating suspect operations in the hundreds of billions. Anti-money laundering enforcement is also left to national authorities. But they can be reluctant see problems at home through being more defenders of 'their' banks than strict, impartial controllers.

It is noteworthy that in both these cases, the administrative capacity of the national authorities would normally be considered very good. The problem was thus not the ability to perform controls, but the willingness to put resources into tough supervision.

Similarly, during the euro crisis, national supervisors tended to declare their own banks sound with the result that the underlying problems were not treated. The European Banking Authority was created to coordinate banking supervision, but it had no executive powers. It was only the escalating crisis that forced member states to agree to the 'Single Supervisory Mechanism' under which the ECB directly supervises the bulk of the euro area banking system.

This is perhaps the model to follow in other areas. There is no need for new, sweeping transfers of sovereignty, but the EU should set up more 'federal' agencies to implement the powers it already has. A European Customs Service or a European Anti-Money Laundering Authority might not represent major steps, but they are needed to make the Union work more effectively.