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**EVALUATION OF COMMISSION RECOMMENDATION OF 27 MAY 2005
CONCERNING AUTHENTICATION OF EURO COINS AND HANDLING OF EURO COINS
UNFIT FOR CIRCULATION**

(In line with Article 12 of the Recommendation)

Introduction

In Article 12 of the Commission Recommendation of 27 May 2005 concerning authentication of euro coins and handling of euro coins unfit for circulation, it is foreseen that “three years after the publication of this Recommendation, the present rules will be evaluated in the light of the experience gained (...)”. The evaluation process has been conducted in two subsequent steps and the results of both have been consolidated in this report.

The first step consisted in taking stock of the level of implementation by Member States of the provisions set out in the Recommendation. The information was gathered by means of a questionnaire sent by the Commission/OLAF to Member States in 2006.

The second step comprised a detailed examination of the different measures put in place by Member States, in order to draw lessons from the experience gained in the implementation of these measures. This study was carried out through a series of three expert workshops, which were organised by the Commission/OLAF and took place between October 2007 and March 2008. The discussions, notably with Member States experts but also with private sector technicians, have enabled the definition of joint considerations on a number of elements of the Recommendation. A particular focus of these considerations was the consideration of a potential transformation of the Recommendation’s provisions into legally binding rules.

1. Implementation of the Recommendation

1.1 Implementation of provisions on authentication of euro coins

The recorded information concerning the level of implementation is based on replies received from fourteen euro area members to the questionnaire prepared by Commission/OLAF sent to the members of the Euro Coin Sub-Committee (ECSC) in March 2006. The Member States’ responses illustrated a vast acceptance of the provisions of the Recommendation both within national law and as a matter of national practice.

The provisions of the Recommendation regarding the authentication of euro coins (Articles 3-6) are implemented overall in a satisfactory way, although the level of implementation varies among Member States. Moreover, it has opened the way for a unified system of authentication of euro coins throughout the euro area. In particular, Austria, Belgium, France and Germany and the Netherlands have reached high standards of implementation, although legislation has not been introduced in all cases. It can be noted that in all these countries, the coin sorting centres, operated by cash-in-transit companies (CIT) or by local branches of the National Central Bank (NCB), form the backbone of the implementation.

In Germany, authentication activities are taking place already for several years. In the current system, around 1000 private companies are in contract with the German Bundesbank allowing them to lodge coins without fee, but in standard packaging. The coins are processed by sorting machines where their authenticity is checked and suspect coins are handed over to the Coin National Analysis Centre (CNAC). The Bundesbank branches check around 10% of the lodgements for the presence of counterfeit coins, foreign coins, other objects and counting errors. In case anomalies are found, a complete check of all lodgements of the company concerned will be performed. If problems persist, the company can lose the benefit of the agreement.

In Austria, coin sorting is carried out in seven centres of GSA (a joint venture of the Austrian National Bank and commercial banks) and these centres annually check around 90% of the volume issued. The Austrian CNAC audits GSA, including detailed reports about the sorting machines. Manufacturer tests are offered by the CNAC in cooperation with the banknote test centre in the premises of the NCB.

Authentication activities in France picked up following the adoption of Decree of 18 May 2005. Coins are checked systematically, mainly by around 60 private operators managing 200 sorting centres, on the basis of bilateral agreements with the Banque de France (BdF). Some sorting is also carried out in BdF branches but only one centre (in Paris) will continue this as of 2008. Teams have been set up by the BdF in order to carry out regular inspections of the sorting centres.

Belgium started performing inspections of sorting centres in 2003. Legal basis is provided by a Law of 12 May 2004 and a Royal decree of 5 April 2006. Two major CIT companies carry out sorting, as well as the branches of the NCB. A yearly visit to each centre includes testing of all sorting machines and an audit. Suspect coins are handed over on a regular basis to the authorities. The ratio of counterfeit coins found compared to the volume of coins processed is compared between the different sorting centres.

In the Netherlands, there is no legal framework for authentication activities. Nevertheless, cooperation has been set up on an informal basis between the CNAC and the four CIT companies, which operate a total of four sorting centres. All rejected coins are sent to the CNAC. New contracts will be proposed shortly by the NCB.

The above-mentioned Member States mostly include to the authentication process all euro coin denominations. They all guarantee that a much higher percentage, than the one recommended under Article 3 of the Recommendation, of the total net volume per denomination is authenticated each year (10%). They mostly maintain lists of controlled sorting centres whose activities they check and provide relevant training to staff. Samples of counterfeits used for the purposes of detection tests cover the full range of counterfeit coins and finally, manufacturers are given the possibility to test their machines at the CNAC.

The Ministry of Finance in Portugal approved on 15 March 2007 a law-decree which sets the bases for implementing the provisions of the Recommendation. The decree enhances the role of the National Central Bank (NCB) which will assume all responsibilities for recycling euro currency and for other operations such as co-operation on the training of staff involved in recycling and conduct of initial and regular tests on equipment. Authentication and sorting of coins outside the NCB is also regulated by the new legislation under monitoring by the NCB. Reference is made to Article 6 of Council Regulation 1338/2001 providing that euro coins shall only be returned to circulation if they have been authenticated and checked either manually or by successfully tested sorting machines. Finally, the decree introduces sanctions in case of non-compliance with its provisions. As of 2008, the decree is expected to yield practical results.

In Italy, working groups, generally under the responsibility of the National Central Bank or the Ministry of Finance, have been initiated with the aim of evaluating the situation and implementing the Recommendation. No timeframe has been defined yet. In Ireland, a working group established in early 2006, has issued its first annual report on the progress made towards implementing the Recommendation. Although not all of its provisions are followed by Ireland, authentication of euro coins is partly been carried out and a paper proposing

further recommendations towards implementation will be prepared by the working group in the near future.

Greece has signalled its intention to implement the Recommendation in the future. However, since 2002 coins are processed in all NCB branches by means of sorting machines that check authenticity and suspect coins are sent to the CNAC. Luxembourg is considering whether to proceed with the implementation of the Recommendation although is already partly carrying out authentication of euro coins including all euro denominations. In Malta and Slovenia, having only recently changed over to the euro, preparations are ongoing for implementing the Recommendation. Finland has no plans to implement the Recommendation.

The above analysis shows that the largest part of the euro area implements the authentication requirements. While procedures still need to be streamlined and even implemented in a number of countries the necessity for authentication of euro coins is now generally accepted and a critical mass has been reached. Consequently it may be considered that the principle of authenticating euro coins may be enshrined in legislation. This obligation would, in that event, apply in some point in the future allowing sufficient time for preparation and precise definition of procedures in line with the experience gained from implementing the Recommendation.

1.2 Implementation level of provisions on the handling of unfit euro coins

With regard to the provisions of the Recommendation concerning the handling euro coins unfit for circulation (Articles 7-10), eight euro area members (Austria, Belgium, Finland, Germany, Italy, Luxembourg, Netherlands and Portugal) have reached a high level of implementation.

Reimbursement of euro coins unfit for circulation is carried out by the vast majority, it is done irrespective of the coins' national side and all these Member States check for the quantity, authenticity and visual appearance of the unfit coins submitted, as provided by the Recommendation.

In the Netherlands this part of the Recommendation is partly implemented (only for coin deposits made by individuals), and in Greece national measures in line with these provisions are to be adopted in the future. Slovenia and Malta will also implement the provision.

With regard particularly to reimbursement or replacement of euro coins unfit for circulation, information received demonstrates that the majority of Member States applies the relevant provisions of the Recommendation. Information on the Government services responsible for reimbursement or replacement of euro coins, as well as packaging standards and/or fees is available in most euro zone members either via the NCB's and other branches website and via other publications. It is noted that Germany is particularly active in removing unfit coins from circulation. This country has therefore reimbursed larger quantities of euro coins unfit for circulation, compared to other Member States.

2. Prospects for future provisions

2.1 Prospects for provisions concerning authentication of euro coins

In addition to the above analysis of the level of implementation, discussions have taken place more recently with experts in order to perform a critical assessment of the provisions, based on the experience gained. This was done with a view to improving the provisions for a future

possible transformation of the Recommendation into legally binding measures. The considerations that were expressed in several expert workshops and meetings have been taken into account in the text below.

Denominations to be authenticated (Article 3, first paragraph)

The coin denominations to be authenticated as a minimum (2-euro, 1-euro and 50-cent) are sufficient and do not need to be broadened. No significant counterfeiting activity has been identified on smaller denominations.

Minimum volumes (Article 3, third paragraph)

According to the Recommendation, the minimum volume of coins to be authenticated within a Member State is 10% of the total volume of the relevant denominations issued by that country. Testing is done in practice when coins go through sorting centres, without any direct link to all coins issued, although related volumes are generally by far higher than the threshold level. If the amended Council Regulation 1338/2001 defines, in line with the Commission proposal, that euro coins need to be checked for authenticity prior to being re-circulated, then it would not appear necessary to define a specific threshold. On the other hand, some reference to proportion of sorting centres to be controlled may need to remain in a revised text, particularly in view of the large number of sorting centres in some countries.

Sorting test (Article 4.1)

The sorting test is an optional test that requires coin sorting machines to sort at least 98% of all (genuine) coins in a correct way. The test is considered of limited relevance, as customers of sorting machines will generally demand a higher machine performance. However, it is important to make sure that sorting machines are operating under normal working settings, as opposed to specific test settings, while undergoing the detection test (see below). Setting a minimum requirement on acceptance of genuine coins could be useful in order to minimise the risk that machines are not working under normal working settings. Therefore, since this requirement is only of limited use, it does not need to appear separately, but can be part of the detection test, in the context of acceptance criteria. In that case, the present provision for the sorting test will be removed.

Detection test (Article 4.2)

The detection test requires coin processing machines to correctly reject a set of counterfeit coins, which is representative of the diversity of counterfeits found in circulation. The description of the test needs to be slightly revised to take account of the deletion of coin-like objects in the updated European procedure. A reference to the detailed description of the test, which is defined and regularly updated in a technical note by the Commission/ETSC, seems useful.

Frequency of testing & Audits (Article 4.3 and Article 6)

The recommended minimum frequency of testing for each machine is once per year. Although some Member States are able to reach this level without difficulties, in others this is not feasible. This depends notably on the number of sorting machines in operation in a country. Therefore, it is proposed to leave flexibility to Member States to implement a system ensuring that sorting machines installed continue to function properly. Regular machine testing, random checks of sorted coins and also audits are options that can be used for that

purpose. Member States should then define what the appropriate sampling is to comply with the authentication requirement. To enable coherence in the approach used in Member States, the level of sampling and the auditing procedures should be discussed at the relevant groups before being determined at national level. However, the number of sorting centres audited (and, therefore, of sorting machines tested) should cover a minimum level of volume of euro coins.

Additional testing (Article 5)

It is appropriate that, eventually, all Coin National Analysis Centres (CNACs) should offer the possibility of testing coin-processing machines to manufacturers and purchasers of such machines. In the short to medium term, this is not feasible for some CNACs as they have insufficient numbers of counterfeits in order to compose the necessary test packs. The Commission/OLAF is looking into the possibilities of exchanging counterfeit coins among CNACs in order to help solving this problem.

Auditing (Article 6)

Some Member States have reported that some operators are currently reluctant to hand over data on the volume of coins authenticated. This is due notably to concerns about competition or confidentiality. When the reporting requirements will be part of a legal obligation, this should not pose a particular problem anymore.

2.2 Prospects for provisions concerning handling of coins unfit for circulation

Definition of unfit coins (Article 1b)

The current definition used for ‘euro coins unfit for circulation’ is rather large. It consists first of a general definition on unfit coins including a description of the possible ways in which they have been altered. This is followed by a more technical definition for unfit coins, which uses deviations of either dimensions or weight compared to the nominal values of genuine coins. Practice in Member States shows that this second definition is rarely used. Further work is necessary on the definition, particularly in the context of fitness testing.

Potential inclusion of fitness testing

The question of how to identify and remove from circulation euro coins unfit for circulation is not addressed in the Recommendation. It has been proposed to look into the feasibility of defining the conditions for rejection of unfit coins with sorting machines.

The issue of rejecting unfit coins was considered on the basis of two methods: one concerns sorting of objects rejected during the currently applied authentication process; these objects are, essentially, unfit coins and counterfeits (as well as foreign coins and some coin-like objects). Discussions with experts from Member States and from private sector indicate that separating between the two is generally possible although the process might, in some cases, be more costly. In addition, unfit coins are, using this process, separated at a level lower than 100%, i.e. the counterfeits rejected may include some unfit coins.

The other method for rejection of unfit coins would involve a specific fitness test, similar to the one performed on banknotes. The definition of such a test involves high technical standards, as well as an agreement among Member States. In particular, preferences among

Member States vary as regards the acceptable level of fitness of circulating coins, in terms of visual aspects (such as oxidation and blackening) or, potentially, of technical aspects (for example degree of deformation or change in electrical properties) or even the cleanness of the coins.

Implementing such standards may be challenging both in specifying them and in determining equipment capable of carrying out the relevant tests (for example, testing for visual aspects is currently not generally provided). In addition, that equipment may represent disproportionately high expenditure compared to the additional number of unfit coins removed from circulation. Indeed, it was argued that the level of rejection of unfit coins by means of the currently applied authentication method may already be satisfactory, so that any additional testing may be of limited use.

Principles for reimbursement (Article 7)

The principle followed in the Recommendation is that euro coins unfit for circulation should be reimbursed. The application of this principle has raised the issue of bulk redeemers, i.e. companies presenting large quantities of unfit coins for reimbursement, in some Member States. These coins come presumably out of metal recycling activities in, notably, Asia. The issue was discussed on several occasions by the ECSC, leading to the question whether and how to avoid reimbursement of such shipments.

Discussion of the issue at the authentication workshop concluded that it is neither the quantity nor the origin, but rather the condition of those coins that poses problem, reflecting the treatment they were subject to. It was shown that many of these coins have been altered through a severe mechanical or a chemical treatment. It was seen that such treatment, verified through examination of the submission and a declaration to be requested, would justify non-reimbursement of these altered coins.

Consequently, it was confirmed that the original and positive wording of the Recommendation is appropriate, stating that “each Member State should provide for reimbursement (...) of euro coins unfit for circulation”. This follows the existing legal thinking behind the Recommendation and the practice in several Member States.

However, it was felt that the issue of bulk redeemers could be addressed with the provision in the Recommendation (Article 7, 2nd paragraph) which allows, in specific conditions only, to refuse reimbursement of deliberately altered coins. This provision could be broadened and completed by referring to all deliberately altered coins (except counterfeits, for which there are specific provisions). This would also include the case where the coins are altered by a process that could be reasonably expected to have the effect of altering them, such as car shredding. At the same time, concern was expressed about oxidised ‘fountain’ coins for which (frequently) charitable organisations obtain reimbursement. Consequently, a text along the following lines is considered: “**Member States should, in principle, refuse reimbursement of euro coins which have been altered either deliberately or by a process that could be reasonably expected to have the effect of altering them, notwithstanding reimbursement for charitable purposes (‘fountain coins’ etc.)**”. In that context, a declaration could also be requested from the submitting entity on the processes and products used on the unfit coins presented for reimbursement.

Another possible source for these shipments (or part thereof) might be defective or already demonetised unfit coins sold as scrap metal. In order to prevent these coins from being

presented for reimbursement, it is proposed to define the conditions used by Member States for destroying or demonetising those coins.

In addition, the Recommendation provides that a company or individual situated in a euro area Member State can only lodge unfit coins for reimbursement at the competent service of this Member State. This is not the case for companies and individuals situated outside the euro area, who can lodge at any competent service in the euro area. It was considered that unequal treatment is not justified and should be abolished in future provisions.

Finally, Article 12 of the Recommendation raises the issue of providing for a compensation mechanism among MS for the unfit coins reimbursed. In this context, the only situation in which a compensation mechanism was mentioned is in relation with the bulk redeemers. Consequently, to the extent that the latter would be addressed by the wording considered, there does not seem to be a strong case for a joint compensation mechanism in the context of unfit coins¹.

Handling fees (Article 8)

A standard handling fee of 5% of face value is proposed in the Recommendation, supplemented by an additional 15% if anomalies are found in the lodgements. This level seems to be appropriate for the majority of Member States.

In practice, many countries offer derogations for individuals and for cash handlers that cooperate on authentication; as a result, it does not seem necessary to abrogate these exceptions.

Packaging (Article 9)

The proposed packaging conventions are recommended only in case national standards do not exist. Member States practice is varied. The conventions seem convenient, although in many cases derogations are offered. In addition to the described standards, which are appropriate for return of large number of coins, a second standard bag with 100 coins per denomination could be useful.

Checks (Article 10)

The description of checks is very detailed and their relevance to practice was discussed; however, overall they do not seem to pose any particular problem.

Reporting (Article 11)

Only a limited number of Member States have reacted to the request for annual reporting, as sent out by the EFC secretariat. Some Member States mentioned that the reporting needs to be streamlined. The Commission/OLAF will propose a template for future reporting.

Need for legislation (Article 12)

¹ The discussion of compensation mechanisms is taken up thoroughly in the report of the Task Force on the consequences of net euro coin migration (30 June 2008).

The Recommendation requires evaluating, i.a. the potential need for legislation in the areas concerned. Discussions point to the need to transform the measures foreseen in the Recommendation, as discussed above, into a binding set of rules.