

Conditionality mechanism: Hungary facing the threat of withheld EU funds

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On 18 September, the European Commission recommended withholding 65% of funding to Hungary for three cohesion policy operational programmes (€7.5 billion in total) in order to 'ensure the protection of the financial interests of the EU against breaches of the principles of the rule of law in Hungary'. This is a further step in the so-called 'conditionality mechanism' procedure initiated in April, shortly after the Hungarian parliamentary elections. At the same time, the commission said that Budapest had made a commitment that, by 19 November, it will fulfil all the main agreements made as a result of several months of dialogue. Commissioner for Budget and Administration Johannes Hahn hailed Hungary's proposals (a package of 17 changes to the law) as a 'step in the right direction', provided they are implemented.

The first comments from the Hungarian side regarding the 18 September decision indicate that the relevant legislation, in line with the commission's expectations, could be enacted already in the next few weeks. The changes will include an increase in the transparency of public tenders and the establishment of an anti-corruption institution independent of the government (it would be operational already in the second half of November). Their implementation would also be a step towards obtaining funds from the EU Recovery Plan, which is being discussed in parallel.

Ultimately, the eventual suspension of funds will be decided by the EU Council by a qualified majority within three months. If this ruling is made, it will apply to one third of cohesion policy funds and would not include, for example, funds from the common agricultural policy. Hungary is the first EU member state for which the so-called conditionality mechanism, established in 2020, has been triggered.

Commentary

- The European Commission's recommendation is a sign of a mounting pressure on Hungary to implement the agreed changes to the law. Brussels is concerned that, despite Budapest's far-reaching promises, there will be no substantial curbing of irregularities in the use of EU funds due to Fidesz's tight political control over the state's institutions. Additional pressure is being exerted on Hungary by the European Parliament. In a resolution adopted on 15 September it described Hungary as an 'electoral autocracy' and demanded a tough response from the European Commission and the Council of the European Union to Budapest's actions. This has thus so far blunted the success of the

Hungarian government's political offensive in Brussels in recent weeks (Justice Minister Judit Varga has met with seven commissioners and representatives of the Czech presidency since the beginning of September) aimed at keeping the funds foreseen for 2021–2027 and to obtain blocked funds from the Recovery Plan.

- Budapest seems determined to maintain the funds - even at the cost of making significant concessions to the European Commission - as it is grappling with a drastically worsening economic situation: high inflation (15.6% in August), a fall in the forint exchange rate (over the past year the largest in the world after the Turkish lira and the Argentine peso) and rising debt (77% of GDP, the highest among the V4 countries). Since August, the Fidesz government has had to abandon the most important social measure of its twelve-year rule, namely subsidising energy prices (due to which individual consumers' bills have increased about fivefold), and has also been forced to increase taxes for the self-employed (which triggered several days of protests in the capital). In this context, maintaining the inflow of EU funds is a prerequisite for the stability of the Hungarian economy.
- Hungary's political marginalisation has weakened its position in negotiations with the European Commission. Due to Budapest's favourable course towards Russia, cooperation in the Visegrad Group has declined since February. Following its withdrawal from the European People's Party in March 2021, Fidesz remains unaffiliated in the European Parliament, and attempts to form a new alliance of populist-right parties have failed. Hungary's relative isolation is confirmed by the fact that Prime Minister Viktor Orbán has made only one visit to EU countries since the April elections (to Austria in July).
- The Fidesz government is trying to keep as much control as possible over how EU funds are spent since they are instrumental for maintaining the stability of the power structure. In recent years, these funds have not only been the engine of the economy, but also an essential tool to serve the interests of party-linked oligarchs, who commonly win public tenders for EU co-financed projects (often as the sole bidder). The European Anti-Fraud Office (OLAF) records the highest number of cases of irregularities in the use of EU money precisely in Hungary (in 2015–2019, 3.93% of funds were affected, followed by Slovakia with 0.53%), and its cases have included Orbán's son-in-law. Between 2012 and 2021, Hungary has seen a drop of 12 positions in the Corruption Perceptions Index (CPI) and is only ranked 73rd in this classification.
- Alongside engaging in dialogue, Budapest is likely to use the tools of political blackmail, linking the issue of funds with support for the EU's common position towards Russia. Hungarian criticism of EU sanctions, which Orbán sees as a source of economic hardship 'invented by the West and detrimental to Hungary and Central Europe', has intensified in recent weeks. Already during negotiations over the introduction of an embargo on Russian oil, Budapest tried unsuccessfully to make its agreement conditional on receiving funds from the Recovery Plan. According to leaks, at a closed Fidesz picnic on 10 September in Kötcse, the prime minister announced that in the autumn the government would try to prevent the EU from extending the sanctions on Russia for another six months. Hungary's opposition last week to the development of a common EU position on the UN's appointment of a special rapporteur on Russian human rights

violations (as reported by Politico.eu on the basis of unofficial information) may be a harbinger of this kind of action.