

HUNGARY: Crunch time for EU funds approaching

- Viktor Orban's government is rushing with anti-corruption reforms not to lose access to more than 13bn of EU funds.
- An eventual compromise is likely, but Budapest's access to EU funds will remain conditional on compliance with anti-corruption and rule-of-law reforms for the foreseeable future.
- While formally unrelated to EU funds, geopolitical considerations could affect the talks between Brussels and Budapest.

Last week, parliament adopted a bill on the establishment of an Integrity Authority, which is tasked to investigate fraud, conflicts of interest, corruption, and other violations related to the use of EU funds. The adopted legislative package also foresees the creation of a separate anti-corruption task force, which would regularly assess existing anti-corruption measures, recommend new ones, and prepare an annual report on risks.

Billions of EU funds at stake

These anti-corruption efforts are part of the 17 remedial measures that Viktor Orban's government has pledged to implement by 19 November in order to address the European Commission's (EC) long-standing concerns over the use of EU funds in Hungary, which could result in financial penalties. As part of the EU's general regime of conditionality for the protection of the budget, on 18 September the EC proposed the European Council (Council) to suspend 65% of funds allocated to Hungary's three operational programs from the bloc's 2021-2027 budget. The proposed financial penalties amount to an estimated EUR 7.5bn or roughly one third of Hungary's total expected allocations from the seven-year budget.

The final decision to suspend funding requires qualified majority support (15 out of 27 member states accounting for 65% of the EUs' population) in the Council. The vote must be taken within one month from the EC's proposal (i.e., by 18 October), but this deadline can be extended in exceptional circumstances for another two months. Considering that the EC has given Hungary until 19 November to implement the agreed remedial measures, such a vote is more likely to take place around mid-December.

At the same time, Hungary is the last EU member state whose National Recovery and Resilience Plan (NRRP) to fund post-pandemic recovery has not yet been approved by the EC. Unless the plan is approved before the end of 2022, Hungary could lose access to 70% (EUR 4.1bn) of EUR 5.9bn allocated to implement the plan.

A compromise is likely

Given the mounting economic and fiscal pressures at home as well as billions of EU funds at stake, Orban's government is demonstrating a willingness to compromise and its commitment to implement the required legislative and regulatory changes by 19 November. Barring some unexpected turnaround, Budapest is likely to adopt the required reforms and present the EC with a dilemma on whether to keep the proposed financial penalties on a country that is willingly and urgently addressing the shortcomings. An excessively strict position on the part of the EC could disincentivize reforms and push Budapest towards closer cooperation with third countries such as China or Russia. However, greenlighting the funds without making sure that the reforms are implemented properly and translate into real changes on the ground could bankroll the increasingly undemocratic Orban's regime.

As many times in the past, the standoff between Brussels and Budapest is likely to result in a compromise. For example, the EC could be expected to approve Hungary's EUR 5.8bn NRRP by the end of the year but link the disbursement of funds to demanding milestones such as judiciary reform, changes to the media landscape, or human rights issues. With regard to the Cohesion Fund, the EC or Council could for instance reduce the proposed cut in financing but keep the procedure going, which requires regular monitoring of compliance with the obligations. Considering that the EC is applying the regime of conditionality for the first time ever, some other options might be possible too. Still, it is increasingly likely that significant amounts of EU funding for Hungary will remain linked to anti-corruption and the rule of law reforms for the foreseeable future.

While the disbursement of EU funds is not directly linked to geopolitical developments or foreign policy decisions, close links between Budapest and Moscow and persisting anti-Brussels rhetoric likely prompt extra caution in the EU institutions when dealing with Orbán's government. At the same time, it cannot be ruled out that Budapest will attempt to leverage its support for sanctions on Russia or the ratification of Finland's and Sweden's membership in NATO for a more favorable agreement on the access of EU funds.

[Client Portal >>](#)

Andrius Tursa

Central & Eastern Europe Advisor
+370 6792 4910
andrius.tursa@teneo.com

© 2022 Teneo. All rights reserved. This material was produced by Teneo for use solely by the recipient. This communication is intended as general background research and is not intended to constitute advice on any particular commercial investment or trade matter or issue and should not be relied upon for such purposes. The views expressed here represent opinions as of this date and are subject to change without notice. The information has been obtained from sources believed to be reliable but no guarantees can be given as to its accuracy, completeness or reliability. No part of this publication may be reproduced, stored in a retrieval system, or transmitted in any form or by any means, electronic or otherwise, without the prior consent of Teneo.