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REGULAR REPORT

ON

HUNGARY'S

PROGRESS TOWARDS ACCESSION

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A. Introduction

a) Preface

In Agenda 2000, the Commission said it would report regularly to the European Council on progress made by each of the candidate countries of Central and Eastern Europe in preparations for membership, and that it would submit its first Report at the end of 1998.

The European Council in Luxembourg decided that: “From the end of 1998, the Commission will make Regular Reports to the Council, together with any necessary recommendations for opening bilateral intergovernmental conferences, reviewing the progress of each Central and Eastern European applicant State towards accession in the light of the Copenhagen criteria, in particular the rate at which it is adopting the Union *acquis*” ... “The Commission’s reports will serve as the basis for taking, in the Council context, the necessary decisions on the conduct of the accession negotiations or their extension to other applicants. In that context, the Commission will continue to follow the method adopted by Agenda 2000 in evaluating applicant States’ ability to meet the economic criteria and fulfil the obligations deriving from accession.”

On this basis, the Commission presented a first series of Regular Reports in October 1998, a second series in October 1999, and a third in November 2000. The Commission has prepared this fourth series of Regular Reports with a view to the Laeken European Council in December 2001.

The structure followed for this Regular Report is the same as that used for the 2000 Regular Report. In line with previous Regular Reports, the present Report:

- describes the relations between Hungary and the Union, in particular in the framework of the Association Agreement;
- analyses the situation in respect of the political criteria set by the 1993 Copenhagen European Council (democracy, rule of law, human rights, protection of minorities);
- assesses Hungary’s situation and prospects in respect of the economic criteria defined by the Copenhagen European Council (a functioning market economy and the capacity to cope with competitive pressures and market forces within the Union);
- addresses the question of Hungary’s capacity to assume the obligations of membership, that is, the *acquis* as expressed in the Treaties, the secondary legislation, and the policies of the Union. This part gives special attention to nuclear safety standards, as underlined by the Cologne and Helsinki European Councils. It encompasses not only the alignment of legislation, but also the development of the judicial and administrative capacity necessary to implement and enforce the *acquis*, as emphasised by the Madrid European Council in December 1995, and confirmed by the Gothenburg European Council in June 2001. At Madrid, the European Council underlined the necessity for the candidate countries to adjust their administrative structures, so as to create the conditions for the harmonious integration of those States. The Gothenburg European Council emphasised the vital importance of the candidate countries’ capacity to effectively implement and enforce the *acquis*, and added

that this required important efforts by the candidates in strengthening and reforming their administrative and judicial structures.

This Report takes into consideration progress since the 2000 Regular Report. It covers the period until 30 September 2001. In some particular cases, however, measures taken after that date are mentioned. It looks at whether intended reforms referred to in the 2000 Regular Report have been carried out and examines new initiatives. In addition, this Report provides also an overall assessment of the global situation for each of the aspects under consideration, setting out for each of them the main steps which remain to be taken by Hungary in preparing for accession.

In accordance with this approach, the assessment of progress in meeting the political and *acquis* criteria (including Hungary's administrative capacity to implement the *acquis*) focuses on what has been accomplished since the last Regular Report, complemented with a view of the global situation for each of the aspects discussed. The economic assessment, for its part, provides, besides an assessment of progress made over the reference period, also a dynamic, forward-looking evaluation of Hungary's economic performance.

The Report contains a separate section examining the extent to which Hungary has addressed the Accession Partnership priorities.

As has been the case in previous Reports, "progress" has been measured on the basis of decisions actually taken, legislation actually adopted, international conventions actually ratified (with due attention being given to implementation), and measures actually implemented. As a matter of principle, legislation or measures, which are in various stages of either preparation or parliamentary approval, have not been taken into account. This approach ensures equal treatment for all the candidate countries and permits an objective assessment of each country in terms of its concrete progress in preparing for accession.

The Report draws on numerous sources of information. The candidate countries have been invited to provide information on progress made in preparations for membership since the publication of the last Regular Report. The National Programmes for the Adoption of the *acquis* of each of the candidate countries, as well as the information they have provided in the framework of the Association Agreement and in the context of the analytical examination of the *acquis* (screening) and the negotiations¹, have served as additional sources. Council deliberations and European Parliament reports and resolutions² have been taken into account in the preparations. The Commission has also drawn on assessments made by various international organisations, and in particular the contributions of the Council of Europe, the OSCE and the International Financial Institutions, as well as that of non-governmental organisations.

¹ As in previous years, the Report does not mention any commitments undertaken or requests made in the context of the accession negotiations.

² For the European Parliament the *rapporteur* is Luis Queiro.

b) Relations between the European Union and Hungary

Recent developments under the Association Agreement (including bilateral trade)

Hungary continued to implement the Europe Agreement correctly and contributed to the smooth functioning of the various joint institutions.

The eighth Association Council met in July 2001, following the ninth Association Committee meeting held in May 2001. These fora provided the occasion to review progress in Hungary's preparations for accession, notably in the light of the Accession Partnership priorities, and in bilateral relations under the Europe Agreement. The system of sub-committees continued to function well as a forum for technical discussions. Over the last year, the Joint Parliamentary Committee, comprising representatives of the Hungarian and European Parliaments, met three times for its 14th, 15th and 16th debates in October 2000, February 2001 and October 2001.

In general, trade relations between the European Community and Hungary continue to be positive and to intensify further. In 2000, EC imports from Hungary amounted to € 21.9 billion, whilst in the same period, EC exports to Hungary amounted to € 23 billion, and are continuously increasing. The EC thus accounts for around 70% of total Hungarian exports and imports. In 2000, the main product groups imported from the EC were machinery, followed by transport equipment and chemical products. Hungary's main product groups exported to the EC in that period were machinery, followed by transport equipment and agricultural products.

Regarding agricultural products, a new agreement on reciprocal concessions with Hungary entered into force in July 2000 on an autonomous basis, pending the conclusion of an Additional Protocol to the Europe Agreement. As a consequence of this agreement, approximately 83% of the EC agricultural imports from Hungary and 62% of EC agricultural exports to Hungary is exempted from duties. A second round of bilateral negotiations for trade liberalisation is presently being prepared and would cover more sensitive sectors, in which current trade is low in particular due to a high degree of tariff protection. Due to the expiry of the bilateral wine agreement between the European Community and Hungary in December 2000, both parties have concluded negotiations relating to new agreements on the reciprocal recognition, protection and control of wine names and spirits designations, including trade arrangements. The results of the trade agreement were applied as of January 2001 as autonomous trade measures pending the adoption of the new agreements as an Additional Protocol to the Europe Agreement (Council Regulation (EC) No 678/2001).

Agreements on the technical level were reached with Hungary on processed agricultural products and on reciprocal tariff concessions in the fisheries sector. The Council is currently dealing with both agreements.

The main difficulty affecting agricultural trade in the reporting period arose in November 2000 due to Hungary's imposition of a ban on exports of non-fodder maize and its discretionary licensing system for other maize exports. Though subsequently lifted in July 2001, these measures led most Community importers to incur significant damages.

In June 2001, the Protocol to the Europe Agreement on Conformity Assessment and Acceptance of Industrial Products (PECA) became operational. The implementation of this

agreement will further remove trade barriers, extending certain benefits of the Internal Market for products groups where alignment with the *acquis* has been completed. The Protocols to the Europe Agreement on PECA are mutual recognition agreements based on the implementation of the *acquis*.

Technical agreement was reached on the revision of the implementing rules regarding the competition provisions of the Europe Agreement, so as to take into account the objections of the Hungarian Constitutional Court to the existing rules. The new rules are to be adopted by an Association Council Decision that is currently being prepared.

Hungary has withdrawn its request for an extension of the grace period for 5 years, during which Hungary was authorised to grant state aid for restructuring purposes to the steel industry under the conditions set out in Article 8(4) of Protocol 2 of the Europe Agreement. Hungary confirmed that no state aids were and will be granted in the period between 1 January 2000 and 31 December 2001 and renewed its commitment to act in full respect of the provisions of Protocol 2 of the Europe Agreement after 31 December 2001.

Accession Partnership / National Programme for the Adoption of the Acquis

A revised Accession Partnership was adopted in December 1999 – its implementation is reviewed in Part D. This Regular Report is accompanied by a proposal from the Commission to update the Accession Partnership. In June 2001, Hungary presented a revised National Programme for the Adoption of the *Acquis* (NPAA), in which it outlines the strategy for accession, including how to achieve the priorities of the Accession Partnership (see Part D).

Community aid

There are three **pre-accession instruments** financed by the European Community to assist the applicant countries of Central and Eastern Europe in their pre-accession preparations: the **Phare** programme; **SAPARD**, which provides aid for agricultural and rural development; and **ISPA**, which finances infrastructure projects in the fields of environment and transport. These programmes concentrate their support on the Accession Partnership priorities that help the candidate countries to fulfil the criteria for membership.

For the years 2000 to 2002, total financial assistance to Hungary amounts annually to around € 96 million from Phare, € 38.7 million from SAPARD and between € 72.8 and 104 million from ISPA.

The **Phare** programme has been providing support to the countries of Central and Eastern Europe since 1989, helping them through a period of fundamental economic and social transition and political change. Its current “pre-accession” focus was put in place in 1997, in response to the Luxembourg European Council’s launching of the present enlargement process.

Phare provides the applicant countries of Central and Eastern Europe with support for institution building (around one third of the Phare allocation), investment to strengthen the regulatory infrastructure needed to ensure compliance with the *acquis* (equally around one third of the allocation), and investment in economic and social cohesion (the remaining one-third of the Phare allocation). This support comprises co-financing for technical assistance, “twinning” and investment-support projects, to help these countries in their efforts to adopt the *acquis* and

strengthen the institutions necessary for implementing and enforcing the *acquis*. This also helps the candidate countries develop the mechanisms and institutions that will be needed to implement Structural Funds after accession and is supported by a limited number of measures (investment or grant schemes) with a regional or thematic focus.

The Phare programme allocated to Hungary € 1 030 million during the period 1992 to 1999 and € 119.8 million in 2000³. The **2001 Phare Programme** for Hungary provides € 89.8 million for the National Programme, which concentrates on the following priorities:

- priority 1: *Support to the Accession Partnership priorities on the political and economic criteria including the integration of minorities;*
- priority 2: *Strengthening administrative capacity to implement and enforce the acquis;*
- priority 3: *Strengthening judicial capacity, law enforcement and border control;*
- priority 4: *Employment and social affairs: Social dialogue and gender equality;*
- priority 5: *Economic cohesion projects, including the preparation for the implementation of Structural Funds;*
- priority 6: *Participation in Community Programmes*

Another €19 million are allocated for cross-border co-operation programmes (CBC), consisting of € 10 million for a CBC programme with Austria, € 5 million for co-operation with Romania, € 2 million for co-operation with Slovakia and € 2 million for co-operation with Slovenia.

Hungary also participates in and benefits from Phare-funded multi-country and horizontal programmes, such as TAIEX and the Small- and Medium-sized Enterprises Facility.

Furthermore, Hungary participates in the following Community programmes: 5th EC Framework Programme on R&D, Leonardo, Socrates, Youth, 5th Framework Programme of the European Atomic Energy Community (Euratom) for Research and Training Activities, Culture 2000, Life III and Fiscalis.

Following the ratification and entry into force of the agreement, the formal participation of Hungary in the European Environment Agency will start in January 2002.

In order to streamline Community legal procedures and thereby facilitate the future participation of Hungary in Community programmes, a Decision has been adopted by the EU-Hungary Association Council establishing the general principles for such participation.

Overall, the impact of Phare has been positive. Effective transfer of know-how, equipment and financial resources has taken place in a number of important fields such as Agriculture, Aid Co-ordination, Education, Trade and Investment Promotion, Transport and Environment. Phare support for Environment, Privatisation and Restructuring and SME Development has succeeded

³ This includes an allocation of €19 million to Cross-Border Co-operation (CBC) Programmes.

in developing sector strategies and essential institutional and financial mechanisms serving enterprises in these sectors

In Hungary, Phare played for example a particularly important role in the following areas:

- In the field of **micro-credit**, the Phare Micro-credit Programme, with an overall budget of € 32.5 million (out of which € 22.4 million was contributed by Phare), has provided more than 16 000 loans to small enterprises over the last nine years. The micro-credit scheme thus contributed to the development of a healthy business environment, and created jobs where most needed.
- In the field of **Internal Market** (Standardisation, Conformity Assessment, Market surveillance), Phare has allocated € 4.5 million to provide technical expertise and to purchase equipment for institutes that test products with regard to their conformity with EC norms. In the **Justice and Home Affairs sector**, € 21.5 million were allocated to purchase surveillance equipment such as patrol boats and mobile thermal camera systems, in order to step up the fight against illegal immigration on Hungary's southern and eastern inland waterways.
- In the context of the Hungary-Austria **Cross-Border Co-operation Programme**, about € 1 million was allocated to the Győr Centre of Innovation and Technology. This project involved the construction of a building, which is now fully occupied by a number of small high-tech and engineering firms.
- In the context of the Hungary-Slovakia **Cross-Border Co-operation Programme**, Phare has co-financed (providing € 10 million) the reconstruction of the Esztergom – Sturovo Bridge over the Danube that was destroyed during the 2nd world war. The bridge was re-inaugurated in October 2001.

The Phare Review of 2000 confirmed the accession-driven approach and emphasised the importance of helping countries to prepare for the Structural Funds. The Review foresees the possibility that the management of Phare funds can be fully decentralised as of 2002, if the strict pre-conditions set down in the Co-ordination Regulation 1266/99 are met. Secondly, Phare programming can be moved onto a multi-annual basis if supporting strategies are in place. Thirdly, the trends introduced in 1997 continue with an increased role for Delegations, further streamlining of procedures and, lastly, increasing emphasis on raising the verifiable and quantifiable impact of Phare projects in institution building, investment in compliance with the *acquis* and economic and social cohesion.

The Hungarian **SAPARD** programme was approved by the Commission in October 2000. The programme is based on two major priorities: the improvement of the competitiveness of the agricultural sector and processing industry focusing on environmental protection aspects, and the enhancement of adaptation capabilities of rural areas (renovation and development of villages, diversification of activities, development and improvement of rural infrastructure).

The Multi-annual Financing Agreement, setting out the rules for implementing SAPARD, and the Annual Financing Agreement, setting out the €38.7 million Community's financial commitments to Hungary for the year 2000, were both signed in March 2001 and entered into force in June 2001. Despite some recent progress, Hungary's preparations for national accreditation of the SAPARD Agency are lagging behind. The Commission decision conferring

management of aid to Hungary - on a fully decentralised basis - will be taken once a number of conditions are met (conclusion and formal acceptance of national accreditation work, notification of the Commission thereof, and examination by the Commission of the basis for the national accreditation).

The **ISPA** programme's contribution for Hungary amounted to € 88 million in 2000. The support was divided equally between environment and transport. In the environment sector, two areas for national priority intervention have been identified, namely, wastewater treatment and solid waste disposal. In the transport sector, ISPA supported the development of railways and roads. The co-financing rate was 50% of the total cost. In general, ISPA projects were co-financed by the European Investment Bank.

During the first year of its operation, 100% of the ISPA funds allocated to Hungary have been committed. In general, the quality of projects submitted was sufficient and acceptable, but there is room for improving project preparation.

All implementation structures have now been put in place in order to ensure proper implementation of the projects. However, better internal co-ordination inside and between the relevant Ministries in charge of ISPA is desirable.

The process towards extended decentralisation is starting and the Hungarian authorities are taking the initial steps in order to assess the situation of the relevant administrative bodies involved in the implementation of Phare and ISPA and to identify gaps to be filled.

Twinning

One of the main challenges the candidate countries continue to face is the need to strengthen their administrative capacity to implement and enforce the *acquis*. As of 1998, the European Commission proposed to mobilise significant human and financial resources to help them in this respect, through the process of twinning of administrations and agencies. The vast body of Member States' expertise is now being made available to the candidate countries through the long-term secondment of civil servants and accompanying short-term expert missions and training.

To start with, twinning focused primarily on the priority sectors of agriculture, environment, public finance, justice and home affairs and preparatory measures for the Structural Funds. It now covers all sectors pursuant to the *acquis*.

A total of 372 twinning projects, primarily in the fields of agriculture, environment, public finance, justice and home affairs and preparation for the management of Structural Funds, have been funded by the Community between 1998-2000. These represent the principal priority sectors that have been identified in the Accession Partnerships. But also other important sectors of the *acquis* have been addressed through twinning, for example, social policy, fight against drugs, transport, and telecommunications regulation.

Thanks to the strong support and response from EU Member States 103 twinning partnerships, funded by Phare 1998 and involving all candidate countries and almost all Member States, are coming to an end or have been concluded. Under Phare 1999 a further 124 projects are being implemented, and the programming exercise for Phare 2000 includes a further 145 twinning

projects. The 2001 programming exercise foresees 131 twinning projects across all Phare beneficiary countries, as well as Cyprus and Malta. Furthermore, the candidate countries are being offered the possibility of drawing on Member States' expertise through "Twinning light" (projects of up to six months' duration), to address well-circumscribed subjects of limited scope which emerge during the negotiation process as requiring adaptation. It is estimated that around 250 twinning projects are operational throughout the candidate countries at any one time.

For Hungary, 23 twinning projects were funded under the 1997, 1998 and 1999 Phare programmes, out of which 13 have been completed. Eight additional projects, that have already been launched, were financed under Phare 2000. They provide assistance in the areas of agriculture, environment, regional development, social policy, customs and fight against drugs. Phare 2001 will finance 18 twinning projects covering areas such as energy, market surveillance, agriculture, social dialogue, environment, justice and home affairs, traffic control, regional policy and the management of future structural funds.

Negotiations / screening

The analytical examination of the *acquis* (screening) has been carried out in the context of meetings of the Association Committee and the sub-committees.

Since the opening of the accession negotiations, substantial discussions on the individual chapters of the *acquis* were launched, and by December 1999, negotiations on all chapters concerning Hungary (with the exception of chapter 30 – Institutions, and chapter 31 – Other) have been initiated.

By the end of September 2001, the following 22 chapters had been provisionally closed: Free movement of goods, services, capital and persons, company law, fisheries, taxation, Economic and Monetary Union, statistics, social policy and employment, energy, industrial policy, small and medium-sized enterprises, science and research, education and training, telecommunications and information technologies, environment, consumers and health protection, customs union, external relations, Common Foreign and Security Policy and financial control.

B. Criteria for membership

1. Political criteria

Introduction

The political criteria for accession to be met by the candidate countries, as laid down by the Copenhagen European Council in June 1993, stipulate that these countries must have achieved “stability of institutions guaranteeing democracy, the rule of law, human rights and respect for and protection of minorities.”⁴

In its 2000 Regular Report on Hungary’s progress towards accession, the Commission concluded that:

"Hungary continues to fulfil the Copenhagen Political Criteria.

Further progress in the modernisation of the public administration is apparent from the continued implementation of the 1999 development programme.

Although the judiciary functions satisfactorily and the training of judges in the EC *acquis* has progressed, the large backlog of cases before the Supreme Court hampers the unification of the Court practice and the development of a consistent jurisprudence. Efforts should be made to remedy this. Sustained training programmes for civil servants and judges should continue in line with the medium-term Accession Partnership.

Despite a number of important measures taken to fight corruption, this remains a problem and renewed efforts should be made to address this issue.

Hungary continues to respect human rights and freedoms. However, overcrowding of prisons is a growing problem, which needs to be remedied.

In line with the short-term Accession Partnership priority, Hungary started to implement the medium-term Roma action programme, supported by financial means at national and local level. This programme facilitates the integration of the Roma and their fight against discrimination in the fields of education, culture, employment, housing, health and social services. However, sustained implementation of this programme is needed in order to obtain concrete results in the medium-term. "

The section below aims to provide an assessment of developments in Hungary since the 2000 regular report, as well as of the overall situation in the country, seen from the perspective of the political Copenhagen criteria, including as regards the overall functioning of the country’s executive and its judicial system. Developments in this context are in many ways closely linked to developments regarding Hungary’s ability to implement the *acquis*, in particular in the domain of justice and home affairs. Specific information on the development of Hungary’s ability to implement the *acquis* in the field of justice and home affairs can be found in the relevant

⁴ These principles have been emphasised in the Charter of Fundamental Rights of the European Union that was proclaimed at the Nice European Council in December 2000.

section (*Chapter 24 – Co-operation in the field of justice and home affairs*) of part B.3.1. of this report.

Recent developments

Accession to the European Union remains high on the political agenda of the Government and efforts were intensified to progress in accession preparations.

1.1. Democracy and the rule of law

As mentioned in the previous Regular Reports, Hungary has achieved stability of institutions guaranteeing democracy and the rule of law. This section focuses on the most significant developments of the past year.

The Parliament

Parliament continues to function smoothly. The overall law-making process is advancing steadily with good results as to the further alignment with the *acquis communautaire*.

In September 2000, a political consensus on accession was reached between all parties, which eased the preparations for accession in the parliamentary context.

There was however no progress in Parliament on agreeing on a system to ensure seats for minorities, although the Hungarian Constitutional Court had already ruled in 1992 that the absence of such a system is unconstitutional.

There exist four Parliamentary Ombudsmen in Hungary. They cover civil and political rights, national and ethnic minorities, education, data protection and freedom of information. Their task is to investigate violations of constitutional rights and to initiate general or individual measures for the remedy of such violations. In this context they are entitled to investigate any authority and request relevant data for inspection. Financial independence is also provided for, as is immunity. The Ombudsmen are elected for six years by a two-thirds majority of votes in Parliament. The last vote took place in July 2001, when three Ombudsmen were newly appointed. There was however no agreement on the new Ombudsman for data protection, so that the post could not be filled. The Ombudsmen are exclusively answerable to Parliament and have to present an annual report on their activity. Their opinions and recommendations are made public and generally have a demonstrable effect.

The executive

The continued reform of the Hungarian public administration remains a priority task under the government programme, and over the past year, further progress has been made in this respect.

The existing legal framework for civil servants, amended in 2001, ensures their independence and career opportunities. Civil servants are appointed on basis of an examination, for indefinite duration. Activities not compatible with the public service are not allowed, nor are political activities in form of a party position or public actions in the name or on behalf of political parties.

In July 2001 a new law on civil servants provided the framework for making the Hungarian civil service more accountable and more efficient. The provisions of the law include a compulsory ethical code, assets declaration for high-ranking civil servants, including their family members, and stricter control mechanisms as part of the Government's fight against corruption, with a focus on preventive measures. Another important element is the obligatory command of a foreign language for future civil servants. The Law also provides for the creation of a "civil servant elite" which would receive outstanding salaries. Budgetary means were significantly increased (by more than four times) reaching € 75 mio in order to ensure the smooth implementation of the law in 2001 including a considerable salary increase of 70% over the next three years above the annual inflation rate and an increased premium for foreign language proficiency. This important change in the salary structure should help to improve the overall status of civil servants and to attract well-educated staff.

As part of the reform, training became a priority and civil servants are obliged to pass an examination on EU related questions. So far, more than one tenth of the civil servants have undergone this examination, which should be completed by 2004. The Hungarian Institute of Public Administration at the Prime Minister's Office is in charge of this task.

Some problems remain however at the level of local administration, notably the relatively low level of local finances through taxation. In view of the continuing process of decentralisation, measures should be enhanced to ensure that the financial means of local authorities are sufficient in order to allow them to carry out their new additional tasks.

The judicial system

Over the reference period Hungary continued to implement the reform of the judicial system and introduced new measures to improve overall efficiency.

Hungary has a well-established court system with three levels: local courts (131), county courts (20), and the Supreme Court. The local and county courts proceed as courts of first instance. County Courts act as appeal Courts in the lawsuits in which the local Court acted as the court of first instance. The Supreme Court acts as an appeal Court in cases brought to it against judgements rendered by county Courts as first instance courts. The Supreme Court is also entitled to review applications for revisions of final judgements as extraordinary remedy. Its basic task is to guarantee the uniform application of law by Courts and the provision of judicial guidance to lower Courts.

The National Council of Justice is in charge of the self-administration of courts and the selection, promotion, evaluation and training of judges. The President of the Council is the President of the Supreme Court. According to the law on the organisation and administration of courts, the National Council of Justice is responsible for the elaboration of the budgetary chapter for the judiciary. This proposal is submitted to the Government. The Government makes its legislative proposal on the central budget, including the chapter for the judiciary, to the Parliament. If there is a difference between the two proposals, the Government must present the proposal of the Council and indicate the reason for the difference.

The Constitutional Court continues to operate at full strength (11 judges).

The Constitution guarantees the independence, impartiality and irremovability of judges.

Judges have to undergo a thorough education and training process and are specialised in civil, criminal and administrative cases. They have to pass a special exam in order to become a judge. The President of the Republic makes the final nomination – on a proposal of the National Council of Justice - after a further probation period of three years. A judge may only be removed or relocated on the basis of specific reasons defined by law. Conflict-of-interest rules prohibit political or economic activities.

Public Prosecution is part of the Hungarian judicial system. The main task of the prosecutors is to bring criminal cases before the courts. Their investigative powers and other competencies are laid down in the Constitution, in relevant Laws and international instruments. One of their main functions is to safeguard the lawfulness of criminal investigations. This includes revising the measures taken by the authorities in the course of investigations, assessing and overseeing the lawfulness of arrests and ordering investigation of an offence or supplementary investigation

The following new developments in the further implementation of judicial reform can be reported:

- The total number of posts for judges at all court levels (local, county and Supreme courts) slightly increased (at local and county level the total number of post reached 2486 in 2001 against 2480 in 2000 and at the level of the Supreme Court this number was 113 in 2001 against 110 in 2000).
- The overall efficiency of court procedures further improved and there was a net increase in cases handled and settled during the reference period. Most proceedings are finished within six months to two years.
- An additional 670 judges received training in Community law.
- The Court Information System was further modernised and is now operational at 19 county Courts, at the Budapest Metropolitan Court and at the Supreme Court and the National Council of Justice. Further links are under establishment for the remaining 130 courts. The system facilitates co-operation between law enforcement bodies by rapid exchange of information. The system provides on-line access to national legislation and to CELEX, the legal database of the European Union.

However, the overall number of cases arriving at the Supreme Court further increased, with the majority of cases being appeal cases. The new Regional Court of Appeal, which – as decided by law - will be set up in 2003 in Budapest, should facilitate and speed up the proceedings in the Supreme Court.

Overall technical facilities at Courts are still inadequate and judges have to spend considerable time on administrative matters connected with their cases. The new profession of “legal assistant” is intended to provide qualified administrative support to Judges. The first college training for this new curriculum started in the academic year 2000-2001.

Despite a nominal increase in the budgetary allocation for the judicial chapter, actual funding for the judiciary has declined, contrary to what would be needed in the light of the increased number of judges and their increasing tasks (resulting in an increased caseload). Budgetary means are also not sufficient to ensure proper court building maintenance and to offer the appropriate facilities for the smooth functioning of Courts. Over the past years, the budgetary

proposals presented by the Government to Parliament were considerably lower than those proposed by the National Council of Justice. The final budget adopted by the Parliament was close to the Government's proposal. However, for the budgetary years 2001-2002 a supplementary budget up to the amount of € 15 mio (corresponding to 11% of the overall allocation) was allocated to the judicial chapter for the recruitment of additional staff and the improvement and extension of the Court infrastructure.

Overall, the judiciary continues to function satisfactorily, with first trends showing improved efficiency. The main problem remains the overloaded Supreme Court, which is hampered in the execution of its main function, and the scarce budgetary resources to implement the remaining elements of the reform started already in 1997.

Anti-corruption measures

Although the fight against corruption remained high on the political agenda of the Government, corruption continued to be a problem, as also pointed out in last year's Regular Report. To address the issue, the following steps were undertaken during the reference period:

- The Government approved a long-term anti-corruption strategy containing modifications to existing laws and a completely new law on lobbying activities. The package covers, among other things, regulations on incompatibility and the extension of the property declaration obligation. Persons responsible for bribery have to be dismissed. Those who pay the bribe ("active briber") may escape prosecution if they detect the bribery and closely co-operate with the authorities. A special body will monitor the enforcement of the forthcoming anti-corruption strategy.
- Parliament adopted stricter conflict-of-interest regulations according to which high-ranking civil servants and their families will have to give an account of their assets annually. Cases raising suspicion will be followed up by a Public Service Control office under the authority of the Ministry of Interior.
- Parliament also amended the law regulating MPs' asset statements. The amendment obliges MPs to make annual asset statements and to include in them all sources of their income.
- Within the Hungarian police forces a mobile unit was created to combat bribery of police officers on street duty. Their task is to detect and report on officers claiming bribes from citizens and to start disciplinary action or criminal proceedings against them, which would then be pursued by the General Prosecutor's Office. In 2000, around 800 such cases were detected.
- Hungary ratified the Council of Europe Criminal Law Convention on Corruption in November 2000.

Hungary is also member of GRECO (Council of Europe Group of States against Corruption), which has made provisions in its statute for regular evaluation of its member countries. As such Hungary is currently being evaluated. Hungary is also participating in the monitoring of anti-corruption measures effected by the OECD Working Group on Bribery in international commercial transactions.

Hungary has not signed the Council of Europe Civil Law Convention on Corruption.

In spite of these developments, there is a continuous negative background of corruption which could undermine the trust of the citizens in the democratic institutions.

1.2. Human rights and the protection of minorities

As mentioned in the previous Regular Reports, Hungary has continued to respect human rights and freedoms. The following section concentrates on major developments since the last Regular Report.

Hungary has already acceded to most of the major human rights instruments (see annex).

In November 2000, Hungary signed Protocol No.12. of the European Convention for the Protection of Human Rights and Fundamental Freedoms containing the general prohibition of discrimination on any grounds, such as sex, race, colour, language, religion, political or other opinion, national or social origin, association with a national minority, property, birth or other status.

Hungary does not have a unified law on anti-discrimination; a codification committee set up by the Minister of Justice has reviewed the anti-discrimination provisions contained in the current legislation with a view to legal consolidation. As a result of the review, it was considered that law enforcement and the sanction system should be strengthened and consistently implemented. It should be noted that the new Labour Law of July had already taken into consideration elements of the anti discrimination *acquis*. In the meantime, the Ombudsman for the rights of national and ethnic minorities submitted his own proposal for a general anti-discrimination law.

The Ombudsman for civil and political rights is responsible for the investigation of cases involving the infringement of constitutional rights. His last annual report stated that the trend of complaints submitted was increasing (around 12%) with the majority of complaints being lodged by NGOs and private persons. Amongst the complaints, the biggest increase was registered in the violation of the rights for rule of law and legal safety (from 379 cases in 1999 to 599 cases in 2000), the right to property (from 128 to 216), the right to best possible physical and mental health (from 96 to 153 cases), the right to healthy environment and the right to life and human dignity. This situation can be explained by increased access by the public to the Office of the Ombudsman and seems to indicate a need to strengthen the legal framework and enforcement mechanisms in these areas.

Civil and political rights

Over the reference period, considerable progress was achieved in the area of asylum, where the situation of asylum seekers has greatly improved. Problems continue to exist notably regarding trafficking in human beings, police behaviour and prison conditions.

Public opinion of *police* behaviour is not very high. Police officers are often suspected of corruption and accused of frequent use of excessive force. In particular, international human rights organisations reported cases of unjustified and *harsh police action* against Roma people as well as the mistreatment of foreigners. The overall number of complaints regarding unjustified police measures lodged at the Offices of the Ombudsman for National and Ethnic Minorities and for Civil Rights had increased in 2000. Of the complaints introduced, only around 30% resulted in court cases whilst in 70% no investigation occurred. Many cases did not reach the

court system and are still pending. However, there have recently been some positive developments in this respect: The Supreme Court decided on a financial compensation to four Romani men who had been mistreated by police special units and in a local court decision, perpetrators were convicted for having physically abused Romani because of their ethnic origin.

There are indications that Hungary became increasingly a country of transit and destination for *trafficking in human beings*. To combat trafficking in human beings, Hungary is cooperating with a number of European countries. Sentences for trafficking have also become stricter (up to 10 years) and foreign traffickers can be expelled from Hungary with immediate effect following a change to the law on the entry and stay of foreigners in May 2001. With a view to better protecting victims, a Victim Protection Office and a victim protection fund were established. Relevant information on victim protection is available in every police station.

Prison conditions continue to be a problem. Prisons are occupied to 58% over capacity, as facilities have been neglected for a long period. According to the Ombudsman for civil rights, certain prisons are below standard and do not offer appropriate facilities for inmates. Accordingly, the number of complaints lodged with the Ombudsman increased over recent months. In order to remedy the situation, the Government development programme foresees the construction of further facilities by 2007. In September 2000 the first new prison in over 100 years was opened in Budapest.

According to recent statistics (from the UN High Commissioner for Refugees) the total number of *asylum-seekers* in Hungary started to decrease significantly by some 32.2% (from 11 500 to 7 800) in 2000. Processing time for asylum applications was reduced to one year (previously 2½ years) - which corresponds broadly to the European average. Since mid-2000 procedural deadlines are generally kept. Some 2541 applications were received in the first quarter of 2001 of which 50% have already been processed. The new Law on Asylum adopted in May 2001 (entry into force in January 2002) introduced amendments to existing legislation, in particular as concerns the definition of unaccompanied minors. It also created the legal background for the future implementation and application of the Dublin Convention. It also reduced the duration of asylum procedures by entitling the asylum authority to decide on the expulsion of asylum applicants whose applications were rejected. For illegal immigrants, the maximum time period for which they can be kept in border guard shelters was reduced from 18 months to 12 months as of January 2001. The Government continued its efforts to modernise the reception facilities for asylum seekers and illegal immigrants. The majority of the reception facilities now fulfil the minimum standards for health conditions and provide basic care. The integration of recognised asylum seekers into society is still difficult and the Government would need to undertake appropriate measures.

Hungary continues to respect the *freedom of the press*. More than 80 percent of the print media and some 70 percent of radio and television stations are in private hands. The financial situation in public service television is at risk. Its basic capital has been reduced to one-tenth, outstanding public debts have doubled and numerous staff have been dismissed over the past two years in an attempt to render it more competitive. In these circumstances it is questionable whether public service television is still able to fulfil the requirements of public service media. The supervision of the public service media by the Presidium of the Boards of Trustees is still not properly ensured. The three Presidiums continue to be composed solely of pro-government members. Despite initiatives taken by the Government, Parliament was not able to settle the issue, as it did not reach the two-thirds majority required for the adoption of a new law. The

situation, which has remained unsolved for two years now, might lead to growing political pressure on the public service media .

Freedom of religion is enshrined in the Hungarian constitution and no particular problems have been reported in this respect.

Homosexual (male or female) relations with minors of 14 years or over are punishable under the criminal law, whereas heterosexual relations with the same age group are not if there is consent. Therefore a difference in the age of consent, depending on *sexual orientation*, remains in place.

The *NGO* sector plays an important role in Hungarian society and the number of NGOs has further increased over the last year. The amendments to the law on taxes made in 2000 give NGOs recognised as being of public service the ability to deduct certain taxes.

Economic, social and cultural rights

Some further progress was made in this area, notably as regards people with disabilities and equal opportunities.

The principle of *equal opportunities* is laid down in the Constitution. However, at parliamentary level, the representation of women is still rather weak and is less than 9%. As a further new development in favour of women, the new Labour Law, adopted in March 2001, strengthens the prohibition of discrimination and includes provisions on equal pay for equal work. It remains to be seen whether implementing measures will be able to address the still difficult situation of women on the labour market (*see also chapter 13: Social policy and employment*).

Hungary ratified the Optional protocol to the Convention on the Elimination of All Forms of Discrimination against Women (CEDAW) in December 2000.

Whilst the legal framework for *people with disabilities* was further strengthened through certain provisions of the new Labour Law on social employment and protection against discrimination, the implementation of the National Disability Programme, adopted in 2000, is lagging behind. One of the important elements of the programme, the disability allowance, was however introduced in January 2001. The creation of job opportunities for people with disabilities was further supported under the two-year budgets. Overall, services for people with disabilities are still limited and public buildings are difficult to access.

There are numerous *trade unions* and employers organisations in Hungary and one third of the workforce are union members. However, autonomous social dialogue between workers and employers remains limited, mostly at enterprise level. At the tripartite level, a relationship of trust between the social partners and government is clearly lacking. Due attention would need to be given to the proper use of the new tripartite structures to permit effective social dialogue at that level (*see also chapter 13: Social policy and employment*).

Minority rights and the protection of minorities

Over the reference period, Hungary further strengthened policy instruments and measures to

improve the rights of minorities, with particular emphasis on the situation of the Roma.

In a separate development, in June 2001, Parliament adopted the Law on Hungarians living in neighbouring countries, with the objective of supporting Hungarian minorities in neighbouring countries and to maintain their cultural heritage (*see Chapter 27 - Common foreign and security policy*).

Whilst the other 12 recognised minorities are well integrated into Hungarian society, the situation of the Roma minority in Hungary remains difficult. Roma account for up to 6% of the population. In general they face poor living conditions and social disadvantages, as a large proportion of them are unemployed. Their mortality rate is over double the national average and there is a life expectancy gap vis-à-vis non-Roma of 10-15 years due to low health standards. Generally, Roma live in parts of the country with underdeveloped infrastructures and weak economic structures. Currently, the majority of Roma students finish primary school, but less than one percent gets a degree in higher education. In addition, the frequent transfer of Roma children out of the mainstream system to special education facilities is a way of discriminating against them, according to the Ombudsman for national and ethnic minorities. Experience has shown that these special facilities generally do not close the gap with the mainstream, but instead widen the education gap. According to estimates, there are more than 150 schools in Hungary where special Roma classes are maintained. In recent years the legal provisions on enrolling children in special classes have become stricter, and the “special status” of the children involved can now be revised any time.

The cumulation of the above factors results in a situation where the Roma are isolated and experience widespread discrimination in education, employment, access to justice and to public services. This is also confirmed by the annual report of the Ombudsman for national and ethnic minorities, which showed that the number of the cases lodged with his Office had further increased in 2000 (459 in 2000 against 435 in 1999). Most of the complaints concerned the Roma minority (291) and affected the local self-governments (126 against 114) and the police forces (35 against 25).

With a view to strengthening the policy framework for the social integration of the Roma minority, in July 2001 the Government prepared a new long-term strategy. Already in 1999 and in line with the Accession Partnership, the Hungarian Government had adopted a medium-term package of measures with a view to better integrating the Roma minority into Hungarian society. Whilst in the early stage of the package no specific funds were available from the central budget for implementation, the situation changed in 2000 and improved further in 2001 when the Government increased budgetary efforts by 30% (against 2000). The funds amounting to € 35 mio come from three different budgetary sources. Certain forms of assistance are targeted directly at the Roma (€ 23 mio), some other resources are made available to both national and ethnic minorities, whereas other funds focus on economically disadvantaged groups. However, the implementation of the programme has been rather slow so far, due to a lack of co-ordination between Ministries involved.

In the period under consideration, the most important measures have been taken in the areas of education, employment, legal protection and culture.

As a consequence, education for Roma in their mother tongue and language teaching is available to more than 75,000 children in kindergarten and primary school. In addition, there has been a

large increase in study grants for Roma students during the 2000-2001 school year (more than 7,580 up from 785 in 1997).

In the field of employment, Roma have actively participated in the public works programme of the Ministry of Social and Family Affairs. Roma received approximately 40% of the funds allocated.

As an important further step in the area of social policy and public health, in January 2001 the Government extended its house-building programme to the Roma, and allocated € 1.1 mio for the purpose. Preconditions for Roma families include that children must attend school and at least one of the parents has to have a job or should participate in some community-service work programme. The scheme will be implemented by the National Roma Self-Governments. Under the national programme for public health € 9.4 mio were made available to set up some 120 health centres to improve health standards. The centres will contain bathing facilities and a kitchen for cooking courses. The programme also envisages training of district nurses.

In order to improve the legal protection of the Roma, specific local conflict management offices and programmes were set up under the Ministry of the Interior. The Ministry of Justice is providing for free legal advice to Roma. In addition, the Office of National and Ethnic Minorities has supported some 29 local legal protection bureaux and the setting up of a network of local conflict-prevention centres. Police received special training on Roma culture in order to decrease the cases of ill-treatment. The police are also promoting the recruitment of Roma people.

Roma Culture is promoted through what are known as Roma Community Houses, a Roma theatre and a Roma information and cultural centre. In the field of disseminating information to the Roma, a major step was taken in spring 2001 when the National Television and Radio Board (ORTT) granted a broadcasting license for Europe's only Roma Radio, Radio C, which now broadcasts in the area of Budapest targeting some 100,000 Roma. Around one hour daily is broadcast in the Roma language. On the other hand, the budget of the Roma Magazine of Hungarian public service TV was considerably decreased, endangering its operation.

As part of the institutional framework, the Office for national and ethnic minorities prepares and monitors the implementation of minority policy. Through the system of local self-Governments, minorities have a considerable degree of cultural autonomy as well as a wide range of educational and linguistic rights.

Overall, the Government has made efforts to progress with the implementation of a comprehensive programme to improve the situation of the Roma and increased the budgetary means to implement it. However these means remain limited in relation to the extent of the social disadvantage affecting the Roma population. The situation in the education sector remains of particular concern as in certain areas up to one third of the school population is of Roma origin and the school system lacks the human and financial resources to specifically address the educational needs of a large portion of the school population. Despite these considerable and acknowledged efforts, the integration of the Roma into the economic and social fabric is only at the beginning of what may be a long process. Hence the importance of determined and sustained efforts to fight against discriminatory attitudes and behaviour, in particular at local and regional level, and to fully implement and enforce existing legislation and to address the situation of widespread social disadvantage affecting the Roma minority. Also, a more direct involvement

of Roma communities' representatives would make those representatives more successful and enhance the integration process. Furthermore, the introduction of impact assessment mechanisms would help to improve the focus of the various measures on the target population. Finally, more active participation of the Roma minority in public life, including through their representation in Parliament, would give a further impetus to the process.

1.3. General evaluation⁵

In its 1997 Opinion, the Commission concluded that Hungary fulfilled the political criteria. Since that time, the country has made considerable progress in further consolidating and deepening the stability of its institutions guaranteeing democracy, the rule of law, human rights and respect for and protection of minorities. Over the past year, further efforts have been made in this direction. Hungary continues to fulfil the Copenhagen political criteria.

In the area of public administration reform, positive steps were taken with the introduction of a new legal framework increasing accountability and efficiency of the administration. In addition, better salaries and career possibilities have made the civil service more attractive. Efforts also continued in the area of training, which has become an important element of the career structure.

Within the judiciary, the overall efficiency of Courts further improved after the introduction of additional measures in the area of institution building, notably the modernisation of IT systems, procedures, continued training and new staff. However, the continued overloading of the Supreme Court reduces its ability to provide guidance to lower courts and to unify the Courts' practice. The scarce budgetary resources make it difficult to implement the remaining elements of the judicial reform.

The fight against corruption remained high on the political agenda and new legislation on asset declaration and more severe punishment was adopted to address the issue. Corruption however remains a problem, and the new measures would need to be implemented quickly to make the fight more effective.

As regards human rights and freedoms, progress can be reported with regard to asylum, where the situation considerably improved due to faster and better procedures and more appropriate reception facilities. However, there is a need to address police behaviour, notably with regard to reported cases of ill-treatment. In the area of public service media, a solution needs to be found regarding the composition of the Supervisory Boards of Trustees.

New policy instruments and measures were adopted for the Roma minority. This process was accompanied by a significant increase of budgetary means for the further implementation of the medium-term action programme, already adopted by the Government in 1999. Support measures in 2001 mainly focused on the areas of education, employment, social policy, legal protection and culture. In this context, it will be important to enhance efforts to fight against widespread discrimination and to fully implement and enforce the legislation already in place. The Roma minority should also be given the possibility to participate more actively in public life.

⁵ See "Making a success of enlargement: Strategy Paper and Report of the European Commission on the progress towards accession by each of the candidate countries", COM (2001) 700.

Hungary had implemented the short- and medium-term priorities of the 1999 Accession Partnership priorities which related to the continued implementation of the medium-term action programme for the Roma and the increase of budgetary means for this purpose, as well as the further reform of public administration and of the judiciary.

2. Economic criteria

2.1. Introduction

In its 1997 Opinion on Hungary's application for EU membership, the Commission concluded:

“Hungary can be regarded as a functioning market economy”; "it should be well able to cope with the competitive pressure and market forces within the Union in the medium term".

This finding was confirmed in the 1998 and 1999 Regular Reports. In its 2000 Regular Report, the Commission found that:

"Hungary is a functioning market economy and should be able to cope with competitive pressure and market forces within the Union in the near term, provided that it stays on its present reform path",

In examining the economic developments in Hungary since the Opinion, the Commission's approach was guided by the conclusions of the European Council in Copenhagen in June 1993 which stated that membership of the Union requires:

- the existence of a functioning market economy;
- the capacity to cope with competitive pressure and market forces within the Union.

In the analysis below, the Commission has followed the methodology applied in the Opinion and in the previous annual Regular Reports.

2.2. Economic developments

The macroeconomic situation continues to be sound. Based on past structural reforms and careful macro-economic management, economic growth has reached its highest level since the beginning of transition. Although privatisation is nearly completed, foreign direct investment (FDI) remains the motor of growth and productivity gains. Inflation is still relatively high, and it is only recently that the authorities have responded by making changes to the exchange rate and monetary policies, focussing on the further reduction of inflation. The current account improved substantially. Fiscal consolidation continued in 2000, but fiscal policy has become expansionary in 2001.

Main economic trends							
Hungary		1996	1997	1998	1999	2000	2001 latest
Real GDP growth rate	per cent	1.3	4.6	4.9	4.2	5.2	4.2 H1
Inflation rate ⁶							
- annual average	per cent	23.5	18.5	14.2	10.0	10.0	9.9 Jan-Sep
- December-on-December	per cent	19.9	18.6	10.1	11.4	10.0	8.0 Sep-Sep
Unemployment rate, end-year							
- ILO definition	per cent	9.9	8.7	7.8	7.0	6.4	5.8 Jan-Aug
General government budget balance	per cent of GDP	-3.2	-6.8	-7.8	-5.4	-3.1	:
Current account balance	per cent of GDP	-3.8	-2.1	-4.8	-4.4	-3.3	:
	million ECU/euro	-1,339	-848	-2,020	-1,975	-1,620	-365 ⁷ Jan-Aug
Foreign debt							
- debt export ratio	per cent	157.3	116.3	108.7	105.8	82.5	:
- gross foreign debt	million ECU/euro	21,746	21,354	23,079	25,272	25,562	:
Foreign direct investment in flow							
- balance of payments data	per cent of GDP	4.0	4.0	3.0	3.4	2.9	:
	million ECU/euro	1,426	1,603	1,260	1,552	1,458	911 ⁸ Jan-Aug

The focus of structural reform is shifting, as Hungary's transition process matures. Given the advanced stage of structural reforms, further progress in the past year has been limited, in particular with regard to the health care system. The implementation of the Széchenyi plan for economic reform in the period 2001-2006 is still at an early stage, although first effects in the areas of private housing construction and SMEs can be observed. The restructuring of the

⁶ PROXY HICP since 1996, CPI 2001 latest (see methodological notes).

⁷ Source: National Bank

⁸ Source: National Bank

railway system continued, and large-scale debt relief combined with a rescheduling of remaining debt has been carried out, but needs to be complemented by more fundamental restructuring. The government's grip on prices in regulated sectors remains too tight. A step-by-step liberalisation of the telecom, gas and electricity sector has been initiated recently.

Main Indicators of Economic Structure in 2000		
Population (average)	thousand	10,024
GDP per head ⁹	PPS	11,700
	Per cent of EU average	52
Share of agriculture ¹⁰ in:		
- gross value added	per cent	4.1
- employment	per cent	6.5 ¹¹
Investment-to-GDP ratio ¹²	per cent	24.6
Gross foreign debt/GDP ¹³	per cent	51.6
Exports of goods & services/GDP	per cent	62.5
Stock of foreign direct investment	million euro	17,946
	euro per head ¹⁴	1,790

Hungary has been continuously catching-up with the EU. The GDP per capita in purchasing power standards (PPS) was 52% of the EU average in 2000, on a steadily increasing trend from 46% in 1995. Regional income disparities are considerable. Compared to the EU average, the GDP per capita in PPS of the central region around Budapest reached a level of 76%, while the Northern Great Plain remains at a modest 32%. Hungary has relatively low rates of participation in the labour markets. In 2000, the economic activity rate and the employment rate have been increasing slightly to the still low rates of 50% and 55.9% respectively. Conversely, unemployment has been declining to just 6.4%. The female unemployment rate was 5.6%, which is below the 7% rate for male. However, economic activity rates for women are also

⁹ Figures have been calculated using the population figures from National Accounts, which may differ from those used in demographic statistics.

¹⁰ Agriculture, hunting, forestry and fishing.

¹¹ Data refer to 1999.

¹² Data refer to Gross fixed capital formation as % of GDP.

¹³ Estimated.

¹⁴ Figures have been calculated using the population figures from National Accounts, which may differ from those used in demographic statistics.

much lower. Youth unemployment stood at around 12% and the share of long-term unemployment in total unemployment was over 44%, both on a rapidly declining trend. Minimum wages increased substantially in 2001, from € 96 to € 192 a month, affecting roughly 25% of the work force.

2.3. Assessment in terms of the Copenhagen criteria

The existence of a functioning market economy

The existence of a functioning market economy requires that prices, as well as trade, are liberalised and that an enforceable legal system, including property rights, is in place. Macroeconomic stability and consensus about economic policy enhance the performance of a market economy. A well-developed financial sector and the absence of any significant barriers to market entry and exit improve the efficiency of the economy.

Strong political consensus on EU accession and economic reform remains unchallenged throughout the political spectrum. The success of the supply-side reforms of recent years is due in no small part to significant wage restraint. The government increased the very low minimum and public wages and pensions significantly in 2001, thus securing continued public support for the transformation process, and also guarding against a brain-drain from public administration. However, developments should be closely monitored to offset any negative effects of these increases on the functioning of labour markets.

Medium-term economic programming plays an increasingly important role in the macro-economic management of the Hungarian economy. The considerable extent to which the Hungarian government has been able to meet its fiscal targets and policy commitments has contributed to a stable and predictable market environment. The analytical and technical capacity of the Hungarian authorities is developing progressively, and co-ordination between several ministries, the National Bank and other institutions functions reasonably well. In May 2001, Hungary submitted its first 'Pre-accession Economic Programme' (PEP) to the Commission. The elaboration of the programme was well co-ordinated and it was formally adopted by the government, and thus represents a firm political commitment.

In 2000, the Hungarian economy grew by 5.2%, the highest rate since the beginning of transition. Despite a deterioration of the international environment, GDP continued to grow by a robust 4.2% during the first six months of 2001 over the same period in 2000. At 15.6%, volume growth of exports during the first half of 2001 indicated a declining trend, as compared to the record 21.8% annual export growth rate in 2000. Over the same period, import growth went down to 14.7%, from 21.8% in the year 2000. Investment increased considerably by 7.7% in 2000, and was more subdued at 4.4% during the first six months of 2001. The structure of growth is changing. Household consumption, which had remained very modest in recent years, is picking up, at a rate of 4.2% during the first six months, reflecting a 4.5% increase in real wages over the same period. Growth of government consumption remained moderate in 2000, and at just 1.6% increased slower than GDP during the first half of 2001. Recent indicators, in particular a drop in industrial output in June and July 2001, suggest a slowing growth trend.

Unemployment further declined below the 6% mark in 2001. Robust economic growth was underpinned by profound structural adjustments in the Hungarian labour market, through

reallocation of labour between sectors and a strong increase in labour productivity. As a result, the unemployment rate was as low as 6.4% in 2000, and declined further to an average 5.8% during the first six months of 2001. However, large local disparities remain. Whereas in the Budapest area labour markets are getting tight, in the underdeveloped East of Hungary unemployment still stands at double-digit levels. The favourable unemployment developments are tainted by a 44.2% share of long-term unemployed. That segment of the labour market to a large degree comprises unskilled persons. It therefore cannot be fully considered an active labour reserve, and is only slowly starting to react to growth and labour market reform measures. Further employment growth will have to be accompanied by a higher participation rate, which at about 50% of the population 15 years and over is low. In particular, female participation rates, at 48%, are very low in Hungary.

Inflation remained relatively high, but has recently started to decline rapidly. After several years of sustained disinflation, the trend broke in mid 2000. External factors accountable were high oil prices and a weak euro, while at the domestic level service and food prices were major contributing factors. A loose monetary policy framework and a depreciating foreign exchange rate, imposed by the former crawling-peg exchange rate system, were not supportive to disinflation either. The average increase of the consumer price index (CPI) for 2000 was 9.8%, and 10% according to the EU's harmonised index (HICP). Over the first six months of 2001, CPI inflation even bounced back to an average 10.4%, while core inflation, which eliminates external effects, turned out higher than headline inflation, indicating a strong impact of domestic prices. Recognising these developments, the authorities embarked on a more committed anti-inflation policy path in spring 2001. Changes to the exchange rate and monetary policies allowed the currency to appreciate significantly, thus lowering imported inflationary pressures. The National Bank formally adopted an inflation targeting monetary policy, and lowered its inflation targets for 2002 and beyond considerably. Since July, CPI inflation has started to decline rapidly, to a year-on-year rate of 8% in September.

Monetary policy was loose in 2000, but has recently started to tighten. Real interest rates were at record lows in late 2000, and mandatory reserve requirements for commercial banks were cut to half in several steps over the review period. This step injected more liquidity into the intermediation system and increased the competitiveness of the banking sector. Monetary conditions tightened after the changes in monetary and exchange rate policy. The significant exchange rate appreciation was accompanied by a rise in real interest rates, as nominal interest rate cuts did not fully follow the slowdown in inflation.

The exchange rate system was made considerably more flexible. During the past six months, the entire monetary and exchange rate set-up has been restructured. A devaluating crawling-peg exchange rate system was abolished as of 1 October 2001, after the currency's trading band had been widened to +/-15% in May 2001. These changes were introduced to be able to fight inflation more effectively. As an accompanying measure, in June 2001, short-term capital movements were fully liberalised, ahead of earlier plans, in order to enable the market to cope with the increased exchange rate risks. The Central Bank is now in a position to conduct a more active monetary policy, which it intends to do primarily through verbal interventions and interest rate adjustments, resorting only in emergency situations to direct market intervention. As an element of the new monetary policy, the NBH adopted a transparent line on the publication of its forecast and the underlying policy deliberations. In the new framework, the National Bank's credibility, measured primarily by future inflation performance, will be more crucial than ever for guiding market expectations.

The currency appreciated substantially, with some speculative fluctuations, following the changes to the exchange rate system. Catching up the effects of several years of high productivity growth, combined with speculative capital inflows upon the removal of capital controls, the forint approached the upper limit of its widened intervention band before turning more volatile at lower levels. The considerable appreciation of the nominal exchange rate will help to bring inflation down, but could put some short-term pressure on the profitability of the exporting sector and affect the current account. Nevertheless, the highly profitable exporting enterprises should be able to absorb this one-off appreciation.

2001-2002 marks the first time that Hungary has used a biannual budget framework. This could increase predictability and commitment to budgetary consolidation. On the other hand, it leaves the government a considerable degree of discretion, in the absence of a legal obligation to submit spending of extra revenue to parliament for approval. Nevertheless, the government recently chose to seek parliament's approval for an expansion of the present budget, in the form of a 'final account' law proposal.

The reduction of the budget deficit has slowed in 2000 and 2001. After some fiscal consolidation in previous years, Hungary's fiscal policy turned expansionary in 2001. This followed from higher expenditure on pensions and public wages, which had fallen far behind private sector wages throughout transition, and high public investment. With a sustained primary surplus (budget balance excluding interest payments) of 1.2% of GDP in 1999 and 2.2% in 2000, the general government budget is increasingly benefiting from declining interest payments, as the debt is gradually being paid down. Consolidated interest expenditure was just around 6% of GDP in 2000. As in 1999, the headline budget deficit in 2000 turned out at 3.7% of GDP, remaining slightly above the 3.5% target. An unbudgeted 1.5% of GDP excess revenues was spent at the end of last year or set aside for expenditure in 2001. In the 2001 budget, a similar excess revenue creating effect is in-built, based on an underestimated inflation forecast. Figures for the first six months indicate that the budget target of 3.4% of GDP (corresponding to a primary surplus of 0.4%) for 2001 can be easily met, provided no excessive spending occurs during the second half of the year. It will be crucial that the government stick to its medium-term fiscal planning in order for the present fiscal stimulus not to turn pro-cyclical, potentially compromising inflation targets and the external equilibrium.

EU fiscal accounting standards make the fiscal relaxation in 2001 more apparent, while a lack of transparency in public spending persists. In April 2001, Hungary submitted for the first time fiscal notification tables drawn up according to the 'ESA95' harmonised EU standard, which should make them more easily comparable to member states' figures. Compared with the government's traditional financial accounting method, the ESA95 general government deficit was 3.1% (instead of 3.7%) of GDP in 2000, and is projected by the authorities at 4.3% (instead of 3.4%) in 2001. A tendency to channel a growing amount of fiscal activity through off-budget funds raises concerns on the transparency and accountability of public spending. In this context, the use of the non-privatised Postabank for semi-government tasks, needs to be fully supervised.

General government debt is declining significantly. In 2000, the debt-to-GDP ratio fell to 55.7%, 4.8 percentage points lower than in 1999. The decline was more rapid than projected, mainly because high inflation pushed up nominal GDP growth above expectations.

The over-decentralised structure of local government complicates fiscal discipline. The high number of local authorities, the slow implementation of larger regional units, the lack of own resources and the absence of effective monitoring mechanisms continue to distort government accounting. In 2000, an upwards correction of the budget deficit by 0.2% was due to the local governments' increased spending of privatisation incomes which were reported late. The system adds to the delays in data availability and increases uncertainties in estimates on general government performance.

Social security contributions for employers were cut by 2%. Further amendments to the tax system comprise higher tax allowances for small enterprises and families with children. Overall, the Hungarian tax system relies heavily on consumption tax and social security contributions, while personal income tax accounts for just one third of the revenues.

The reform of the pension system has not been fully implemented. In 1997, Hungary introduced a comprehensive multi-pillar reform of the pension system, whereby existing employees were offered the choice between the state-run pay-as-you-go system (first pillar) and the private funded system (second pillar), while for new market entrants the second pillar has been made mandatory. A government-guaranteed return on investments made the second pillar, which by now covers over 2 million Hungarians, highly popular. As a result, mandatory private pension fund assets almost doubled in 2000. Due to the popularity of the second pillar, the public cost of pension reform turned out higher than projected. As a consequence, the government decided to further postpone the planned increase from 6 to 8% of its contribution to the second pillar. This could put the longer-term viability of the pension system at risk and could create a potential for future budgetary liabilities.

After a promising start, healthcare reform has been delayed. The present system is showing major shortcomings. Even after the privatisation of general practitioners' practices, the fixed cost of maintaining an inefficient over-hospitalised infrastructure remains high. The delivery of services is deteriorating as the equipment is outdated and doctors and nurses are underpaid. The budget outflow into the healthcare fund accounted for 0.8% of GDP in 2000. A rapidly ageing population aggravates the problem of an inefficient healthcare system and, without proper implementation of reform measures, poses a serious risk to public finances in the long term. At present, there is no comprehensive reform project, although in mid 2001 the government adopted a very general 10-year action plan without operational commitments.

Substantial debt relief to the state-run railway company MAV marks an important starting point for further reform. During most of the past year, implementation of the 1999 rail reform programme had been put on hold, since under the Széchenyi plan priority for public investment into the transport infrastructure has been given to motorway construction. Still, railway infrastructure modernisation continued at a modest pace. A recent decision by the government to take over more than half of the ailing railway company MAV's debt burden and to reschedule the rest over a ten year period improves the financial position of the enterprise substantially. This step needs to be supported by continuous restructuring efforts. While the impact of railway reform on the budget in the short term will be negative, a considerable budget risk can be eliminated in the long run. Starting from 2001, the modernisation of the railway network has also been addressed through ISPA funding and a long-term credit by the European Investment Bank.

Current account developments have been favourable. The current account deficit consolidated to 3.3% of GDP in 2000. A shift among the balance sheet items took place in 2000. While the trade balance deteriorated, the services' balance improved due to high service revenues, particularly in the form of tourism receipts. In 2001, the merchandise trade deficit showed a declining trend as well, leading to even lower current account deficits throughout the first eight months of the year. Energy, machinery and equipment have mainly driven strong import growth during the first six months of 2001. The current account deficit in 2000 continued to be largely covered by foreign direct investment and inter-company loans, while the country's net foreign exchange debt further decreased and international reserves increased.

The overall policy mix has contributed to macro-economic stabilisation, which should be complemented by the recent more ambitious disinflation policy. Over recent years, macroeconomic policies have been successful in reducing imbalances and establishing more sustainable, higher growth. However, this was primarily achieved through favouring external competitiveness over inflation reduction, in particular in the choice of exchange rate policy. The lack of ambition of the disinflation policy had led to entrenched high-inflation expectations. The recent changes in monetary and exchange rate policy are addressing this problem, but should be supported by a tighter fiscal policy. The present relaxation of fiscal policy is providing some compensation to the deterioration of external demand, but there is a need to restore the path of fiscal consolidation to contain the current account deficit and reduce overall vulnerability.

Although the market sets most prices, the government has maintained a too strong hold on prices in regulated sectors. Regulated prices account for 18.5% of the consumer price basket. Until early 2001, capping regulated prices for energy, drugs, housing, transport and telecoms was the government's main tool to limit inflationary developments. In the energy sector, differentiated price increases have been agreed for the household and corporate sectors. Hungary has prepared the legal preconditions for a step-by-step price liberalisation for telecoms in 2002, for electricity starting from 2003 and for gas starting from 2004. A price shock after lifting those restrictions could put inflation targets under pressure. More independent regulators might be needed to let prices adjust smoothly to market forces.

The privatisation process is ending, while no significant further progress occurred during the past year. Most of the outstanding privatisation projects, like that of the national airline MALEV, were postponed last year, due to the unfavourable stock exchange environment and further restructuring needs. Other enterprises like Postabank have been reclassified as strategic, and the state will keep control over them. Hungary has advanced the restructuring of its steel industry. Mirroring these altered challenges, the Hungarian Privatisation Agency will be dissolved. Its assets and liabilities will be transferred into two independent entities, one dealing with long-term liabilities resulting from the privatisation process, the other operating as a permanent holding for state-owned entities.

The private sector continues to develop and there are no significant barriers to market entry and exit. The private sector accounts for 80% of the economy's output. The number of registered enterprises grew by 5.7% in 2000. The implementation of bankruptcy legislation is improving.

Land markets continue to grow, but the efficiency of the agricultural land market still has to be increased. A large part of the land used by the larger individual farms and companies is leased, and some has been purchased. Lease contracts are growing in terms of duration and

sophistication, improving tenure security for the farms and consequently incentives for investment. Progressing computerisation of the land registers has improved the quality of public services in this field.

There is a high degree of legal certainty. Property rights are firmly established. Collateral collection is slowly gaining importance for the banking system. These developments support a generally favourable investment climate. However, the motorway construction programme continues to be implemented without recourse to public procurement procedures.

All parts of the financial sector are dynamically expanding, while banking continues to dominate. The expansion of banking, insurance and securities markets has been associated with a significant increase in profitability in 2000. Banks' total sector assets grew by 15.1% in real terms in 2000. Both the return on assets (at 1.4%) and the return on equity (at 13.7%) more than doubled, indicating recovery from the 1998 Russian crisis. The financial intermediation ratio, measured by total domestic credit as a percentage of GDP, increased to 53.8% in 2000. Lending to SMEs and households, albeit still low, has been increasing at a very fast pace.

The banking sector is chiefly in private hands, dominated by foreign ownership, and expanding its products. Postabank, which was originally scheduled for privatisation, was integrated as a subsidiary into the national post office, and together with OTP now forms the only major state-dominated banking conglomerate. Branch networks in the retail sector are dense, and a consolidation process is ongoing. Lending by banks was up 34% in 2000, with retail banking leading the dynamic trend. Through government credit guarantees to boost SME schemes, and subsidised mortgage programmes, attractive small-scale financing options have become available. The share of non-performing loans in banks' portfolios decreased rapidly to a level of 2.7% in 2000. However, with banks facing a more competitive environment following the opening up of capital markets and the structure of risk exposure rapidly changing, prudence remains an important issue.

The capital market is small, but developing rapidly. The Budapest Stock Exchange does not play a major role in corporate finance. The success of the new mandatory pension funds is the backbone of the sector's development, which is entering a phase of consolidation. The funds' profitability in 2000 was generally negative, at an average of minus 5.6%, which can be attributed both to the international investment climate and a generally conservative investment behaviour. The recent liberalisation of capital inflows helps the creation of more liquid hedging markets, with a range of new products emerging due to the need for the exporting sector to hedge its foreign exchange exposure.

The insurance sector is growing dynamically, and accounts for roughly 6% of households' financial assets. Foreign participation is close to 90%. In 2000, revenues from the life insurance sector increased by 48%, while non-life related revenues rose 16%. Profits more than doubled.

The financial system in Hungary is stable and relatively well regulated and supervised. In August 2000, the NBH started the publication of bi-annual 'Reports on Financial Stability', which provide monitoring tools of high quality and sophistication, and reflect a well-developed expertise on financial stability issues among the authorities. The consolidated Hungarian Financial Supervisory Authority (HFSA) has been established for a couple of years, improving

the strength, quality and effectiveness of the supervisory framework. However, the agency's regulating powers are still limited, although it fulfils some important elements of independence, like the appointment and dismissal of its president by Parliament. A government proposal to also grant the HFSA regulatory power failed to receive the necessary quorum in parliament. A modification to the Banking Act as of 1 January 2001 enhanced supervision of financial conglomerates – important in the context of the ongoing concentration process in the Hungarian financial sector – and imposed higher transparency on credit institutions and investment service providers.

The Capacity to Cope with Competitive Pressure and Market Forces within the Union

The ability to fulfil this criterion depends on the existence of market economy and a stable macroeconomic framework, allowing economic agents to make decisions in a climate of predictability. It also requires a sufficient amount of human and physical capital, including infrastructure. State enterprises need to be restructured and all enterprises need to invest to improve their efficiency. Furthermore, the more access enterprises have to outside finance and the more successful they are at restructuring and innovating, the greater will be their capacity to adapt. Overall, an economy will be better able to take on the obligations of membership the higher the degree of economic integration it achieves with the Union before accession. Both the volume and the range of products traded with EU Member States provide evidence of this.

Hungary is a functioning market economy which has achieved the necessary macroeconomic stability and has created the required institutional framework. Market participants can take their decisions in a climate of stability and predictability. Market allocation works well and the basis for sustained growth based on private sector initiative is in place.

Availability of skilled labour at moderate cost, productive restructured enterprises and an improving infrastructure are the backbone of the country's economic success. Hungary is gradually becoming a production centre for relatively capital-intensive, technologically sophisticated goods and services dependent on skilled management and labour. The high percentage of well-educated workers in the economy meets this demand. While over 60 percent of the 14-17 year old attend vocational schools on a full-time basis, 17.5 percent of the 18-22 year old population are enrolled in colleges and universities. Moreover, the secondary school enrolment ratio has substantially improved, from 18% of 15-18 year olds in 1989 to 27.2% in 1998. Access to tertiary education has also risen strongly, from 12.1% of 19-24 olds in 1989 to 27.4% in 1998.

Some regional labour markets are becoming increasingly tight. With shortages appearing in the Budapest area and along the Western border, the government has made labour market reform a priority. Mobility across the country typically is very low and needs to increase. Lately, rising employment figures in the poorer regions suggest that the high growth, gradual regional spreading of FDI, and the active labour market policy pursued by the government are starting to produce an effect. The government has reduced the entitlements for unemployment benefits in order to provide greater incentives for the re-integration of long-term unemployed into the labour market.

Implementation of the 2001-2006 Széchenyi plan for economic reform is progressing. Over a thousand projects have been granted during the first half of 2001. The budgetary

resources earmarked for this economic development programme which bundles and focuses existing programmes and combines them with new targets, is roughly 2% of GDP in 2001. Another 2.5% of GDP have been appropriated in the framework of an additional 'Szechenyi plus' package, for spending in 2002. The first results are becoming visible with increasing registration of new housing. Grants for tourism projects are also in high demand. However, while interest in the funds is livelier in the already industrialised regions, it is proving difficult to stimulate activity in the more depressed parts of the country. Overall, actual spending in 2001 seems to turn out lower than projected. The economy's overall investment share remained at a growth-promoting level of about 24% of GDP in 2000.

Substantial inflows of foreign direct investment continue beyond privatisation. At 2.9% of GDP, the level of FDI has remained robust, although it is decreasing. Greenfield investment dominates, and the trend from low value-added to high-tech investment continues, providing a constant inflow of innovation. A number of substantial investment decisions by multinational companies have been announced during the past twelve months, indicating a continuation of the country's attractiveness to foreign capital. Preferred FDI targets continue to be the rapidly growing central and western regions, while the eastern regions are only slowly becoming attractive to foreign investors, also in line with the gradual improvement of transport and telecommunication infrastructure.

Various state aid schemes exist. Some of the main state aids are given in the form of tax reliefs, often in favour of large foreign investors. There are concerns about the transparency of state aid granted by local authorities and by the para-fiscal Hungarian Development Bank, but new already adopted legislation will address the situation as of January 2002.

A clear differentiation has emerged in Hungary between the large foreign-owned companies and primarily domestic SMEs. The differentiation concerns sector specialisation, ownership structures and regional distribution alike. On the one hand, the larger part of GDP and exports is generated by a few large companies, which are typically in foreign ownership and often operate under privileged conditions in the so-called 'free zones'. On the other hand, employment is primarily provided by a very large number of micro-, small and medium-sized enterprises, typically in sole proprietorship and operating on the Hungarian market. A reduction of the SMEs' disadvantages vis-à-vis large companies is highlighted as a priority under the Széchenyi Plan. Along with a number of other measures, the 'bridging' between domestic SMEs and large companies through multilevel subcontracting networks, supported by government incentives, is showing first promising results.

The small and medium-size enterprise sector continues to develop favourably. SMEs account for 45% of GDP and 69% of the workforce. Sectors dominated by SMEs are trade, the processing and building industries, communal services, tourism, transport and support services in the real estate and IT businesses. As the development of retail banking structures has progressed, credit availability for SMEs has continued to expand, at a faster pace than credit for larger enterprises. Improvements in the system to secure collateral and preferential loans and guarantee schemes for SMEs backed by the government have supported the positive trend. Tax credits for micro-enterprises that were introduced in 2000, along with a reduction of the administrative burden, have contributed to enhanced financial stability for the smallest enterprises. Certain sectors that are dominated by SMEs, namely the food, textile and tourism industries, have recently suffered adverse effects from the rapid currency appreciation. In July

2001, the government adopted a package of measures to support SMEs through interest rate subsidies and standardised currency risk hedging products.

The growing openness of the Hungarian economy was emphasised by a sharp increase of exports and imports to 129% of GDP in 2000. At an annual 39%, exports to CEFTA countries grew strongest, compared to a 26% increase in trade with developed countries, and of 24% with the EU. In addition, exports to CIS countries picked up again. The overall share of exports to the EU remained stable at 75%, while the share of EU imports dropped to 58%. As in recent years, machinery and transport equipment accounted for the lion's share of 60% in total exports. The most dynamic growth was registered in electric engineering and instruments, with the relevant export share increasing to nearly 40% of manufacturing exports.

The economy as a whole continues to be highly competitive. In 2000, productivity grew by 4.2%. The development of price-based real exchange rates differed significantly from the cost- and profit-based indices. In 2000 the CPI based real effective exchange rate appreciated only by 1% compared to 1999, while the manufacturing price based real exchange rate appreciated more than 5%. Over the same period, the unit labour cost based real exchange rate in the manufacturing industry depreciated by 0.5%. Thus, despite rising wages and prices, competitiveness as measured by relative unit labour costs in manufacturing kept improving. However, in the short term, the currency appreciation in 2001 is affecting export price competitiveness, since lower domestic inflation will take some time to be established and to translate into export prices.

2.4. General evaluation¹⁵

Hungary is a functioning market economy. Provided that it fully maintains and implements its reform programme in a consistent manner, it should be able to cope with the competitive pressure and market forces within the Union in the near term.

The macroeconomic situation continues to be sound, with high GDP growth underpinned by a rising investment share, further declining unemployment and favourable current account development. Railway restructuring continued through a major bailout and debt restructuring. It has adopted a more appropriate monetary and exchange rate framework, which is contributing to lower inflation.

However, fiscal policy has become expansionary in 2001. Together with recent non-transparent fiscal practices, the uncertainty over the further reform of the pension system and the delays in the reform of the health care system have raised some concern about the continuation of consolidation and the medium-term sustainability of public finances. The authorities will need to maintain fiscal discipline to ensure that fiscal policy supports the new monetary policy framework and the external balance. This would contribute to lower inflation. The health care reform should be undertaken swiftly.

¹⁵ See "Making a success of enlargement: Strategy Paper and Report of the European Commission on the progress towards accession by each of the candidate countries", COM (2001) 700.

3. Ability to assume the obligations of membership

Introduction

This section aims to update the Commission's 2000 Regular Report on Hungary's ability to assume the obligations of membership - that is, the legal and institutional framework, known as the *acquis*, by means of which the Union implements its objectives. Alongside an evaluation of relevant developments since the 2000 Regular Report, this section seeks to provide an overall assessment of Hungary's ability to assume the obligations of membership, and of what remains to be done. This section is structured to follow the list of twenty-nine negotiating chapters, and incorporates an assessment of Hungary's administrative capacity to implement the *acquis* in its various aspects. Hungary's progress in translating the *acquis* into its official language is assessed in a separate section.

The European Council in Madrid in December 1995 referred to the need to create the conditions for the gradual, harmonious integration of the candidates, particularly through the adjustment of their administrative structures. Taking up this theme, in Agenda 2000 the Commission underlined the importance of effectively incorporating Community legislation into national legislation, and the even greater importance of implementing it properly in the field, via the appropriate administrative and judicial structures. This is an essential pre-condition for creating the mutual trust indispensable for future membership.

The European Council in Santa Maria da Feira and in Gothenburg in June 2000 and June 2001 respectively recalled the vital importance of the applicant countries' capacity to implement and enforce the *acquis*, and added that this required important efforts by the applicants in strengthening and reforming their administrative and judicial structures. Building on the assessment of Hungary's administrative capacity provided in the 2000 Regular Report, the present Report seeks to add further depth and detail, focusing on the main administrative structures which are required for implementing the *acquis* in its various aspects.

In the 2000 Regular Report, the Commission concluded that :

"Hungary's continued to make progress in aligning and implementing the *acquis* in most sectors thereby reaching a good level of preparation for membership. This process was in general accompanied by satisfactory institution building measures.

Over the reference period good progress could be noted concerning *internal market legislation*, in particular as regards harmonised and "new approach" product legislation, insurance and accounting law and the transparency and alignment of certain State aid schemes. Continued efforts are still needed especially for developing adequate market surveillance and for aligning state aid granted in the form of tax benefits. While the basic structures of the *acquis* related to VAT and excise duty are already in place, further efforts are required in the area of *taxation* with regard to reduced rates, exemptions and direct taxation. The Central Liaison Office, and co-operation and mutual assistance with tax administrations in Member states, will also need to be strengthened. Considerable progress was made in the area of *customs*, and the new law on customs reflects the Community Customs Code to a large extent. In the field of *telecommunications*, where the market is in principle open to competition, Hungary's needs to align further with the terms and conditions of universal service.

In the area of *agriculture* the basic structures of the *acquis* are in place, but the administrative structures required for the implementation of the CAP still need to be put into place. Alignment will need to be speeded up especially in the veterinary and phytosanitary sub-sectors.

In the area of *environment* only little progress in terms of alignment was made over the last year, and the administrative capacity of the Ministry of Environment needs improvement due to the lack of qualified staff and the wide distribution of responsibilities related to environmental issues.

Alignment needs to be speeded up in the area of *transport*, in particular in the road and air sub-sectors, and new institutions will have to be set up in order to enforce the *acquis* adequately. In the *energy* sector, the main principles of the internal energy market were adopted, but will need to be implemented, and the Hungarian Energy Office will need to be further strengthened in order to be able to discharge its tasks in the future internal energy market.

Hungary made significant progress in developing the necessary structures for the implementation of *regional policy* after accession, although the structures in the regions still appear rather weak to guarantee efficient programming and decision making. In the area of *financial control* the internal and external control bodies, which were already set up some time ago, will need to be strengthened in order to provide the basis for sound financial management and control of EU funds in the context of decentralisation towards the regional level. As to *financial and budgetary provisions*, further efforts are needed in order to meet Community requirements with regard to co-financing and multi-annual programming.

On the other hand, good progress was made in the area of *social policy and employment* in terms of legal transposition, although considerable work remains to be done with respect to the implementation of the *acquis* on health and safety where implementation is to occur gradually, but before accession. There is also a need to exploit better the new structures for social dialogue. In the area of *economic and monetary union* the main outstanding issue relates to the further consolidation of the independence of the National Bank. As to *industrial policy*, the situation in respect of the restructuring of the Hungarian steel industry is still unsatisfactory and the steel restructuring plan adopted by Hungary will need to be further revised. In the area of *Justice and Home Affairs*, progress was registered mainly in the fields of visa policy, border management, migration and asylum.

Hungary continued to make steady progress in building up its administrative capacity to apply the *acquis* in most areas. Further progress was made towards public administration reform, and continued emphasis was placed on training in EU matters throughout the administration and the judiciary. Most of the key institutions needed for participation in the internal market are in place. Nonetheless, administrative and judicial capacity still needs to be strengthened in specific areas such as state aid control, market surveillance, transport, the environment, veterinary and plant health.

Hungary has satisfactorily addressed most of its short-term Accession Partnership priorities with the exception of agriculture, the environment, certain elements related to the internal market, industry policy and economic and monetary union. Hungary has already started to implement a number of medium-term priorities.”

3.1. The chapters of the *acquis*

As indicated, the review of Hungary's ability to assume the obligations of membership that is below has been structured in accordance with the list of twenty-nine negotiating chapters. Accordingly, this section opens with an assessment of progress related to the so-called "four freedoms", the cornerstones of the internal market, and continues with a systematic review of progress on each of the chapters, to cover the *acquis* in all its various aspects, including sectoral policies, economic and fiscal affairs, regional policy, environment, justice and home affairs, external policies, and financial questions.

Chapter 1: Free movement of goods

Further steady progress was made in the field of free movement of goods.

In the area of **horizontal and procedural measures**, Hungary continued the rapid adoption of European standards as Hungarian national standards. By May 2001, the Hungarian Standards Institution had implemented 10564 European standards as national standards, or 84% of all European standards. They include 89% of the European standards harmonised to the New Approach Directives. The Hungarian Standards Institute presented an application for full membership of CEN and CENELEC in January 2001.

Following good progress noted in previous years as regards **sector specific legislation**, Hungary has continued its alignment. In the areas covered by *New Approach Directives*, the legislation on telecommunications terminal equipment and pressure vessels was aligned. As regards sectors covered by the *Old Approach Directives*, some further pieces of legislation were adopted in the field of aerosols, fertilisers, food additives, coffee and chicory extracts, dangerous chemicals, detergents, and legal metrology. The *acquis* on the registration and marketing authorisation of medicines for human use was also transposed, but the provisions on the protection of test data of medicines will only enter into force in 2003.

Further progress was made in institutional development. The main body responsible in the area of market surveillance is the General Inspectorate for Consumer Protection (GICP), which is under the responsibility of the Ministry of Economic Affairs. Numerous other bodies also perform market surveillance, depending on the sector concerned; a number of co-operation agreements have been signed between the GICP and the other bodies, as well as with the customs service. In sectors where alignment has been completed, further market surveillance bodies and bodies for testing, inspecting and certifying the conformity of products have been designated by the responsible ministries. The technical equipment of some testing and certification bodies has been developed. Furthermore, Hungary decided to set up a Food Safety Agency, but its functions have not yet been specified.

No new developments are to be reported with regard to **non-harmonised sectors**.

In the area of **public procurement**, no further legal developments have taken place. Hungary has continued not to apply public procurement rules to motorway construction. In 2000, the total number of public procurement procedures declined somewhat to 3710 in 2000, but the total value increased by one-fifth compared to 1999 to HUF 524 billion (around € 2 billion). The proportion of open procedures rose to 76 % in value terms in 2000, and about 10% of the tenders was won by bidders with headquarters abroad, mostly in the EU.

Overall assessment

Hungary is already well advanced in this area.

As regards horizontal and procedural measures, the New and Global Approach is generally well established in Hungary. The infrastructure required for legislation, standardisation, accreditation and certification is in place. The Ministry of Economic Affairs has a notification and information centre dealing with technical regulations. The Hungarian Institute for Standardisation is a full member of the European Telecommunications Standards Institute (ETSI), the International Electrotechnical Commission (IEC) and the International Standards Organisation (ISO). Full membership of CEN and CENELEC will need to be achieved. The Hungarian Accreditation Board is a full member of EA, the European Co-operation for Accreditation. The organisation and procedures of the Hungarian Institute for Standardisation, the Hungarian Accreditation Board and the Hungarian National Office of Measurements broadly appear to meet the needs of the *acquis*. As regards safety checks on products, efforts need to continue to strengthen customs and market surveillance infrastructure and in particular to ensure effective administrative co-operation between competent regulatory and surveillance authorities and to ensure the full implementation of the Central Information System on Market Surveillance. At present, no safety control takes place at the border. The capacity of some of the testing and certification bodies should be further enhanced and their independence from the regulator should be ensured.

A large part of the sector-specific *acquis* is also in place. With regard to the *New Approach Directives*, work remains to be done on construction products, lifts and explosives for civil use. The outstanding legislative issues under the *Old Approach* relate mainly to cosmetics, metrology, dangerous chemical substances, drug precursors, pharmaceuticals, wood and residue limits of veterinary medicinal products in foodstuffs. The protection of test data of pharmaceuticals should be introduced as a matter of urgency. The *acquis* on the provision of information on technical standards and regulations must also be transposed before accession. Where alignment is completed, market operators should be more widely informed about their new tasks and responsibilities, and the previous pre-market control and mandatory standards should be clearly abandoned. With regard to food safety, Hungary lacks of a clear plan on how to rationalise activities across ministries, although each of the single ministries have plans for better internal co-ordination among their own services. Hungary needs to continue to upgrade the relevant structures for inspection and analysis of foodstuffs, and promote the introduction of Hazard Analysis and Critical Control Points (HACCP) principles across the entire food chain (*see also chapter 7 – Agriculture*). Also, sufficient administrative capacity needs to be built up in the field of marketing authorisations for medicines.

In the non-harmonised sectors, the internal screening by the Ministry of Economic Affairs of measures hindering the movement of goods should be continued and should lead to the elimination of incompatible provisions. The principle of mutual recognition will have to be well established by accession. The State Secretariat for European Integration in the Ministry of Foreign Affairs will be responsible for notifying national measures derogating from the principle of free movement. The *acquis* on the return of unlawfully exported cultural goods will be implemented by the Cultural Heritage Protection Office. While much of the legislation is in place, further institution building is necessary, in particular the creation of a database of cultural goods. The *acquis* on firearms has not yet been transposed.

The alignment of legislation on public procurement is well advanced, but further efforts are necessary especially with regard to value thresholds, time limits, exemptions, evaluation criteria, the treatment of utilities, and the abolition of national preference. Some rules are presently stricter than the *acquis* allows; however, except for certain gas and water sectors, utilities are still not covered by the procurement rules. In the area of enforcement and remedies, the rules for initiating proceedings, for utilities and for damages need to be further aligned. The further legislative alignment should not await the adoption of new *acquis*.

Hungary has already put in place the necessary bodies to implement this part of the *acquis*. Public procurement policy is developed by the 19-member Public Procurement Council. It consists of interested central government bodies, contracting agencies and bidders. The Council is legally independent from the Government and answers to Parliament, to which it is required to report annually. The Council oversees the application of public procurement rules and may initiate amendments to the relevant legislation. It provides information and publishes the notices for procurement procedures. It has developed a substantial training programme. The monitoring and review of procurement procedures is carried out by the Public Procurement Arbitration Committee. This law enforcement body can be considered to be a semi-judicial body as required by the *acquis*. The number of arbitration Commissioners was increased to 18 to cope with the growing workload related to complaints. A total of 700 cases were submitted to the Public Procurement Arbitration Committee for legal remedy in 2000, i.e. about 20% of all procedures, a rising trend which continued in 2001. Infringements were found in 277 cases. A particular effort is needed to ensure transparency of public procurement at all levels, including at lower levels of government, and in all sectors, in particular as regards major public infrastructure works such as road construction. The *acquis* does not allow for the circumvention of basic procurement principles, including the obligation to tender, by the manner in which contracts are structured or by delegating the implementation of public works to nominally private but state-controlled agencies. Further work is expected to provide both the procurement agencies and the supervisory bodies with sufficient staff and modern information systems.

Chapter 2: Free movement of persons

The current reporting period has seen further alignment with Community provisions, and preparations for complete alignment, as well as for the establishment of the required administrative structures, have continued to take place. In the area of **mutual recognition of professional qualifications** no particular developments are to be reported.

Some progress can be reported on **citizens' rights**. With the adoption in May 2001 of the law on entry, stay in Hungary and immigration of foreigners, Hungary has made substantial progress in aligning with provisions on residence rights. Legislation on student rights needs to be further aligned. No particular developments are to be reported in the area of voting rights. It is recalled that the Constitution will need to be amended.

Limited developments are to be reported in the area of **free movement of workers**. Preparation has continued to facilitate Hungary's participation in European Employment Services (EURES).

Hungary has continued to strengthen bilateral relations with a view to the future **co-ordination of social security** matters and development of institutional capacity has accelerated. A

bilateral agreement with Austria, covering health insurance, pensions, unemployment benefits and family allowances, entered into force in January 2001.

Overall assessment

The situation in Hungary in relation to free movement continues to be satisfactory, and, although efforts are still required, legislative and other work is generally being carried out in a timely manner. These efforts will need to be maintained and institutional capacity strengthened in some areas.

Hungary was already largely aligned with the *acquis* in the area of mutual recognition of professional qualifications. Further legislative work is however necessary to achieve full alignment and to provide for the establishment of the necessary administrative bodies. Outstanding issues relate in particular to alignment with EC legislation on lawyers and pharmacists. The Director General of the Equivalence and Information Centre of the Ministry of Education has been appointed as national co-ordinator, as required under the general systems directives, and is responsible for co-ordinating the activities of the competent authorities. Designation of the latter should now take place without delay. While further preparatory work has taken place, these efforts will need to continue in order to ensure full alignment by accession. It will need to be ensured that, by accession, there are no provisions in Hungarian legislation which contradict Community rules, in particular with respect to nationality, residence or language requirements. Legislation on mutual recognition needs to be monitored to ensure that it distinguishes between academic and professional recognition and includes simpler procedures to allow the provision of services. With respect to professional qualifications obtained before harmonisation, Hungary should introduce measures to ensure that all its professionals can, as of accession, meet the requirements laid down by the directives.

With the adoption of legislation on residence rights, Hungary is now largely aligned with the *acquis* on citizens' rights. Preparations should however continue so as to align with the provisions on voting rights.

In the area of the free movement of workers, legislation is only partially aligned and efforts are required to ensure complete alignment by accession, including also the social and cultural integration of migrant workers and their families.

As regards future participation in European Employment Services (EURES), efforts should be continued, especially with regard to language training.

With a view to the future co-ordination of social security systems, further work to develop the necessary administrative structures is needed. Institutional capacity needs to continue to be strengthened so as to enable Hungary to apply the *acquis* on co-ordination of social security. Agreements such as that signed with Austria on social security will facilitate Hungary's compliance with the regulations as of accession, as they normally rely on the same principles as the social security co-ordination regulations and this familiarises the administration with the procedures.

Chapter 3: Freedom to provide services

Some progress has been made since last year's Regular Report, in particular in the field of banking and insurance.

As regards the **right of establishment and freedom to provide services**, the rules on self-employed commercial agents have been aligned with the *acquis*.

In the field of **financial services**, new legislation on the credit institutions passed at the end of 2000 has achieved quite a number of further alignments in the *banking sector*, with the exception of those parts of the *acquis*, which can only be applied by Member States. In particular, licensing procedures and criteria, the own funds definition, the solvency ratio and capital adequacy rules have been addressed. Consolidation and large exposure rules, as well as the post-BCCI directive, have also been addressed.

In the *insurance sector*, a series of implementing legislative acts on reporting, intermediaries, technical reserves and other issues were adopted, thus completing the framework set out in the insurance law of 2000. The system of compulsory third-party motor vehicle liability insurance has been revised and liberalised.

No particular development can be reported with respect to the *securities markets*.

No further developments are to be reported with regard to the **movement and protection of personal data**.

The alignment of the Hungarian legislation with the **information society** *acquis* continued with the adoption of a law on electronic signatures in May 2001.

Overall assessment

Hungary has already achieved a substantial degree of alignment with the *acquis*.

Whereas by law legal persons and self-employed persons from the EU enjoy the basic right of *establishment* based on national treatment, the *freedom to provide cross-border services* does not yet exist. The respective rules to facilitate effective access of non-nationals to industrial, trade, tourism and agricultural activities, *inter alia* through the recognition of qualifications, still need to be aligned. Restrictions on the acquisition of real estate also hamper effective access.

On the other hand, Hungary has already achieved a substantial degree of alignment in *financial services*. Of course, it is only upon accession that the necessary rules providing for internal market conditions with regard to branching and the free provision of services can take effect. In particular with regard to securities, more work will be needed before Hungary can be regarded as fully complying with the *acquis*; contractual netting and investor compensation schemes should be addressed. The accounting standards meet EC and international requirements and international co-operation is underway with current efforts to conclude memoranda of understanding with the most relevant partner countries. The present regime for the setting up of foreign bank branches in Hungary is rather rigid and will have to be modified with a view to accession. In the insurance sector, it is also still necessary to review the regime governing

composite (life and non-life) insurance businesses, as well as that concerning the investment of assets covering mathematical reserves and the guarantee fund.

The Hungarian Financial Supervisory Authority is responsible for the financial services sector. It has its own separate budget and is legally independent. It is guided by the Basle Core Principles for Banking Supervision. It has a duty to protect the interest of clients of financial institutions, to enhance transparency of the markets and to ensure maintenance of fair and regulated market competition through permanent surveillance of the prudent operation of organisations and entities engaged in financial services in the largest sense. This includes not only the classical sectors of banking, securities and insurance, but also depositories, private pension funds and the whole commodities market. However, it has no regulatory power itself, as the adoption of prudential rules remains the prerogative of the Government and the Minister of Finance. The Supervisory Authority is managed by a President who is appointed by Parliament upon the Prime Minister's proposal. The Authority has a staff of around 440. It carries out on-site inspections of every bank, insurance company and investment firm once every two years. As a result of these inspections, 36 licences were withdrawn and 44 licences suspended in 2000. Intensive training programmes for the staff at the Supervisory Authority were held in 2000 and 2001. The Authority publishes an annual activity report in the official Journal of the Ministry of Finance.

Hungary appears to have the necessary supervisory institutions in place, but further efforts are needed as regards the practice of consolidated supervision, especially within groups of connected institutions and with regard to the aggregation of accounts within conglomerates. The further development of the supervisory system will focus on supervision on a consolidated basis, monitoring and early warning systems, and establishing effective co-operation with supervisory authorities of the Member States.

Further work is required to align with rules related to *information society services*, in particular on the provision of information in the field of technical standards and regulations, the legal protection of services on conditional access and e-commerce, as well as to adjust the legislation on electronic signatures. The variety of legally different types of electronic signatures and the requirement of prior authorisation for providers of electronic signature-related services is not yet in line with the *acquis*. The legislation on the *protection and movement of personal data* requires fine-tuning. The Parliamentary Commissioner for Data Protection is a fully independent ombudsman elected by Parliament for a term of six years and supported by a staff of 20 trained officials. The Commissioner is responsible for the monitoring of the data protection regulations and for investigating complaints, as well as for ensuring the maintenance of a data protection register and for issuing recommendations and opinions, often at the request of data controllers themselves. The ombudsman can investigate infringements of data protection rules and initiate criminal proceedings before the competent authorities, but he is not empowered to directly order the authorities to delete data which has been collected or processed illegally; he may only invite them to do so. In the final resort, he can bring issues to the attention of Parliament. His recommendations are generally respected and overall the enforcement capacity of the administration is already quite satisfactory. However, the position of the Parliamentary Commissioner for Data Protection is currently not filled.

Chapter 4: Free movement of capital

Good overall progress has been made in this field.

In the area of **capital movements and payments**, the liberalisation of short-term capital flows was accelerated in connection with the widening of the exchange rate band of the Hungarian forint. Most restrictions on foreign exchange operations and transactions were lifted, thereby establishing the conditions for full convertibility of the national currency.

No further progress is to be reported as regards the *acquis* on **payment systems**.

As for the *acquis* on **money laundering**, new legislation adopted at the end of 2000 prohibits the opening of anonymous savings books and the deposit of additional funds into existing ones, and requires customer identification for withdrawals. However, these new provisions will only enter into force upon Hungary's accession. While the stock of anonymous savings deposits has decreased during the latest years the remaining deposits still amount to approximately € 600 million. As a result of the present situation, Hungary was added to the list of non-co-operative countries and territories in June 2001 by the Financial Action Task Force (FATF), an international body set up to promote the fight against anti-money laundering. In October 2001, the Government submitted a bill to Parliament, which aims at meeting the FATF recommendations. If adopted, this bill would considerably strengthen the fight against money laundering by accelerating the conversion of anonymous savings books into registered accounts. It would also tighten regulations and identification and reporting requirements with respect to beneficial ownership, funds handled by non-financial institutions such as certain liberal professions, the transfer of cash across the border and currency exchange.

Overall assessment

Hungary's legislation is already aligned to a large extent with the *acquis*.

Hungary is already very advanced in the liberalisation of *capital movements*, and only a limited number of specific measures remain to be taken. Certain restrictions on direct investment still exist, institutional investors still face restrictions on investment in foreign assets and the state maintains golden shares in a limited number of privatised companies.

Partial harmonisation has been achieved in the area of *payment systems*. Full alignment needs to be achieved, and a complaints and redress procedure for the settlement of disputes on cross-border credit transfers needs to be introduced.

Hungary's legislation on *money laundering* already provides a good basis for alignment, provided that the pending legislation on money laundering is adopted. The phasing out of anonymous savings books should be brought forward. A financial intelligence unit with 10 staff members has been operating within the Organised Crime Directorate of the National Police since 1994. The unit receives approximately 1,000 suspicious transaction reports per year. So far, 9 cases have been prosecuted. The financial intelligence unit needs to be strengthened further. Hungary needs to ensure compliance with the recommendations of the Financial Action Task Force and should seek its removal from the FATF's list of non-co-operative countries as soon as possible.

Chapter 5: Company law

Hungary has continued to progress steadily, notably in building up its administrative capacity.

In the area of **company law** as such, no new developments are to be reported.

Some progress was made in the field of **industrial and intellectual property rights** with the adoption of legislation on the protection of designs in June 2001.

Overall assessment

Legal alignment is already quite advanced, and administrative capacity is being built up.

In the field of *company law* a significant degree of alignment has been achieved. The few outstanding issues are mainly of a technical nature. Provisions on economic interest groupings also need to be introduced.

The 19 county Courts and the capital Court of Registration are responsible for the registration of companies and partnerships. The register can be consulted on payment of a fee, and the Courts have the task of enforcing company reporting requirements. The Hungarian Chamber of Auditors established in 1997 is responsible for the accreditation of auditors. Approximately 7,000 auditors and auditing firms are registered. Hungary does not have an accounting standards body, and has yet to begin introducing national accounting standards.

In the field of *industrial and intellectual property rights*, the Hungarian legislation is largely in line with the *acquis*. Some further efforts are required to introduce supplementary protection of patented pharmaceutical and plant protection products. Alignment with the *acquis* on databases, copyright in the information society and resale right also needs to be completed. Also, Hungary will need to fully implement the *acquis* on the legal protection of biotechnological inventions. Hungary has ratified the two 1996 WIPO treaties on copyright and on performances and phonograms.

The Hungarian Patent Office is the single government institution responsible for the protection of both intellectual and industrial property rights. The Office is self-financing, and has over 250 staff. There are six collective management organisations administering copyrights and related rights. These are associations formed by a representative number of rightholders. The Budapest Metropolitan Court has exclusive competence to hear most of the industrial property cases, whereas intellectual property cases are also handled in county courts. Since 1997, the courts have imposed over 200 provisional measures in trademark infringement cases and customs has taken border measures against goods in more than 200 cases, leading to over 100 court cases. The number of pirated and counterfeited goods has decreased, but remains at a high level. Actual convictions in industrial and intellectual property cases are not numerous and the penalties imposed have not been severe.

The Hungarian Patent Office and the collective management societies are acknowledged to have good administrative capacity, but the specific training of bodies in charge of enforcement –police, customs, prosecutors and judges– should be continued. Progress has been made in increasing the efficiency with which intellectual and industrial property rights are enforced, but further efforts are needed to ensure rapid and deterrent legal action against offences and to ensure efficient border control measures. Hungary will join the European Patent Organisation as of July 2002.

Hungary is preparing to apply the new Regulation replacing the Brussels Convention as of accession.

Chapter 6: Competition policy

Since last year's Regular Report, Hungary has continued to make progress.

In the field of **anti-trust**, a number of further substantive and procedural adjustments were made to the basic Law on the Prohibition of Unfair and Restrictive Market Practices.

In the area of **state aid**, an amendment to the Law on Public Finance introduced a general prohibition on granting state aid, including for local governments, while exemptions to the general prohibition are detailed in an implementing decree. A regional aid map has also been included in the legislation. The amended state aid control system enters into force on 1 January 2002. An amendment to the Law on Corporate Tax and Dividends provides for a single tax benefit scheme as from accession, under which the taxpayer may claim new tax benefits solely with the permission of the Government. Since the beginning of 2001, local governments are obliged to report their total state aid as a separate item in their annual report, and companies now also have to report aid falling under the scope of the Europe Agreement in their annual accounts.

The *State Aid Monitoring Office*, working independently in the Ministry of Finance, is the main administrative body. Its staff has increased slightly; it currently employs eight persons. The enforcement record has developed and 150 opinions were issued in 2000. State aid reports have been submitted for the years up until 1998 and the quality is good. A state aid inventory has been prepared covering aid measures in operation in Hungary, except at local level.

Overall assessment

Hungary is well advanced in the field of competition policy, also as regards administrative capacity, but further alignment work is still needed in specific areas.

Hungary's *anti-trust* legislation is already to a large extent aligned with the *acquis* and contains the main principles of the rules on restrictive agreements, abuse of dominant position and merger control. A number of block exemptions regarding restrictive agreements have been adopted, but further alignment is still necessary, especially in view of recent developments in the *acquis*.

Investigations are conducted by the legally and financially independent Office of Economic Competition. Its staff of over 100 persons prepares the decisions of the Competition Council, which consists of seven members and a president. In 2000, 144 competition decisions were taken, comprising 11 on horizontal agreements, 7 on vertical agreements, 55 on abuse cases and 71 on mergers. The Office of Economic Competition appears to have a reasonably good enforcement record. The main challenge is now to ensure that priority is given to cases that concern the most serious distortions of competition and that sanctions have the necessary deterrent effect. Investments should continue in training (including the judiciary) and IT facilities.

The new *state aid* control legislation represents a considerable strengthening of the regime but it is still not fully comprehensive. In particular, important fiscal aid schemes at national and local level are not yet covered by state aid control. An immediate alignment is necessary of these fiscal aid schemes, under which some benefits last until 2011. Hungary needs to ensure that tax benefits, including aid to the so-called sensitive sectors, are compatible with the *acquis*. Also,

some adaptations are needed to the regional aid map to ensure an appropriate differentiation of maximum aid intensities in assisted areas.

Although the State Aid Monitoring Office does not take binding decisions, its assessments appear in practice to have been respected. Contested assessments are referred to the Government for decision. The Office has a good enforcement record as to quality, but is insufficient in scope, as it does not extend to the alignment of fiscal aid schemes. The Office should be given sufficient powers and resources to ensure a fully comprehensive state aid control.

Chapter 7: Agriculture

In 2000 the share of agricultural gross value added was 3.9% of total production¹⁶, compared to 4.8% in 1999. Agriculture and forestry employed 6.5% of the working population, compared to 7.1% in 1999¹⁷.

EC imports of agricultural products originating in Hungary increased by 8% to € 1183 million in 2000 while EC exports to Hungary increased by 25% to € 605 million. The agricultural trade balance in favour of Hungary amounted to € 578 million compared to € 618 million in 2000¹⁸.

The most important product groups in terms of EC imports from Hungary were meat, oilseeds and vegetables. As far as EC exports to Hungary are concerned, the most important sectors were meat, prepared feed, fruit, cereal and cocoa preparations.

Subsidies for the agricultural markets, for production, for investment, and for rural development measures have considerably increased. The number of registered farmers or agricultural producers has increased. Registration is a pre-condition to qualify for support.

No progress can be reported with regard to the legislation on land consolidation and the National Land Fund.

Horizontal issues

As regards the implementation of measures related to *the European Agricultural Guidance and Guarantee Fund (EAGGF)*, the Hungarian government made efforts to develop the Agricultural Intervention Centre (AIK) into the paying agency in charge of managing the EAGGF Guarantee payments. The AIK will also play a crucial role in the management of the major common market organisations.

As part of the preparations to establish the Integrated Administration and Control System (IACS), the concept to develop an integrated IT system was established in January 2001.

¹⁶ Estimated.

¹⁷ Eurostat Labour Force Survey definitions (LFS). Agricultural employment is defined in LFS terms as economically active persons who gain a significant part of their income from agriculture.

¹⁸ Source of trade figures: Uruguay Round definition of agricultural products, figures from EUROSTAT COMEXT (see U.E. 12/15: Commerce des Produits Agricoles 1988-2000, 1 Partie D.G. AGRI / A.2 Analyses quantitatives, prévisions, statistiques, études, 2001, page 10-57 and 86-89).

However, implementation has not yet started. A national aerial survey was carried out in 2000 and the aerial photographs have been digitalised. Measures were taken to complete the identification and registration of pigs by 2001, whilst all cattle have already been identified and registered.

The preparations for Hungary's participation in the Farm Accountancy Data Network (FADN) are satisfactory: the coverage of the network reached 90% in 2000 and the preparations for publishing the FADN data in the format required by the EC is under way. The agricultural census was completed in 2000 and the results were published in 2001.

As concerns quality policy, a system similar to the EC system for protection of designations of origin, geographical indications and certificates of a specific character has already been in place since 1998, but it was implemented practically in 2001 through the registration of the first product names.

Regarding trade mechanisms, Hungary has already indicated the administrative structures prescribed by the *acquis* as necessary for accession (in particular a paying agency for export refunds, an issuing body for import/export licences, a body for collecting export taxes, a control body for verifying the destination of products sold from intervention stocks, a body to carry out physical checks, body to carry out veterinary checks for animal welfare).

Common Market Organisations

Since last year's Regular Report, Hungary has made limited progress in introducing the legal framework and administrative structures for the establishment of the Common Market Organisations. The role of the Produce Councils in the future common market organisations will need to be defined, since they currently also perform tasks that will be carried out by the future intervention agency.

In October 2001, Hungary adopted a law regulating the sugar market through the establishment of quota for processing firms. The Hungarian milk sector is regulated through a system of quotas partially in line with EC legislation. The quality of milk delivered is generally good (83% meets the relevant EC quality requirements). Further improvement of the health and hygiene conditions is planned and necessary.

In the meat sector, the bovine identification system has already been set up, and it needs to be extended to the sheep, goat and pig-meat sector over the coming years. The beef sector has suffered from a generally difficult period.

The marketing standards applied to exports of fresh fruits and vegetables to the EC were extended to imported and domestic products in November 2000. The number of inspectors has been increased. Standards and inspections have reached a satisfactory level. Five Producer Organisations already exist and received preliminary recognition in 2000. They benefit from national financial support (for about 10% of the value of their marketed production), whereas an aid scheme is in place for processing of tomatoes. Preparations for the implementation of other measures connected with the market organisation for fruit and vegetables need to be completed. The establishment of regional wholesale markets would be useful progress in this sector.

In the wine sector, Hungary has introduced excise duty on wine and set the legal conditions for keeping wine cellar registers. The law on statistical surveys of areas under vine and fruit

orchards was adopted in December 2000, and the statistical survey was carried out between June and October 2001. As the next step, a fully functioning vineyard register needs to be put in place and constantly updated.

Rural Development and forestry

Little progress was made in this field. The implementation of the national Agri-Environmental programme, adopted in 1999, was further delayed. It should be highlighted that according to the *acquis*, the national rural development plans must include agri-environmental measures.

As regards forestry, the law on protection of forests against fire was adopted in April 2001. Hungary is undergoing a long-term afforestation programme. Preparations for the establishment of the Hungarian part of the European Forestry Information and Communication System (EFICS) have started.

Veterinary and phytosanitary issues, including food safety

Hungary has intensified its preparations for complying with the *acquis* in the **veterinary field**. The amendments to the Veterinary Act entered into force in July 2001, introducing the principle of regionalisation and animal passports and defining the tasks of State and private veterinarians. The amendments to the law also cover the principle of full compensation for producers and the rules concerning veterinary checks in the internal market, although these provisions will only enter into force on the date of accession.

Two pilot projects on the identification and registration of pigs started in September 2000. The veterinary institution network was rationalised and the Central Veterinary Institute was designated as the National Reference Laboratory for all OIE 'A' list diseases. The government adopted a strategy on the development of border inspection posts in January 2001. Progress in upgrading the Border Inspection Posts at Letenye, Roszke and Zahony was impeded by difficulties in acquiring the land.

The Hungarian Veterinary Service has carried out an evaluation of the food safety status of fresh meat establishments. Out of the 471 existing plants, 228 are high capacity and 64 are in compliance with EC requirements. The remaining 164 plants were required to draw up a detailed development plan, to start eliminating identified deficiencies by March 2001 and to finish their upgrading at the latest in December 2007.

Hungary introduced EC rules on specific risk material (SRM) in April 2001. Since then, the application of SRM rules in all slaughterhouses, regardless of their capacity, has been compulsory in Hungary. A monitoring programme in compliance with EU rules on TSE testing was launched in March 2001. In the context of the Geographical BSE Risk Assessment, Hungary has been classified in group III.

While no progress was registered in relation to animal welfare, progress has been made as regards animal nutrition. The Hungarian legislation of feeding stuff was amended in June 2001, thereby ensuring alignment with the *acquis* in a number of areas (feed additives, feed sampling and analysis, the circulation of feed materials, prohibited ingredients in animal nutrition, maximum permitted levels of undesirable substances and products, the method of calculation for the energy value of compound poultry feed and the use and marketing of enzymes, micro-organisms and their preparations in feeding stuff).

In the **phytosanitary sector**, some progress has been made since last year's Regular Report. Alignment with the *acquis* on pesticide use and registration and harmful organisms was continued with the implementation of the law on Plant Protection.

The administrative system for plant and soil protection institutions has been reorganised and a Central Service for Plant Protection and Soil Conservation has been established for performing national official tasks as well as for organising and co-ordinating activities of the Services in the counties.

The plant health system in the potato sector is generally good, although further improvement is recommended.

The number of border inspection posts has been reduced from 18 to 10. So far, none of them is in full compliance with the EC requirements.

As regards **food safety**, in April 2001 Hungary drew up a Food Safety Strategy, which was prepared by the inter-ministerial working committee on food safety. It outlines the various official bodies involved, their roles, organisation and staffing as well as the institutional changes planned in order to ensure co-ordination between the Ministry of Health, the Ministry of Agriculture and Regional Development and the General Inspectorate of Consumer Protection. An advisory committee has been established within the Ministry of Health (*see also Chapter 1 – Free movement of goods*).

Overall assessment

While Hungary has a generally good record for the application of the *acquis*, it needs to speed up its preparation for accession in a number of areas. Despite wide political debate, the issues related to land market and land consolidation remain to be tackled. With few exceptions, the agricultural sector suffers from a general lack of competitiveness and does not attract the investments that would be necessary for its modernisation.

However, some progress can be registered in the food safety and veterinary fields, and the foundations have been laid for important registration instruments for cattle and vineyards. Hungary continues to have a positive agricultural trade balance with the EC, though lower than in the past. 2001 was a much better year for arable crops and poultry meat, but still a critical year for beef and pig-meat sectors.

Hungary has not yet taken the necessary formal decisions regarding the establishment of the management structures for the EAGGF Guidance and Guarantee Section and for the future common market organisations, including the Integrated Administration and Control System. This has slowed down its progress in preparing for the implementation of the agricultural *acquis* over the last year. In order to achieve these results, much remains to be done in terms of the adoption of the legal background and establishment of the procedures and of the structures in charge of implementation of the agricultural *acquis*.

Despite some recent progress, Hungary's preparations for national accreditation of the SAPARD Agency are lagging behind. National accreditation might be achieved before the end of 2001.

Further recruitment and training of qualified staff is recommended. Ensuring an appropriate degree of stability for the Ministry staff is equally important.

As regards **horizontal issues**, progress in establishing the Integrated Administration and Control System (IACS) also requires the adoption of decisions regarding organisational structure, co-ordination and financing. Progress also needs to be made to complete the land parcel identification system, especially as regards digitalisation of land parcels according to EC requirements.

Concerning the implementation of **Common Market Organisations**, the role of the Agriculture Intervention Centre in the management of the common markets needs to be further clarified and subsequently legally endorsed. The key management mechanisms for most common market organisations need to be established and the future role of the produce councils needs to be decided. Some improvement in the market information system can be registered. In the arable crops sector further progress is still required with regard to the preparation for the implementation of the common agricultural policy, although an area-based subsidy scheme is already in place.

In the area of **Rural Development and Forestry**, Hungary needs to establish the institutional structure and to allocate suitable budgetary resources to implement the National Agri-Environmental Programme.

Concerning the **veterinary field**, the amendments to the Veterinary Law provide the necessary legal framework for the harmonisation of the Hungarian veterinary legislation with the *acquis*, however complete transposition requires the adoption of technical regulations. The shortcomings identified in the bovine identification and registration system need to be addressed and more progress is needed as regards the identification and registration of pigs, sheep and goats, including the transposition of EC rules on pigs. Controls at the future external borders of the EU are not yet in compliance with the *acquis*. Specific action has begun in upgrading establishments but further progress is required in this area.

At present, a large portion of the high-capacity fresh meat establishments does not meet the requirements of the veterinary hygiene *acquis*.

In the **phytosanitary sector**, further efforts are needed as regards the registration of operators, the issuing of plant passports and the system of notification. The legislation on seeds and propagating material, maximum residue levels, plant hygiene and animal nutrition still needs to be further harmonised.

With regard to **food safety**, Hungary lacks of a clear plan on how to rationalise activities across ministries, although each of the single ministries have plans for better internal co-ordination among their own departments.

Chapter 8: Fisheries

No further progress was made over the last year with regard to alignment with the *acquis*. However, progress was achieved towards the reinforcement of the administrative capacity by the recruitment of staff dealing with fisheries in the Ministry of Agriculture and Rural

Development, as well as by the appointment of new inspectors in the Regional Offices for Agriculture.

Overall assessment

Although the basic framework legislation is mostly in line with the Common Fisheries Policy, further amendments are required in order to implement marketing standards and to establish the conditions for the control of species and provenance of imported fish.

As regards the administrative structures, Hungary still needs to establish the system for controlling imported fish, and improve the control of the implementation of common marketing standards, the application of the recognition conditions for producers' organisations and the implementation of the structural policy for fisheries. Further efforts are required as regards the preparations for the implementation and the management of the structural policy in the fisheries and aquaculture sector.

Since Hungary is a landlocked country, parts of the *acquis* related to fisheries are of lesser importance to this country.

Chapter 9: Transport policy

During the reference period Hungary continued to align with the transport *acquis* although progress was rather limited in the road and rail sectors. No particular progress can be reported as regards administrative structures.

As regards **Trans-European Transport Networks**, infrastructure construction work was speeded up, in particular as regards motorways. The planned development projects for 2001-2 include the construction of the Füzesabony-Polgár stretch of the M3 motorway, the reconstruction of the M7 motorway between Budapest and Zámárdi and the construction of Szekszárd bridge across the Danube. In addition, a wider road rehabilitation programme has been developed with a view to meeting the required increase in the maximum axle load (weight) of trucks. Meanwhile, the first direct railway connection between Hungary and Slovenia was opened to traffic in May 2001.

In the **land transport** sector, some progress was made in *road transport*. The main regulatory achievement was the alignment as of May 2001 of the rules for admission to the occupation of road haulage operator. The alignment of safety belt legislation has been completed. A further positive development was the signing of the INTERBUS Agreement in June 2001 concerning occasional international passenger transport and the entry into force on 1 June 2001 of the Agreement between the EC and Hungary concerning the carriage of goods by road and the promotion of combined transport.

On *railways*, the accounting separation of railway infrastructure from railway operations has been completed within the Hungarian Railways Company (MÁV).

In the *inland waterways* and *maritime transport* sector, on the basis of the framework law on water transport of May 2000, implementing legislation has been adopted on the registration of vessels, licensing of navigation operations, navigation qualifications, inspectors' qualifications and identification cards, technical requirements for vessels, and designation of bodies for the

certification of conformity of vessels. The planned Inland Waterways Fund still needs to be set up.

As concerns **air transport**, progress has been achieved with aligning technical requirements and administrative procedures of civil aviation, a code of conduct for computerised reservation systems, rules on licensing of air personnel and air carrier liability. It is also positive that Hungary this year became a full member of the Joint Aviation Authority. However, negotiations with Hungary on the European Common Aviation Area (ECAA), which would ensure an early application of the aviation *acquis*, have not been finalised.

An attempt to privatise a minority share of the state-owned airline Malév failed in early 2001. The government remains committed to (partial) privatisation, but the medium-term prospects of the national flag carrier remain rather unclear. A restructuring programme aimed at restoring the financial and commercial viability of Malév is underway, involving staff and cost reduction.

No particular developments can be reported concerning the administrative capacity in the field of transport.

Overall assessment

Partial alignment has been achieved in the transport field; further efforts are required to enhance administrative capacity in the road, rail and air sectors.

Hungarian policy in the field of transport infrastructure already takes into account the objectives and priorities of the Community guidelines on the Trans-European Transport Network (TEN-T) and the requirements on TEN financing. In the area of *road transport* there is, despite progress made, a need to further align throughout the subsector, particularly with the provisions on access to the market and the profession, fiscal matters, social legislation and technology, safety and environment (e.g. maximum weights and dimensions).

With regard to *rail transport*, the restructuring of MÁV is an urgent task, in particular in the light of the new *acquis* in this area. The revision of the rail reform programme adopted in 1999 is progressing rather slowly; further restructuring and legislative alignment should not be delayed. The administrative capacity of the Hungarian railways should be further developed. In particular, Hungary needs to set up a separate unit for allocation of capacity and for infrastructure charging.

Presently, the General Transport Inspectorate (GTI) is responsible for road, rail, inland waterways and maritime issues. The major part of its budget is funded through fees, the levels of which are set by the Ministry of Transport. Some two-thirds of fee revenues come from vehicle inspection. The GTI is being strengthened over a number of years, including new technology and equipment and several hundred more staff. The transport authority's staff was increased by 56 people in 2000. First investments were made in mobile vehicle weighing installations. The supervisory authority of the water transport sector is the Maritime and Inland Navigation Inspectorate within the GTI; it has 29 employees, including two persons who are certified for Port State Control duties. Including on-site checks, 5000 to 6000 cases are investigated annually by the GTI.

The plans for the reinforcement of the General Transport Inspectorate (GTI) in terms of staffing and technology, if carried through and if combined with the necessary training and organisational changes, should help to bring administrative capacity up to the required level. All transport subsectors should benefit from this strengthening (road, rail and waterways). The necessary organisational changes include the improvement of co-operation with other agencies. The GTI already works closely with the Police, including on joint inspections, but some aspects of their interaction, such as access to vehicle registration data, still need to be clarified.

Some specific further efforts to align with the *air transport acquis* remain, notably concerning market access. Hungary should consider again its negotiating position regarding the possibility of joining the future European Common Aviation Area. Administrative control is now concentrated in the Air Traffic and Airport Administration located at Ferihegy (Budapest) airport. Overall state control is secured at ministry level, as are regulatory policy-making and international activities. An independent accident investigation authority, an independent slot co-ordination authority and a body for licensing and safety need to be established.

Chapter 10: Taxation

Hungary has continued to make progress in the area of taxation.

In the area of **indirect taxation**, the VAT regime was further harmonised in November 2000. This amendment to the tax law provides for gradual alignment with the *acquis* concerning the scope of products covered by a reduced VAT level and the supply rules for telecommunication services. The law entered into force in January 2001.

In the area of excise duties, gradual harmonisation of the duty levels continued. The approximation of the minimum duty on alcoholic products and tobacco was approved by Parliament in the framework of voting the 2001-02 national budget. In January 2001, the duty for the lower-taxed fruit brandies was increased by 10% and for other alcoholic beverages by 5%, bringing the preferential rate up to 87% of the regular one. As concerns cigarettes, the excise duty was increased in January 2001 by 15% to 42.8% of the normal rate.

In the area of **direct taxation**, in 2000 Hungary fully aligned its system with the common system of taxation applicable to mergers, divisions, transfers of assets and exchanges of shares concerning companies of different Member States. Some of the implementing provisions will enter into force upon accession. As regards the taxation of holding companies, new legislation excludes current tax benefits available to these companies for investments initiated after accession.

Hungary further improved its effectiveness in excise collection by setting up a special unit within the National Headquarters of Customs and Excise. Its task is to fight abuse and fraud in the trade of mineral oils, cigarettes and alcoholic products. The revenues of the Hungarian Tax and Financial Control Administration from ex-post controls increased by 33% in 2000. The Administration issued about 500 000 audit decisions of first instance, of which 11 300 were appealed to the second instance. Out of these latter, about 75% were upheld by the Court. In 2000, criminal cases were initiated against 1 589 individuals. The most common cases were those concerning fraud and tax fraud, but the number of cases involving counterfeit and offences against accounting rules also increased.

In order to further improve tax collection, the National Headquarters of Customs and Excise Authorities agreed to set up a 30-40-strong special commando unit to curb abuses of excise duties.

As concerns the modernisation of the tax current account register, since January 2001 all taxpayers and contributors have made their payments on a uniform tax current account.

The operation of the taxation system is based on self-assessment. The system is still dominated by paper-based documents, which are then processed by computer. Since January 2001, document forms for tax return have also been available online. It is also possible for organisations and businesses to fulfil their data supply obligations via magnetic data carriers. However, at present it is only possible for some 520 large corporate taxpayers in Budapest and Pest County to submit tax declarations and returns electronically, on the basis of a bilateral agreement with the tax authorities.

There are no specific developments to report in the area of **administrative co-operation and mutual assistance**.

Overall assessment

Hungary continued its alignment in this sector, where the basic structures of the *acquis* related to VAT and excise duty are already in place. In the area of VAT, further efforts were made to harmonise and implement the relevant provisions of the *acquis*. However, further efforts are needed with regard to the scope of reduced VAT rates, including the abolition of zero-rates, tax refunds for foreign taxable persons, and special regimes.

In the area of excise duty, although rates were further harmonised with the *acquis*, further efforts are still needed concerning duty suspension arrangements and the adoption of excise duty levels for cigarettes, tobacco products and spirits. A risk analysis method – to be applied by the customs authority – also needs to be developed.

In the area of direct taxation, Hungary has to finalise the review of its legislation in line with the Code of Conduct for Business Taxation. Furthermore, the current regulation governing taxation of dividends has to be reviewed. Finally, work has to be carried out on the taxation of certain items of income received by non-residents in a Member State other than that in which they are resident.

As concerns administrative co-operation and mutual assistance, rules on the co-operation among tax authorities of Member States have to be harmonised. Continuous efforts are still needed regarding the further development of the IT systems allowing for the exchange of electronic data with the Community and the Member States. This concerns in particular the Central Liaison Office (CLO), for which in particular appropriate IT material has to be purchased and developed in view of the pilot test scheduled for September 2002. The customs authority has to prepare the connection of the SEED database with the EC excise system.

Chapter 11: Economic and Monetary Union

A detailed assessment of Hungary's economic policy in its various aspects has been given above, in the Chapter discussing the economic criteria (B-2). Therefore, the present section is

limited to a discussion of those aspects of the Economic and Monetary Union *acquis*--as defined by title VII of the EC Treaty and the other relevant texts--which candidate countries should implement before accession, i.e. the prohibition of direct public sector financing by the central bank, the prohibition of privileged access of the public sector to financial institutions, and independence of the national central bank. As to the process of liberalisation of capital movements, upon the completion of which compliance with the EMU *acquis* is conditional, this aspect has been covered above, in the section on *Chapter 4 – Free movement of capital*.

Since the last Regular Report, Hungary has made significant progress in the adoption of EMU-related *acquis*.

Progress towards reaching full alignment with the *acquis* was achieved in June 2001 with the adoption of a new law on the National Bank (NBH) which further strengthened the **independence of the National Bank**. The new 2001 Act on the National Bank of Hungary entered into force in July 2001. In the area of personal independence for members of the decision-making bodies, the new Act brought the legislation in line with the *acquis*. Rules defining the term of office of all members of the decision-making bodies and in particular the conditions for their dismissal have been further aligned. In the area of institutional independence, the new Act provides that the Bank and its decision making bodies shall be independent and neither seek nor take instructions from the government or any other body, a provision now fully in line with the *acquis*.

Furthermore, the financial facility provided by the National Bank to the state budget was eliminated in December 2000. The rules for the allocation of profits and losses have also been modified prior to adoption of the new Act on the NBH. Therefore, **direct financing by the National Bank** is no longer possible.

In addition, in order to comply with the *acquis* from the point of view of prohibition of **privileged access of the public sector to financial institutions**, the 1996 Act on Home Savings and Loan Associations has been amended by eliminating the preference afforded to Hungarian Government securities in the portfolio composition of these institutions. This amendment entered into force in July 2001.

Overall assessment

Hungary will participate in EMU upon accession with the status of a country with a derogation under Article 122 of the EC Treaty. It will need to implement the necessary changes to its institutional and legal framework by the date of accession.

Hungary's legislation in the area of economic and monetary union is already substantially in line with the relevant provisions of the *acquis*. During the reporting period, Hungary has further aligned its legislation with the relevant provisions of the *acquis*. The abolition of direct public sector financing by the National Bank – which took the form of direct lending to the Central Budget or by subscription of State Bonds - and the adoption of an amendment to the law on the National Bank in June 2001 were important steps in this direction.

The National Bank is well staffed. It has a comprehensive web-site and regularly issues material on its work, including monthly reports, quarterly inflation reports and surveys of credit institutions and, twice a year, reports on financial stability.

Chapter 12: Statistics

Hungary continued the alignment of its statistical system with the *acquis*, especially in the area of social and economic statistics.

As regards the **statistical infrastructure**, the Hungarian Central Statistical Office is a professionally independent public administration body with national competence under the immediate supervision of the Government. Currently, the number of permanent staff amounts to 889 in the central administration compared to 833 last year, while the total number of people employed at regional offices is 965. The Central Statistical Office is adequately endowed with resources including human resources and IT equipment.

Concerning **classifications**, in 2000 the statistical units of the production system were defined and applied in accordance with the provisions of the *acquis*, including the use of local kind of activity units. Statistical classifications, including NACE, have already been implemented in Hungary.

Concerning **demographic and social statistics**, a population census was carried out in February 2001 in conformity with the relevant rules of the *acquis*. Quarterly reporting to Eurostat on the results of the Labour Force Survey (LFS) was established in 2001, and additional LFS modules were implemented. Work on the development of a labour market information system continued. Preparatory work for a labour cost survey (reference year 2000) was carried out, while the methodology continues to develop within the framework of the project organised by Eurostat. A pilot survey with the aim of establishing a labour cost index was carried out in 2001.

Hungary already provides substantial amounts of statistical data at the **regional** level.

As concerns **macro-economic statistics**, further steps towards harmonisation were taken regarding the harmonised consumer price index and the coverage of the price index has been extended.

For **business statistics**, the improvement and extension of the business register continued in accordance with the requirements set by Eurostat.

In the area of **transport** statistics, the conditions for the introduction of the following data collection systems were established: carriage of dangerous goods by road, international carriage of goods by road and combined carriage of goods.

In the field of **tourism**, conditions for the introduction of data on tourism demand by both the resident population and foreigners were introduced.

On the basis of the **agricultural** census carried out in 2000, a fruit tree and vineyard survey was conducted between June and October 2001.

Overall assessment

Hungary is very well advanced in the field of statistics. Statistical co-operation with international organisations runs smoothly. Some further efforts are still needed to fine-tune the harmonisation of some statistics, including foreign trade statistics, and to increase the timely availability of

macroeconomic statistics. An adequate level of resources ensures the sustainability of the statistical operation.

Chapter 13: Social policy and employment

Considerable progress has been made in this area since the last Regular Report.

The amendments to the **Labour Law** entered into force in July 2001, except for elements related to the transposition of the Directives on the posting of workers and European Works Councils. The amendments aim to further align the Hungarian legislation with the *acquis* on a range of issues including collective redundancies, working time, young people and posting of workers. The county public employment services are the competent public authority for projected collective redundancies. In order to facilitate the effective enforcement of the *acquis* in this field, a one-year training programme for labour law judges was launched in the beginning of 2001.

In the field of **equal treatment for women and men**, the amendments address the directives on equal pay and on the burden of proof.

In the area of **health and safety**, new legislation entered into force, aiming at the transposition of the directives on chemical, physical and biological agents, indicative limit values, banning of certain specified agents or certain work activities, vinyl chloride monomer, metallic lead, asbestos, and carcinogens. Also, in the areas of drilling, mineral-extracting industries and noise, progress was made in March and May 2001, respectively.

The National Labour Inspectorate was designated as the national focal point for the European Agency for Health and Safety at Work. The Inspectorate was also further upgraded technically, and staff underwent, *inter alia*, language training.

In June 2001, Hungary adopted a 10-year **Public Health** Action Programme with the ultimate goal of increasing overall life expectancy (women from 75 to 78 years and men from 66 to 70). In December 2000, new legislation on the regulation of tobacco advertising entered into force, which partially aligned Hungarian legislation with Community tobacco legislation. A programme to re-organise and improve the blood supply system has been launched, and a new regional system established. The National Public Health and Medical Officers' Service organised a number of training courses for its staff on EU legislation with special emphasis on legal approximation and law enforcement.

In the area of **social dialogue**, the relationship between the government and the social partners continued to be marked by a lack of confidence and trust and by difficulties in operating effective tripartite social dialogue within the various newly established structures. In the reference period, this lack of confidence was illustrated by the controversies, which arose on the modification of the Labour Code and on the decision-making process used for setting the national minimum wage for 2001. More recently, agreement was reached on the increase for 2002. Autonomous sectoral social dialogue continues to be rather weak with few collective agreements signed at sectoral level. At enterprise level, collective agreements exist mainly in large companies. In March 2001, the government concluded a three-year agreement with the largest trade union confederation of the public sector, which foresees, *inter alia*, the creation of a new forum for consultation in the public sector called the National Labour Council for Public Employees.

The situation in the labour market improved further in the reference period. The unemployment rate continued to decrease in 2000 reaching 6.4%, and to below 6% in the first half of 2001. Also, long-term unemployment continued to fall and is lower than the EU average.

Hungary and the European Commission have launched an **Employment Policy Review** with a view to examining the progress made by Hungary in adapting its employment system so as to be able to implement the European Employment Strategy. This document lays down the key priorities and tasks for the pre-accession period. The final version is to be jointly signed by the Commission and the Hungarian authorities in November 2001.

In relation to the future establishment of the **European Social Fund** (ESF), the Ministry of Education will assume responsibility as the Managing Authority of the Human Resources Development (HRD) Operational Programme. The ESF Inter-ministerial Task Force and the Human Resource Development Working Group further improved the co-ordination of ESF-related policies and activities of line Ministries and other relevant bodies (in the context for instance of the Joint Assessment of the Employment Policy Priorities). The establishment of the ESF National Implementing Agency also represented an important development in the context of future ESF-related implementation arrangements.

As regards **social protection**, preparatory steps have been taken to further continue the pension reform, scheduled for implementation in 2003. The implementation of the National Programme for People with disabilities has had some first results in the areas of work environment, communications, transportation, health care, education and training, employment, sports and leisure time and social welfare.

As regards anti-discrimination, no further progress can be reported at this stage, but the Ministry of Justice will, following a review of anti-discrimination provisions contained in the current legislation, further consolidate the legal framework by improving enforcement and sanctions mechanisms. (*see also section B.1.2. - Human rights and the protection of minorities*).

Overall assessment

Overall, Hungary is rather advanced in terms of legal alignment in all areas. The amendments to the labour law address a large part of the relevant Community *acquis*. However, further efforts are required, notably as regards the directives on part-time work, insolvency and the European Works Councils. Further strengthening of the National Labour Inspectorate, both in terms of staffing and technical facilities, is also needed.

Regarding equal treatment for women and men, Hungary is already well advanced regarding both transposition, implementation and enforcement. However, further efforts are needed to finalise the transposition of the Directives on equal treatment in agriculture and self-employment as well as on equal access to employment and vocational training. Institutional mechanisms for implementing and enforcing the *acquis* require further strengthening. Hungary has continued to participate in the Community Action Programme on Equal Opportunities.

Regarding health and safety at work, transposition advanced well in 2000 and 2001. Hungary needs to finalise the transposition of the directives on workplaces, fishing vessels, display screen equipment, health and safety requirements at temporary or mobile construction sites and

medical treatment on board vessels. Considerable work remains to be done with respect to the effective implementation of the *acquis* in this area. In this respect, particular attention should be paid to small- and medium-sized enterprises.

With regard to public health, further efforts have to be made to meet the requirements of the directive on the quality and safety of blood. In general, Hungary has continued to participate in a number of Community public health programmes and has expressed its interest in taking part in all of them.

Sound developments in social dialogue should be actively promoted. Strengthening the administrative capacity of both social partners and the government would help them to find ways of progressively operating more effectively. To this end, the planned government-training programme should now be implemented with a view to helping social partners to build up their own research and negotiation capacity. On the tripartite level, ensuring due process within the existing tripartite structures would contribute to restoring confidence. In this context, particular attention could be paid to the statutes and procedures of these structures. Autonomous social dialogue, especially at sectoral level, should be promoted. Social partners should make more use of their autonomy to conclude agreements among themselves. The registration of these agreements by the government could also be improved.

Regarding employment, the Joint Assessment of the Employment Policy Priorities of Hungary (JAP) by the European Commission and Hungary's authorities will represent an important step in the preparation for accession. It will now be important to ensure an effective monitoring of the phasing in of the priorities and commitments contained in the JAP.

In its capacity as Managing Authority for the HRD programme, the Ministry of Education will need to further strengthen effective inter-ministerial co-operation. Within the co-operation framework established, the Ministry should take the necessary steps to ensure that all European Social Fund type assistance is directed across policy fields and implemented in the context of the multi-annual National Action Plans. It will also need to ensure appropriate complementarity with the ESF component of the integrated Operational Programme (OP) for Regional Development. Although not assuming the responsibilities of a Managing Authority, the role of the ESF National Implementing Agency should now be developed under the future implementation arrangements. The operation and control of the ESF Task Force should also be reviewed in the light of the Government's decision of June 2001 on future programming structure.

In the field of social protection, sustained efforts are required in implementing the reforms that have been introduced. This concerns, *inter alia*, the health care reform, in order to further improve the level and the efficiency of social protection. The strategic aims of the National Programme for people with disabilities, notably those to facilitate their social integration and to fight all form of discrimination should be further pursued.

The fight against exclusion, as laid down in art. 136 of the Treaty establishing the European Community, forms part of the objectives of EU social policy. As decided at the Lisbon and Nice European Councils, policies to combat social exclusion combine commonly agreed objectives at the EU level, and national action plans. The Gothenburg European Council in June 2001 invited candidate countries to translate the Union's objectives of promoting social inclusion into their national policies.

Finally, further efforts are needed to ensure alignment with the *acquis* on anti-discrimination based on Art. 13 of the Treaty.

Chapter 14: Energy

Since the last Regular Report, Hungary has made limited further progress in this area.

In the context of its preparations for the **internal energy market**, legislative work has not yet led to concrete results. The Hungarian Government prepared a revised draft law on the liberalisation of the *electricity* market, which however has not yet been adopted by Parliament. Thus, the original plan to partially liberalise this market (15% of total annual consumption) as of January 2001 was further delayed. No progress was made in the *gas* sector either.

As a further step in the area of institution building, the independent system operator (MAVIR, the Hungarian Power System Operator Company) was established in October 2000.

In January 2001 and July 2001 respectively, a new price system for the period came into force with a view to gradually eliminating the existing price distortions in the electricity and gas sectors. As a consequence, the average consumer prices for electricity were increased by 6% as of January, and the average consumer prices for gas were increased by 12% as of July 2001 respectively.

The Government continued to promote **energy efficiency** in line with the energy efficiency programme adopted in late 1999. For this purpose HUF 910 million (around € 3,5 million) were made available in 2000. Under the programme, support is given to energy saving loans, the use of renewable energy sources, the modernisation of district heating supply and consumption systems, improved public energy awareness and the promotion of energy efficiency in transport.

In the field of **nuclear energy**, Hungary operates one nuclear power plant located at Paks. There are four units of VVER 440/213 type in operation. The nuclear safety programme of the Paks Nuclear Power Plant – supposed to be finished by the end of 2002 - continued to be implemented with more than two-thirds of the actions already finished by the end of 2000. As a result of these measures, the core damage probability has decreased by a factor of 10.

Overall Assessment

Overall, Hungary is advancing in preparing for the energy *acquis* and has continued to strengthen the administrative framework. However, efforts relating to the internal energy market still need to be enhanced.

As regards **security of supply**, Hungary already reached the required levels for stocks of crude oil and petroleum products.

In the area of the internal energy market, Hungary should speed up its preparations regarding the adoption of new electricity and gas laws in order to avoid additional delays. In this context, the Hungarian Energy Office should be further strengthened to perform its role as the energy regulator. Remaining price distortions should be eliminated. Furthermore, efforts regarding energy efficiency should be stepped up.

The institutional structure is well developed and comprises the following bodies:

The Ministry of Economy is in charge of energy policy in general. The Hungarian Energy Office is an independent body under the responsibility of the Minister of Economy and in charge of licensing, price regulation and energy conservation. In 2000, the Office issued 99 decisions, of which 14 were challenged and one was withdrawn. At present, its staff numbers 83 (no change since 2000). The Office is funded by duties from licensing. This body should be further strengthened.

The Energy Interest Reconciliation Council is a consultative body comprising the regulator, the consumers and the suppliers of the industry.

The Energy Centre is in charge of energy efficiency, environment protection, labelling, and energy statistics. The Centre's annual budget amounts to HUF 200 million (around € 770,000) with a staff of around 20 people. However, as regards energy statistics, further efforts are necessary to align with the *acquis*, in particular as concerns energy efficiency indicators.

The Hungarian Mining Office is in charge of licensing, monitors the mining activities and compliance with the law, and controls safety at work.

The Hungarian Atomic Energy Authority is in charge of regulation, licensing and supervision. Although it operates under the supervision of the government, it is an independent authority with a separate budget funded from the central budget and from fines collected. The Authority has an important role to play in supervising liability for compensation. Under international agreements it covers potential damage within Hungary and across the border. Following the mission of the International Atomic Energy Agency (IAEA) International Regulatory Review Team (IRRT) in May 2000, it was confirmed that the Hungarian Atomic Energy Authority is a highly competent organisation, which has the technical capability to deal with the regulatory and technical areas, for which it is responsible. On the basis of recommendations and suggestions in the IRRT report, an Action Plan has been developed.

In relation to nuclear facilities, the Nuclear Safety Directorate issues facility system and equipment licenses in accordance with requirements specified in the relevant law and safety regulations. Facility licenses must be obtained for selecting a site for a nuclear facility and for constructing, commissioning, and modifying, suspending, closing down or decommissioning a facility. A safety review performed every 10 years is also considered to be a requirement of facility licensing. The licensing related to the nuclear civil structures and their design may be carried out either in the framework of or separately from the facility licensing procedure. In its emergency preparedness and response activities, the Nuclear Safety Directorate performs analyses and evaluations independently from the operator in the early stages of accidents.

As regards the issue of nuclear energy, the European Union has repeatedly emphasised the importance of a high level of nuclear safety in candidate countries. In June 2001, the Council of the European Union took note of a Report on Nuclear Safety in the Context of Enlargement. This report contains findings on the situation and perspective regarding nuclear safety in each candidate country, as well as recommendations for specific improvements. In July, the Commission conveyed this report to the candidate countries.

General recommendations of the Council Report call for all candidate countries with nuclear power plants to complete their plant-specific safety improvement programmes, and to ensure

that their programmes include measures considered good practices within the European Union, particularly regarding various specified safety measures such as assessment practices, emergency procedures, feedback of experience, resources of the regulatory authority and other aspects.

The report recommends all candidate countries to continue their national programmes regarding the safe management of spent fuel and radioactive waste, and regarding the safety of their research reactors.

With regard to Hungary, the Council Report recommends completing the strengthening of the independence of the regulatory body and measures to complete the regulatory review regarding the bubbler condenser systems of the Paks NPP.

In the field of nuclear energy, competencies are well defined, the institutional structure is clear and transparent, and enforcement is efficient. Nonetheless, as recommended in the Council reports on nuclear safety, Hungary should complete the ongoing process of strengthening the independence of the regulatory body related to the operation of nuclear facilities.

Finally, regarding the independence of the nuclear safety regulator, the report recommends completing the on-going process of strengthening the independence of the regulatory body in relation to persons, bodies or organisations that are related to promotion of nuclear energy or operation of nuclear facilities.

Hungary still needs to provide facilities for the deposit of small and medium-activity radioactive waste.

Hungary is a party to all major international legal instruments and member of the International Atomic Energy Agency (since 1957) and the OECD Atomic Energy Agency (1996). Hungary will need to ensure compliance with Euratom requirements and procedures. In this respect, continued attention should be given to preparing the implementation of Euratom Safeguards, in particular regarding the reporting of nuclear material flows and inventories directly by the persons or by structures operating nuclear installations or storing nuclear material. It should be noted that Hungary has concluded a Full Scope Safeguards Agreement with the IAEA. An additional Protocol of this Agreement has been in force since April 2000.

Chapter 15: Industrial policy¹⁹

Over the reference period Hungary made some further progress in developing its industrial and enterprise policy.

The **industrial strategy** of Hungary continued to be based on the improvement of the competitive economic environment and the maintenance of balanced growth. Through the implementation of the Széchenyi Plan more financial resources have been dedicated to proactive measures aimed at promoting networking and innovation and reducing the imbalances of industrial development by attracting new investors to the east of the country. Measures having a bearing on industrial development are included in several sub-programmes, the main one being

¹⁹ Developments concerning Industrial policy should be seen in relation to the overall enterprise policy, including the SME policy (see Chapter 16 – Small and medium-sized enterprises).

the Enterprise Development Programme, which amounts to more than 10% of the total budget of the Széchenyi Plan in 2001, i.e. HUF 31.4 billion out of HUF 295.9 billion (around € 121 million out of € 1.138 billion). As the tendering process is still ongoing, it is premature to assess the impact of these initiatives.

The process of **industrial restructuring** continued, and privatisation is virtually completed. FDI continues to be a significant driving force behind the modernisation of industry. Electronics and car manufacturing are productivity leaders.

In the reporting period Hungary advanced the restructuring of its steel industry. The Hungarian Government withdrew in June 2001 its request for the extension for 5 years of the 'grace period' authorising to grant state aid for restructuring purposes to the steel industry under Protocol 2 of the Europe Agreement. The liquidation procedure for DAM Kft. has been completed and the assets transferred to the new owner, while Dunafer, under new management since February 2001, has delayed plans for privatisation.

Overall assessment

Significant convergence can be noted between Hungarian industrial policy and the principals and objectives of the EC industrial policy.

Hungary has successfully implemented a market-based privatisation and restructuring programme over the years, which has contributed to attracting regular and high levels of FDI. As a result, the industrial sector is internationally oriented. Technology-driven industries account for a growing share of exports to the EU (around 50%). The challenge is now to further close the gap between the regions, on the one hand, and between large export-oriented companies and local-market-oriented small businesses, on the other hand.

The Ministry of Economic Affairs, as the body responsible for the formulation and co-ordination of industrial policies, has developed the industrial policy in an integrated manner. Line ministries that are responsible for managing specific industrial branches take part in the policy-making process. A wide range of agencies and governmental bodies are involved in the implementation process. The main ones are the Privatisation Agency and the Investment and Trade Development Hungary Co-operation, which is jointly operated by the Ministry of Foreign Affairs and the Ministry of Economic Affairs, and has 9 regional offices. Several mechanisms such as the Economic Council, the Enterprise Development Council and the Investors' Council, are in place to consult the business community and social partners, and operate in a satisfactory manner. The Confederation of Hungarian Employers and Industrialists, MYGOSZ, is a key partner for the government. It covers all industrial branches and represents the interests of 6.000 enterprises totalling 1.2 million employees.

It should be noted that an important element of any industrial policy is the control of state aid and the compatibility of support schemes with EC rules, including the current rules on state aids of the ECSC Treaty, which will have to be examined. (*See Chapter 6 - Competition policy*)

Chapter 16: Small and medium-sized enterprises²⁰

Hungary has made further progress in developing its SME policy since the last Regular Report, in particular through the launch of the Széchenyi Plan in autumn 2000.

The Széchenyi Plan has become the main instrument for implementing the priorities of Hungary's **SME strategy**. The Enterprise Development Programme (EDP) is an incubator programme founded by the Hungarian Enterprise Development Foundation. Its objectives are to facilitate the establishment of new innovative SMEs, to promote the development of existing small enterprises into medium-sized enterprises and to promote the economic strengthening of already operating medium-sized businesses, their access to foreign markets and the establishment of links to the information economy.

The programme consists of three sub-components. The SME Development sub-programme supports the technological innovation of SMEs and access to foreign markets. It further aims at enhancing quality development and supporting SMEs producing crafts. The bridging sub-programmes aim at strengthening contacts between Hungarian SMEs and at integrating them with large companies in the area of production, innovation and information. The investment promotion sub-programmes concentrate on the development of a service-oriented public administration and provide means for the promotion of direct investment.

Several measures have been introduced to simplify the **business environment** during the reporting period. For example, the administrative procedure for the registration of sole proprietors was centralised by the Ministry of Interior, which took over this responsibility from the economic chambers. Licensing of a number of commercial activities was also centralised in November 2000 and was put under the responsibility of the Office of Approvals and Public Administration of the Ministry of Economic Affairs. In the beginning of 2001, amendments to the taxation regulations were introduced to reduce the burdens on SMEs such as the possibility to extend flat-rate taxation.

Overall assessment

Hungary's SME policy is generally in line with the principles and objectives of EC Enterprise policy. The definition of micro, small and medium sized enterprises is practically in line with the EC definition. The Széchenyi plan, whose implementation started in 2001, should contribute to the continuous sound development of the SME sector in Hungary. It should also help to increase the amount of capital invested in SMEs and the low creation rate of SMEs outside Budapest and the Pest County. However, a good co-ordination between measures under this plan and measures foreseen under other schemes will be necessary.

With a view to boosting entrepreneurial activity, legal and administrative burdens would need to be further alleviated and access to finance made easier.

The department for SMEs in the Ministry of Economics comprises 10 people. Since 2000, an SME target fund is in existence. Its budget was HUF 5.2 billion in 2000 (around € 20 million) and increased to HUF 12 billion (around € 46,1 million) in 2001. These funds mainly go to the

²⁰ Developments concerning SME policy should be seen in relation to the overall enterprise policy, including the industrial policy (see Chapter 15 - Industrial policy).

Széchenyi plan. No budget was planned for staffing or training purposes. The basic infrastructure for the implementation of the SME policy is in place both at national and regional level. However, more efforts could be made to co-ordinate the activities of the different networks supplying business support services and to make them more visible.

Chapter 17: Science and research

Further progress has been made in this area since the last Regular Report.

In 2000, the Government launched a National Research and Development Programme, which is to serve as a long-term development programme for Hungarian science, technology and innovation. It is targeting five main fields: improving quality of life, information and communications technologies, environmental and materials research, research on agribusiness and biotechnology, research on the national heritage and contemporary social challenge.

In order to lower research and development costs of companies, certain further tax benefits were introduced in spring 2001. For this purpose, some € 208 million were made available under the Széchenyi Plan. The Programme helps the continuous development of research and development, the modernisation of the relevant infrastructure and the development of human resources.

A network of National Contact Points and R&D liaison offices, operated by the Ministry of Education, was established at the end of 2000. The active participation of other ministries is ensured by their representation in the programme committees.

During the reference period, Hungary continued to be fully associated with the Fifth Framework Programme as well as with the Euratom Framework Programme.

Hungary has, like the other candidate countries associated with the Fifth Framework Programme, been granted observer status (since May 2001) in meetings of CREST (*Comité pour la Recherche Scientifique et Technique*).

Overall assessment

Hungary's institutional structure of science and research is well established and operates efficiently with qualified staff. It comprises the Science and Technology Policy Council and its Science Advisory Board.

Although gradually increasing, the share of science and research in central budgetary allocations is still relatively small. The low level of salaries in the sector, particularly at the level of junior research fellows, has led to shortage of qualified staff in science and research.

For the further development of the sector and for an effective integration of Hungary into the European Research Area (ERA), it is also important to increase the gross domestic expenditure on research and technological development.

More and more multinationals have been establishing their research centres in Hungary, primarily in the fields of the pharmaceutical industry, IT technology and telecommunications.

The knowledge transfer between the research and business sectors is still at an early stage. The promotion of research and development activities under the Széchenyi Plan aims in particular at enhancing the respective capacities of the SME sector.

Though the financial and institutional framework for association with the 5th Framework Programme is well established, the administrative capacity and infrastructure should be further reinforced, *inter alia* to ensure a successful participation of Hungary in the Framework Programme.

Chapter 18: Education and Training

During the reference period Hungary continued to progress in this area.

In the reference period, Hungary continued to participate in the second generation of **Community Programmes** Socrates and Leonardo, as well as in the new Youth programme (which incorporates European Voluntary Service activities, *see part A.b – Relations between the European Union and Hungary*).

As regards **reforming its education and training system**, there has been progress in the field of upgrading education. An increase in the real value of teacher's wages was ensured. Teachers will receive a total salary increase of 20% from September 2001. However, their salaries are still quite low compared to other public employees.

The Ministry of Education launched a comprehensive programme that should enable the full implementation of the provisions of the **Directive concerning education of children of migrant workers** in time for accession.

Parliament adopted a new loan system for students and, as of September 2001, students are entitled to draw preferential loans to finance their studies.

The Ministry of Education increased resources (€ 12 million) to support schools engaged in the education of socially disadvantaged children (such as young Roma and children living in remote areas with insufficient access to education facilities).

The gradual alignment of vocational training with EU practices and objectives continued. In July 2001, the County Vocational Training Committees were reorganised into seven new Regional Vocational Committees linked to the National Council for the Development of Vocational Training. The aim of this reorganisation is to ensure that funds are effectively targeted at projects that meet regional priorities for the development of vocational training.

Overall assessment

In general, Hungary's legislation is in line with the relevant *acquis*, notably the Directive concerning education of children of migrant workers.

Improving quality and accountability remain top priorities, as emphasised by the accounting mechanisms introduced in the proposed Adult Training Law, which the Government recently presented to the Parliament for adoption. Based on the concept of lifelong learning, the proposed Law aims at providing a single regulatory, accreditation and financial framework covering the whole of the adult training sector.

The framework curricula for vocational education, introduced into all schools in September 2000, provide a framework for the national core curricula and local curricula. Further progress is needed to strengthen the link between the needs of the labour market and the skills acquired by the graduates of vocational schools. Continuing the modernisation of the vocational training qualification system is a Government priority in this area of policy-making.

Chapter 19: Telecommunications and information technologies

Hungary continued to make progress in this area. In particular, there has been greater emphasis on the requirement for cost orientation in telecommunications tariffs to be imposed on certain operators. The *acquis* requires this in certain limited circumstances.

Concerning the **liberalisation of the telecommunications market**, a further positive step to promote competition in the market was the recent auction of five licences for fixed wireless access (3.5 GHz). According to the government, frequency allocation for GSM is now compatible with the *acquis*.

A recently enacted telecommunications law is intended to transpose the 1999 *acquis*. The extent to which the new law aligns Hungarian legislation with the *acquis* still remains to be determined by the Commission.

As regards the **regulatory framework**, Hungary has succeeded in implementing some parts of the EU regulatory regime under existing powers, without waiting for the new law.

As regards **postal services**, there has been little progress in terms of alignment to the *acquis*. A new liberalisation policy for the postal market, including the Universal Service obligation in conformity with the EC Directives, is currently being developed.

Over the reference period postal services were further modernised and operating figures improved even if the staff numbers employed remain very high (the company is the country's second largest employer). In addition, further security measures were introduced in order to decrease the risk of robberies. Conversely the traffic rate per inhabitant is one of the highest in the CEECs.

Overall assessment

Hungary's legislation in this sector is already partially in line with the *acquis*. Efforts should now focus on alignment with remaining key parts of the *acquis*, such as those related to interconnection, leased lines, competition through carrier selection and number portability and unbundling of the local loop.

The country's approach to developing the telecommunications sector through the concessions granted in the early 1990s was successful in attracting large-scale foreign investment. This, and the licensing of mobile operators have contributed to a considerable improvement in the size of the infrastructure and the quality of services available. Moreover, by deciding to sell the whole of the state's shareholding in the incumbent operator, Hungary avoided the problems that often arise from lack of clear separation of the state as regulator from the state as operating company. There has been considerable activity in the liberalised part of the market, but the monopolised part is still very large.

Hungary has been relatively slow in completing transposition and implementation of key parts of the *acquis*, notably those related to interconnection, leased lines, competition through carrier selection and number portability and unbundling of local loop. This should now become the main focus of action, to ensure that the rest of the market is opened as soon as possible and is properly regulated. In addition, rapid progress will now be needed to ensure that the new law on telecommunications is implemented in time for the liberalisation of the market foreseen in January 2002. If the market opening measures are to be effective, it will be important well before this date to ensure that any necessary licences are issued, that vital facilities, such as call-by-call carrier selection, are available on demand and that effective procedures are available for the resolution of interconnection disputes. Any delay in these areas would be damaging to the market. In addition to interconnection of fixed networks, outstanding issues include alignment with the *acquis* for universal service.

The Communication Authority is legally separate from and independent of the ministries and other governmental organisations holding stakes in the operators. It has a separate budget line and full jurisdiction and nation-wide competence in licensing telecommunications equipment, networks and non-concession services, including the postal services. It carries out its activities under the supervision of the Government Commissioner. In the telecommunications area, the regulatory authority manages scarce telecommunications resources (frequencies, numbers, etc.), prepares system regulations to ensure technical and traffic integrity of the national telecommunications networks, as well as market regulations to set the rules for new entrants and promotes fair competition among service providers.

One of the important activities of the Authority is market surveillance. It monitors the market players and services, and elaborates up-to-date methods for conformity assessment of telecommunications and postal services, as well as their requirements and documentation. It collects, processes and assesses significant market data, and forwards the results of the assessment to the competent international organisations as well as informing the public.

The new institutional arrangement in form of a Government Commissioner responsible for telecommunications regulation, governmental informatics, the information society and postal services has worked well and has helped Hungary maintain its seminal role in Information Society matters. The Hungarian Communications Authority is due to be restructured to take account of the recently enacted law. These changes are needed to ensure that regulation of the telecommunications market is fully in line with the *acquis*.

The Communication Authority, as a regulatory authority, also monitors the market, examines changing social expectations towards postal services, and deals with pricing. It regulates the management of scarce postal resources (e. g. postal codes), monitors international postal standardisation, takes part in the standardisation activity of international organisations and initiates the introduction of international standards in Hungary. It defines the fundamental principles of postal service quality assessment and quality requirements, and participates in the preparation of national and European qualifying standards. The Authority promotes the preparation of postal standards (to be issued by the Hungarian Standardisation Body) and participates in the international and regional standardisation organisations.

As for the incumbent postal operator (Hungarian Post Company) and telecommunication service provider (MATÁV), the State's ownership and regulatory functions are separated. The ownership rights of the State are exercised by the Ministry of Transport and Water

Management. National policy-making and postal regulation belong to the responsibilities of the Office of the Government Commissioner.

Chapter 20: Culture and audio-visual policy

No further progress in aligning with the **audio-visual** *acquis* can be noted since last year's Regular Report.

In April 2001, the Government submitted a revised proposal to amend the 1996 Act on Radio and Television Broadcasting, which aims to align with the *acquis* in a large number of areas. However, Parliament has not yet adopted the law, which requires a two-thirds majority and which has been pending for more than two years.

In the field of **culture**, Hungary has continued to strengthen the structures necessary to participate in Community structures. The decision of the Association Council on the participation of Hungary in the "Culture 2000" programme was adopted by the Government and entered into force in July 2001.

Overall assessment

Hungary's legislation is still not fully aligned with the *acquis*, given that the adoption of the Media law by the Parliament is still pending.

Parliament has made the adoption of the Media Law dependent on a compromise to be found on the supervision of the public service media (Hungarian Radio, Hungarian Television and Duna TV) by the Presidiums of the Boards of Trustees. The three Presidiums continue to be composed of solely pro-government members. Despite initiatives taken, Parliament was not able to settle the issue as would be required for the adoption of the new law, which needs a two-thirds majority.

Hungary has ratified the Council of Europe Convention on Transfrontier Television and will be bound by its amending Protocol upon the date of entry into force.

The National Radio and Television Board of Hungary is the national regulatory and monitoring body in audio-visual matters. It has monitoring and sanctioning powers and is independent of the executive; the 7 members of the Supervisory Board are selected by Parliament. The staff (comprising 110 members in 2000) runs daily operations and supports the Board. In November 2000 a new unit comprising 2 staff members was set up, the Strategy Directorate. Its main purpose is to formulate strategies and positions to support the Board and currently to follow the state of play regarding the New Media Law (Amendment of Act 1996) pending its adoption by Parliament .

Chapter 21: Regional policy and co-ordination of structural instruments

Since the last Regular Report, Hungary has made progress in preparing for the implementation of structural policies.

No new developments are to be reported regarding Hungary's territorial **organisation**.

Hungary has further adapted its **legislative framework** and has defined the **institutional framework** with regard to programming and implementation of Structural and Cohesion Funds. This includes Government decisions on the establishment of the future managing authorities and the co-ordination of individual Structural Funds. The responsibility for planning and programming remains with the Ministry of Economy while the Office of the Minister without portfolio responsible for Phare has been entrusted with the responsibility of setting up the managing authority for the Community Support Framework. The paying authority or authorities have not yet been designated.

In order to sustain the new programming process and prepare for the future management of Structural Funds, Hungary is reinforcing the relevant ministries and agencies. Over 200 civil servants from all the relevant ministries have been trained. The Ministry of Economic Affairs has allocated additional staff to programming tasks and in April 2001 a new department was created to deal with accession-related institution building and to make proposals concerning the organisation of the Ministry in relation to the management of Structural Funds after accession. Within the Ministry of Agriculture and Regional Development, the Regional Development Department has been strengthened. The department is in charge of co-ordinating the regional elements of the programming process and establishing the future managing authority for the Regional Development Operational Programme.

The Government also strengthened the “National Agency for Regional Development” and established a European Social Fund Implementing Agency, which has started functioning, with a staff of 12. Other relevant agencies are placed under the responsibility of the Ministry of Economy. The Implementing Agencies established in the Ministry of Transport and Water Management and in the Ministry of Environment for the implementation of ISPA will be in charge of the implementation of the future Cohesion Fund (*see also Section A.b - Relations between the European Union and Hungary*).

With regard to **programming**, Hungary submitted the final version of the preliminary National Development Plan (pNDP) in April 2001. This document is effectively used as a basis for programming and co-ordinating pre-accession assistance.

Under the overall responsibility of the Ministry of Economy, the preparation of a development plan (referred to as “National Development Plan - NDP) within the meaning of the Structural Funds regulations started in January 2001. The co-ordinating body for the development plan is the Inter-ministerial Committee for Development Policy Co-ordination. A National Development Plan Task Force was set up as part of the Planning Sub-committee of the Inter-ministerial Committee. Five working groups support this task force, in the following areas: regional development, economic development, agriculture and rural development, infrastructure, and human resource development.

In the context of this new exercise, Hungary decided to prepare a limited number of operational programmes, including a single, centrally managed Operational Programme for Regional Development. This simplified structure should facilitate both absorption and effective implementation of the Funds in the shortened programming period until 2006.

In order to ensure the application of the **partnership principle**, the Economic Council (including the social partners), the National Regional Development Council (which includes the presidents of the Regional Development Councils) and the National Environment Protection

Council are being consulted in the preparations of the plan. One representative of the regions participates in each of the five thematic working groups of the National Development Plan.

Concerning **monitoring and evaluation**, the *ex-ante* evaluation of the development plan and a macro-economic impact study are being prepared. An evaluation sub-committee of the Inter-ministerial Committee for Development Policy Co-ordination has been established. A pilot IT monitoring system has been created, with Community assistance, in the Government Control Office.

Preparations for the **financial management** of the Structural Funds and the Cohesion Fund are based on the financial management system established for the pre-accession instruments.

The legal framework for the **financial control** for public expenditure has been established and the necessary internal and external control bodies have been set up. The Ministry of Finance has been given the responsibility for the overall regulation, supervision and development of the areas of public finance, the treasury system, public internal financial control, and financial audits, including the co-ordination of measures necessary for the consistent implementation of the *acquis*, as well as for the co-ordination with Community Institutions.

As concerns **statistics**, data required for determining areas eligible for Community Support are provided by the Hungarian Central Statistical Office, through the Territorial Information System.

Overall assessment

Programming of Structural Funds is proceeding well in Hungary. Concrete steps have also been taken concerning the definition of implementation structures, but considerable efforts are still required in order to develop the administrative capacity required for managing the Structural and Cohesion Funds. Regarding the territorial organisation, Hungary has confirmed its decision to maintain the existing provisional NUTS classification agreed with EUROSTAT in July 1997.

As a matter of priority, the future paying authority or authorities need to be designated and the role of the line ministries, 'agencies' or other bodies due to act under the responsibility of the future managing and paying authorities needs to be defined. There is also a need to clarify the role of the future Community Support Framework managing authority and its relationship with the future managing authorities of the operational programmes as well as with ministries responsible for specific policy areas or for 'co-ordinating' individual Funds (e.g. the co-ordination of European Social Fund interventions in the context of the European Employment and Social Inclusion Strategies). Above all, the administrative capacity of the units within the ministries designated or to be designated as future managing or paying authorities needs to be considerably strengthened in order that they will effectively be able to take on the responsibility for the efficiency and correctness of the management and implementation of Structural Funds.

With regard to the crucial issue of developing the required administrative capacity at all levels, the current division of tasks between the Ministry of Economic Affairs (responsible for programming and negotiations as well for co-ordinating the European Regional Development Fund and the European Social Fund and managing two of the future operational programmes) and the Office of the Minister without Portfolio dealing with Phare (responsible for the establishing the managing authority of the Community Support Framework) requires a particularly high level of co-operation of the two ministries in order to work effectively.

Substantial progress is also needed at the level of the technical preparation of projects to be co-financed by the Structural and Cohesion Funds.

The programming process that will lead to the preparation of the development plan and the draft operational programmes as required by the Structural Fund regulations is firmly under way. Procedures should be further streamlined in order to avoid duplication of structures. In order to match sectoral and regional approaches, inter-ministerial co-operation and partnership need to be made more effective and comprehensive, both at national and regional level. Genuine partnership structures at regional level, including the regional and local authorities and other competent public authorities, the economic and social partners and any other relevant bodies (e.g. minority groups) should be established, and a strong input of the regions into the programming process taking place at national level should be ensured.

As to the monitoring and evaluation system, further work on ensuring compliance with the *acquis* requirements is still necessary, in particular as regards the *ex-ante* evaluation of the development plan and the collection and processing of the relevant statistical information and indicators. The existing pilot IT system needs to be extended to the whole future implementation structure for the Structural Funds. The timely functioning of an effective monitoring and evaluation system will be of crucial importance for the effective and efficient implementation of the Structural Funds programmes.

In relation to financial management and control, Hungary needs to ensure that the necessary legislative framework is in place for the co-financing of Structural and Cohesion Funds, including provisions for transfer of funds during its implementation. The procedures concerning payments to project beneficiaries, currently centralised in the Treasury, need to be reviewed with a view to managing substantially larger amounts of projects and payments. Appropriate systems and procedures for financial management and control need to be established, in particular in relation to the structure of the managing and paying authorities, in order to fulfil the specific requirements of the Structural Funds regulations.

As to regional statistics, further efforts are necessary to bring them up to the level required for regional policy planning and programming, in particular *ex-ante* evaluation. Hungary still needs to improve the system for the collection and processing of relevant statistical information for the purpose of *ex-ante* evaluation.

Chapter 22: Environment

Since the last Regular Report, Hungary has made significant progress in this area, notably through the adoption of legislation on the Environmental Impact Assessment, on water, waste, industrial pollution control and risk management, chemicals and radiation protection.

With regard to the **integration of the environment into other policies**, Hungary continues to make broad use of the Environmental Council, an advisory body to the Government, bringing together several authorities on environment, to promote and enhance environmental policy, whilst trying to achieve integration of environment in other policies.

In the field of **horizontal legislation**, further progress was made in April 2001 with the adoption of legislation on environmental impact assessment regulating the assessment of the effects of certain public and private projects. By ratifying the Convention on Access to

Information, Public Participation in decision-making and Access to Justice in environmental matters (the Aarhus Convention) in May 2001, Hungary made further progress in implementation of relevant parts of the environmental *acquis*.

As regards **air quality**, Hungary aligned its legislation with the quality of ambient air Directive and its daughter Directives on limit values of sulphur and nitrogen dioxides, nitrogen oxide, particulate matter, lead, benzene and carbon monoxide as well as in relation to the exchange of information and data regarding air pollution with Member States. It has also ratified the Gothenburg Protocol to the 1979 Convention on long-range Transboundary Air Pollution on Further Reduction of the Sulphur Emissions. The development of an air monitoring system and a data reporting system at the national level is in progress. There are some 44 monitoring stations, out of which 28 are located in cities. An air quality database was established at the Institute for Environmental Management to ensure uniform data supply in the context of the different reporting requirements. The Institute is also responsible for quality assurance and quality control.

In the area of **waste** management, further alignment was achieved with the adoption of implementing legislation for the Law on Waste Management. In particular, the following areas were covered during the first quarter of 2001: public service providers for waste management and public service contracts, calculation of fees for municipal waste management services, categories of waste and hazardous waste treatment; whereas full transposition has been achieved in relation to disposal of waste oils, disposal of PCB/PCT, use in agriculture of waste water and sewage sludge and the treatment thereof, and the handling of batteries and accumulators. A Ministerial Decree on the list of wastes was issued, which will enter into force in January 2002. In October 2001, Hungarian legislation was aligned with the EC landfill Directive.

In December 2000, Hungary signed the Basle Protocol on liability and compensation for damage resulting from the transboundary movement of hazardous wastes and their disposal.

A computerised register of authorisations concerning waste management was set up under the municipal solid waste programme and four modern regional landfills serving 51 municipalities were established.

Several training programmes have been launched for local government and environmental authorities to facilitate the implementation of the new 2000 Act on Waste Management. The number of staff at the Ministry for Environment, at the National Inspectorate for Environmental Protection and Nature Conservation and at the 12 regional Environmental Inspectorates dealing with waste management issues has been increased.

In the field of **water quality**, a detailed national programme for the implementation of the respective *acquis* was drawn up in June 2001. Sensitive areas were designated in January 2001 for the purpose of wastewater collection and in May 2001 the law was fully aligned with Community legislation on nitrates pollution from agricultural sources. Furthermore, in October 2001 national legislation was adopted transposing the Directive on the discharge of dangerous substances into the aquatic environment. In the reference period, in addition to the three already existing monitoring stations, two surface water-monitoring stations were established (River Drava and Danube) and the monitoring network for ground water quality was expanded. The

number of staff dealing with surface water and groundwater was increased in the relevant departments of the Ministry for Environment and at the Environmental Inspectorates.

As regards **nature protection**, some progress was made concerning the alignment in relation to the protection of wild birds. Prohibition of capture, killing, disturbance, transport, trade, etc. of species was also extended to all protected species (Annex IV of the 1992 Council Directive on the conservation of natural habitats and of wild fauna and flora), as well as to all wild birds in Europe by new legislation in May 2001. An assessment of suitable sites for the conservation of natural habitats and of wild fauna and flora and of special protection areas (SPA) is being carried out.

In March 2001, Hungary fully aligned with Community legislation in relation to the establishment, operation and maintenance of zoos and other facilities for animal keeping.

As regards **industrial pollution control and risk management**, Hungarian law was aligned with the 1996 Directive on the control of major-accident hazards involving dangerous substances in June 2001, but did not yet enter into force. The Competent Authority (National Authority) is being established in the framework of the National Directorate General for Disaster Management of the Ministry of Interior. The *acquis* on the limitation of volatile organic compounds due to the use of organic solvents in certain activities and installations was harmonised in July 2001. Thus, all installations for which an application for authorisation was submitted after April 2001 will be subject to the requirements of the *acquis* immediately. In October 2001, Hungarian legislation was brought fully in line with the IPPC Directive.

In the field of **genetically modified organisms and chemicals**, the following areas were further aligned with the *acquis* during the first months of 2001: dangerous substances, and in particular their marketing and use, classification, packaging, labelling, export and import; chemical safety, and in particular the operation of the inter-ministerial committee, chemical load fines, restrictions on their marketing and use, and assessment of risks to man and the environment; and the prevention of environmental pollution by asbestos.

Concerning **noise**, a new information system is being created within the framework of Hungary's noise strategy, which will incorporate data from industrial and commercial operations and from traffic. Alignment with the Directive on noise emissions of outdoor equipment has been achieved and the relevant Government Decree will enter into force in January 2002. Alignment also has been achieved in relation to airborne noise by household appliances with a Government Decree that will enter into force in January 2002.

In the field of **radiation protection** (*see also chapter 14 – Energy*), Hungary has aligned its legislation in relation to the supervision and control of shipments of radioactive waste between Member States and into and out of the Community, protection of outside workers from ionising radiation and protection from individuals from ionising radiation due to medical exposure.

In the reference period, the administrative capacity of the Ministry of Environment was strengthened and the overall number of staff increased.

Environmental investments in Hungary have increased from € 513 million in 2000 to € 627 million for 2001 and € 666 million for 2002 according to the two-year budget. The share of environment investments in GDP has reached 1-1.1%. The bulk of the environmental

investments is spent for the protection of surface and ground waters (40%), the reduction of waste (30%) and air quality (20%).

Overall assessment

Hungary has achieved a very high level of alignment with the environmental *acquis*. Previous delays in the ambitious transposition schedule were made up over the last year.

Hungary has also prepared the necessary implementation programmes in the field of air, waste, water and industrial pollution. These programmes need to be continuously up-dated and, if necessary, added to as implementation proceeds.

In the area of horizontal legislation, further measures still need to be taken to ensure better access to environmental information and to improve the reporting requirements.

In the area of air quality, legislation should be adopted to achieve harmonisation with the relevant Community environmental *acquis*, including the adoption of legislation on the substances that deplete the ozone layer.

In the area of waste management, further efforts are needed concerning the harmonisation with Community legislation concerning the management of hazardous waste, shipment of waste in and from the EC and packaging and packaging waste. The National Waste Management Plan, establishing the intermediary collection and recovery targets that are necessary for the attainment of the corresponding Community targets set by the *acquis* still needs to be approved by the Parliament. The plan is to be completed in order to comply with the requirements of the Waste Framework Directive by regional Environmental Inspectorates and local governments respectively.

Waste disposal facilities at municipal level and for hazardous waste will need to be extended. Out of the 728 registered landfills, only six are so far in line with the *acquis* and a further 67 seem to be aligned to a large extent. In particular, a great number of low capacity local landfills are not in conformity with the *acquis* and there exists a large number of illegal ones. Measures should be taken for the closure of all illegal ones and of all those not complying with the *acquis*, paying attention that the closed landfills are not themselves harmful to the environment.

In the field of water quality, legislative efforts should be made to harmonise with the Community Directives on drinking water, bathing water, surface water for abstraction for drinking water, measurement and sampling of surface water and quality of fish water as well as with the daughter Directives the Directive on discharge of dangerous substances into the aquatic environment. Although water quality monitoring in Hungary meets the requirements of the law currently in force, in order to comply with all the requirements set by the Water Framework Directive, further developments will be necessary. Capacity building is also planned in the sector of water protection. The inventory of List II substances within the framework of the Directive on the discharge of dangerous substances into surface water should be drawn up as soon as possible, in order to allow for the establishment of the relevant pollution reduction programmes before accession.

In the field of nature protection, legislation concerning the use of animals in laboratories for experimental purposes and the use of leghold traps have already been aligned with the *acquis*.

Special Protected Areas (SPA) for the protection of birds (part of Natura 2000) still have to be established by law before accession. Considerable staff increases are needed, within both the national park directorate headquarters and the nature conservation authority.

In the field of industrial pollution control and risk management, the implementation of the Integrated Pollution and Prevention Control Directive (IPPC) should be taken further, which will entail considerable administrative efforts as well as requiring the revision of the Hungarian environmental permit system. In this respect, the newly adopted Act amending the Environment Act introduces the concept of an integrated permit. In order to ensure the implementation of the transposed IPPC directive, a separate unit has begun operations in the Institute for Environmental Management, an institution linked to the Ministry for Environment. The unit should facilitate the drawing up of the necessary national registers and guidance notes. Legislation on hazardous waste incineration to align with the corresponding EC directive should be enacted. In the field of chemicals and genetically modified organisms, legislative efforts should be made to transpose Community legislation on asbestos, biocides and genetically modified organisms. Particular efforts should be also made to establish the necessary bodies to implement the legislation on chemicals and genetically modified organisms.

The 1999 Law on Management and Organisation for the Prevention of Disasters and the Prevention of Major Accidents involving Dangerous Substances provides the framework for civil and radiation protection. Hungary still needs to join the ECURIE system and to make further progress in harmonising with the *acquis* in this field (certain issues of temporary and final depositing of radioactive waste, and alerting and informing the public in case of an emergency).

Hungary should continue to integrate environmental protection requirements into the definition and implementation of all other sectoral policies with a view to promoting sustainable development.

With regard to the administrative capacity, the responsibilities for environmental protection are divided between six different Ministries, each of which has various implementing bodies at regional and national level. However, there are no clear responsibilities and clear division of competencies amongst them. Environmental tasks are fragmented, all concerned authorities have their own specific and exclusive permitting, compliance checking and enforcement tasks; no general regulatory system exists, but instead there are several small independent ones. There is regional as well as sectoral fragmentation, and a significant amount of unnecessary work. A rationalisation of the whole system should be carried out, otherwise serious implementation problems can be expected. Although the administrative capacity in the Ministry of Environment has improved, it seems that the Legal Department still needs further strengthening.

Inspectorates have too many tasks to carry out (altogether 19 are listed). A wide range of ministerial organisations are involved in the licensing procedures, which need to be streamlined. The 12 regional inspectorates and the 8 national park directorates are first instance bodies. The Chief Inspectorate is the second instance body, which, however, also issues permissions. The Chief Inspectorate is a ministerial office with an independent budget line, acting at the national level. It issues licences on import/export of hazardous waste, for instance. The regional inspectorates are governmental bodies with a separate budget, acting at regional level. They are responsible for environmental permits. The division of tasks and competencies between the Chief Inspectorate and the Regional Inspectorates should be rationalised and made more

flexible and transparent. More staff, or better allocation of staff, is needed at both central and regional levels to ensure adequate monitoring and enforcement of the legislation.

Concerning enforcement in particular, penalties and fines should be revised in order to provide a real deterrent for polluting installations. Judges should be trained in Community environmental legislation.

Chapter 23: Consumers and health protection

During the reference period some progress was made in this sector in terms of legal alignment.

However, no particular progress can be reported with respect to **safety related measures**.

Existing legislation in the **non-safety related measures** field was amended in various areas with the aim of improving alignment with the *acquis*. In particular, provisions relating to Directives on Consumer Credit, package travel, holidays and tours and comparative and misleading advertising were introduced. While the amended legislation on consumer credit entered into force in January 2001, the Government Decree on package travel, holidays and tours has been applicable since April 2001 and the legislation on comparative and misleading advertising has been in force since March 2001. New legislation aligning the Directive on indication of the prices of products and services offered to consumers entered into force in September 2001.

No relevant progress has been made either with promoting a more efficient institutional structure to implement consumer policy or with the modernisation of **market surveillance**.

Overall, **the institution in charge of consumer protection** is the Ministry of Economic Affairs, assisted by other Ministries in the areas of their competence (justice, health, agriculture, environment and transport). The Office of Economic Co-operation is in charge of procedures against unfair manipulation of consumer choice. The General Inspectorate for Consumer Protection is responsible for enforcement of consumer and health protection. Under its co-ordination and management, a Central Market Surveillance and Information System started functioning in January 2000. To facilitate the functioning of the Information System, during 2001 the Inspectorate concluded various co-operation agreements with the other authorities that carry out market surveillance.

The Co-ordination Secretariat of the **TRAPEX** system (Transitional Rapid Exchange of Information System) connecting the market surveillance authorities of Central and Eastern European applicant countries is located in Hungary and operates from the premises of the General Inspectorate for Consumer Protection.

The **Arbitration Boards**, created in 1997, started working at full capacity in 2001. They received financial support from the central budget and the Ministry of Economic Affairs and handled 420 cases and disputes in 2000.

In the course of 2000 and 2001, the General Inspectorate for Consumer Protection contributed to activities relating to **education and information of consumers** through the issuing of general publications and specialised material and textbooks for consumer protection training. Financial support from Government targeting **civil organisations** specialising in consumer protection amounted to more than HUF 100 million (around € 385 000) in 2000. In 2001 about HUF 70

million (around € 269 000) should be available for this purpose. A total of nine civil organisations are at present active in the field of consumer protection in Hungary.

Overall assessment

Subject to a detailed assessment of the recently adopted legal provisions by the Commission, Hungary's legislation appears to be largely in line with the *acquis* in the areas of misleading advertising, consumer credit, indication of prices, and package travel, holidays and tours.

Further alignment is needed as regards general product safety, liability for defective products, distance contracts, injunctions for the protection of consumer interests, and certain aspects of the sale of consumer goods and associated guarantees.

The various structures created to implement consumer protection policy are functioning smoothly. However, further efforts will be needed with regard to staff, training and financial resources. Moreover, the relevant authorities at present devote most of their efforts to ex post controls, such as quality testing based on consumer complaints, instead of establishing an effective market surveillance system to prevent the sale of faulty, dangerous, mislabelled or expired products.

The existing system for out-of-court dispute settlement represented by the Arbitration Boards needs more support from the Government, and the Boards' members should get specific training so as to facilitate the efficient settlement of disputes.

Further support for consumer organisations is needed in order to enable them to protect consumer interests effectively.

Progress also remains to be made with enhancing consumers' and producers' awareness of their respective rights and responsibilities.

Chapter 24: Justice and Home Affairs

Since the last Regular Report, progress has been registered in Hungary in numerous fields such as visa policy, migration, asylum, the fight against organised crime, corruption, drugs and judicial co-operation.

In the area of effective personal **data protection**, a National Supervisory Body has been set up for the activities of NEBEK, which is the counterpart authority for Europol and the Schengen Information System.

As to **visa policy** new visa obligations have been introduced for Belarus, Bosnia-Herzegovina, Moldova, FYROM and Russia. Concerning the uniform visa format, the new Law on Entry and Stay of Foreigners adopted in May 2001 provided for new visa stickers further aligning with the *acquis*. The law that will be introduced in January 2002 also provides for the exchange of personal data between the co-operating aliens policing authorities and ensures alignment with the requirements of the Common Consular Instructions. These provisions will, however, only be applicable upon accession. The Hungarian on-line system to support the visa procedure has been extended offering access to 59 diplomatic and consular. 77 out of 91 consular missions received equipment for the detection of forged documents, with devices corresponding to

standards set by the *acquis* for low risk countries, while 10 missions have been supplied with devices supplemented by infra-red cameras and monitors.

Hungary has initiated local consular co-operation in certain third countries with their visa partners (France and Portugal) and instructed all its missions to participate in EU consular co-operation wherever possible. Staff of the office of immigration and naturalisation has been further increased.

In the area of **external borders**, a strategy on the integrated development of border crossing points was adopted in January 2001. It foresees the modernisation of 46 priority border crossing points (at the Ukrainian, Yugoslav and Croatian borders) with participation of all bodies concerned (the Border Guard, Customs and Finance Guard, Veterinary and Phytosanitary services). Concrete steps mentioned in the plan include institution-building measures, training and an increase in staff. Furthermore, the Hungarian Government drew up a **Schengen** Action Plan in March 2001, which addresses the main issues of the *acquis*.

On the institutional side, the infrastructure at the borders has been further modernised and upgraded. New infrared surveillance equipment, fast patrol boats, patrol equipment and criminal investigation devices have been deployed since June 2001. The off-road patrol vehicle fleet was replaced and increased in 2000. In May 2001, the Hungarian Parliament adopted a law distinguishing between internal and external borders in line with the Schengen requirements. Certain elements of the Law will however only enter into force, once Hungary is entitled to eliminate border controls at the future internal borders. Negotiations for bilateral agreements on border traffic control with neighbouring countries are under way.

The installation of the border register system has been completed at all land border control points that are open regularly and at the international air border crossing point. As a result, there was a significant increase in the numbers of illegal migrants and vehicles detected. A common border contact point was opened at Hegyeshalom in June 2001 following a bilateral agreement with Austria. This should facilitate border traffic and migration matters.

In 2000, some 87 million border crossings were registered, including 32 million vehicles. 16,500 illegal border crossings, 600 traffickers, and 2,900 instances of official document forgery were detected, representing an increase of 6% against 2000. Nevertheless there is still a considerable problem of illegal crossborder traffic, and work should continue on strengthening the control of future external borders, namely the borders with Ukraine, the FRY and Croatia. In 2000, due to the automated border crossing system, the checking of passengers has become quicker and more accurate.

The Hungarian Border Guards currently number 11,000, and efforts should be maintained to reach the target of 14,000, established by the Government. Training in *acquis*-specific issues as well as in languages for the border guards has continued. Moreover, the Hungarian Government has taken the first steps to improve the career system and the pay of civil servants, including law-enforcement staff.

As far as **migration** is concerned, progress was achieved with the new Law on Entry and Stay of Foreigners of May 2001 in connection with the admission of third country nationals for study, employment and family purposes and a standard travel document for the expulsion of third country nationals. The new Law further introduced the unified residence permit. In 2000,

34,017,070 foreigners entered Hungary legally, 32,762 persons held a permanent residence permit and 25,749 a temporary residence permit.

The law also simplified expulsion rules. Simplified expulsion is applicable to foreigners who have entered Hungary illegally, if there is a possibility of using a readmission agreement and the person concerned has been arrested within 15 days of the illegal entry. Moreover, under these agreements persons must be readmitted within 30 days.

Hungary has concluded new readmission agreements with Albania and Portugal. Further agreements are under preparation with Estonia, Latvia, Lithuania, FYROM, Yugoslavia, Moldova and Greece.

Hungary continued to be a target country for **asylum** seekers. In 2000, the overall number of asylum seekers dropped from 11,500 to 7,800. However, the number of asylum-seekers from non-European countries increased by 6%. Most came from Afghanistan, Iran and Bangladesh. In 2000, 197 persons were granted asylum, 680 persons were authorised to stay and 2,930' persons claims were rejected in ordinary procedure. 48 persons' petitions were rejected as manifestly unfounded claims and 4,916 persons' cases were dismissed. Some 2,541 applications were received in the first quarter of 2001, with some 50% processed already. The backlog in handling asylum applications has been reduced, and since mid-2000 the procedural deadlines set by the Asylum Law have generally been respected. Despite this positive trend, illegal migration had risen in 2000.

In May 2001, the Hungarian Parliament adopted a revised Law on Asylum bringing alignment to a large extent with the *acquis*, in particular for the definition of unaccompanied minors. It also provided the framework for the future implementation and application of the Dublin Convention. It further reduced the duration of the asylum procedure by entitling the asylum authority to decide on the expulsion of asylum applicants, whose applications had been rejected. Appeals can be lodged at the authority within 15 days of the decision.

The overall living conditions in the reception facilities for asylum seekers have been further upgraded over the reference period in line with a plan established by the Office of Immigration and Naturalisation.

In total, 61 staff work on asylum procedures, and 32 staff decide on the hearing procedures. In order to further speed up procedures on decision-making, staff at the Office of Immigration and Naturalisation was increased by 25. Appeals against the decisions made by the asylum authorities can be made at the Budapest Metropolitan Court and the Supreme Court. On average 60 to 70 new appeal cases have been lodged each month.

Training also continued for the staff involved. In 2000, 5,562 law enforcement agents participated in professional training and 3,473 in language training, compared to 929 and 206, respectively, in 1999.

Hungary continued to develop the **police co-operation** with its neighbouring countries and the EU Member States. A Co-operation Agreement between Hungary and the European Police Office (EUROPOL) was signed in October 2001. The International Law Enforcement Co-operation Centre established in 2000 was identified as the national contact point in Hungary. Internal liaison officers were delegated to the Centre by the Customs and Finance Guard, the Border Guards, the Tax and Financial Control Office, as well as by the Organised Crime

Directorate of the National Police Headquarters. However, communication between regional and national level is rather weak, and further efforts are needed to improve communication between the various agencies.

In accordance with the law on establishing the Co-ordination Centre against **Organised Crime**, co-operation between the national security services and the joint investigating authorities has been reinforced. A co-ordinating body was set up which consists of the deputy heads of the Customs and Finance Guard, Border Guards, Tax and Financial Control Office and each of the national security services, representatives of the Chief Public Prosecutor's Office and the National Council of Justice. It is chaired by the Criminal Director of the Hungarian National Police Headquarters. The Centre has been operational since April 2001 under the supervision of the Minister of Interior. The Centre collects, analyses and processes organised crime related information and intelligence received from all law enforcement service responsible for prevention, detection, suppression and investigation of this kind of criminal offence. The main tasks of the Centre are to co-ordinate the investigations and to prevent and avoid overlaps among investigative services.

In the area of the **fight against fraud, corruption and money laundering**, Hungary has further aligned its legislation with the *acquis*. A new anti-corruption strategy providing for additional legislative and practical measures has been adopted by the Government (*see Section B.1.1. - Democracy and the rule of law*). The amended penal code introduced criminal liability of heads of businesses in connection with bribery of foreign public officials and fraud affecting the European Communities' financial interests. Furthermore, the concept of passive bribery of foreign national public officials was made punishable. As a result, public officials of international organisations and officials of a foreign country will have to face the same punishment as Hungarian public officials in case of both active and passive bribery. In November 2000, Hungary ratified the Council of Europe Criminal Law Convention on Corruption.

In the area of **money laundering**, the Government submitted a bill to Parliament in October 2001, which aims at strengthening the fight against money laundering by accelerating the conversion of anonymous savings books into registered accounts. It would also tighten regulations and identification and reporting requirements with respect to beneficial ownership, funds handled by non-financial institutions such as certain liberal professions, the transfer of cash across the border and currency exchange.

Staff at the Security Service of Law Enforcement Agencies of the Ministry of Interior that is responsible for the prevention, detection and investigation of corruption cases within law-enforcement agencies have been increased by 86%. A new work programme has been adopted for the prevention of corruption of staff of law-enforcement and public-safety services. Within the police, a specialised mobile unit has been set up to detect street corruption of police officers. Their tasks include detecting and reporting of officers taking bribes from citizens and starting disciplinary action or criminal proceedings against them. In 2000, a total of 800 such cases were detected, 200 of them by this unit. Training in this area also continued. In order to strengthen the fight against money laundering, the Financial Intelligence Unit within the Hungarian National Police was further strengthened through the recruitment of additional staff.

Regarding **drugs**, in December 2000 the Hungarian Parliament adopted a new comprehensive strategy, for the implementation of which HUF 17 billion (around € 65.4 million) was made

available in 2001. The strategy describes the long-term tasks of strengthening means of criminal law, prevention, and social action needed to effectively address drug-related problems. Furthermore, it aims at reinforcing prevention, rehabilitation and medical institutions. The programme extends to drug-addicts as well as children and young people in general, their relatives, local and urban communities and the public. The chairman of the committee is the Minister of Youth and Sports.

Training of staff involved has continued as have preparations for participation in Reitox, the European information network on drugs and drugs addiction. Co-operation in the public health field has been increased. A National Contact Point on Co-operation and Information Exchange with the Law Enforcement Network of the Union and the International Police Organisation has been set up. It falls under the competence of the National Police Headquarters.

In the area of **customs co-operation**, Hungary already has bilateral agreements on mutual assistance with a number of Member States. Training of customs officials has continued, focussing on customs and excise administration, criminal law and criminal procedures. The IT system has also been further up-graded (for more details see also *Chapter 25 - Customs Union*). To increase the efficiency of customs co-operation, the Hungarian Customs and Finance Guard has signed memoranda of understanding with several organisations, private and commercial entities. The information gained from this co-operation is used as a primary source for risk analysis.

In the area of **judicial co-operation**, provisions on International Private Law were adopted in 2000 in accordance with the rules laid down by the Brussels Convention in the areas of jurisdiction, mutual recognition and enforcement of judgements. The Central Authority is the Ministry of Justice. The prosecutor's office and the courts also participate in co-operation.

Overall assessment

Overall, Hungary has reached a high level of alignment with the *acquis*. However, further efforts are needed to ensure full adoption and practical implementation of the *acquis* in this area.

With a view to guaranteeing effective personal **data protection**, Hungarian legislation is already aligned to a large extent. This also encompasses legislation in the areas of criminal co-operation and the fight against organised crime.

Continued efforts were made to align the Hungarian **visa** regime with that of the EU. However, further efforts are still needed to align with the *acquis*, in particular as regards visa obligations and visa-free travel.

Further progress has been made as regards **external borders**. However, continued efforts are necessary in particular as regards the border management infrastructure relating to equipment and staff. At green and blue borders, control should be improved and made more efficient. Finally, additional efforts are needed to facilitate the exchange of information, as currently border crossing points are not directly linked with national headquarters.

As regards Hungary's agreements on simplified border crossing with its neighbours, this kind of agreement is not in harmony with the *acquis*. Hungary will need to take the necessary steps to remedy this situation.

Practical co-operation between the Hungarian Border Guards and their Romanian, Ukrainian and Yugoslavian colleagues is increasingly hampered by a growing discrepancy with regard to technical and other resources.

In the field of **migration**, the new Law on Entry and Stay of Foreigners provides for wide harmonisation in this area by regulating the admission of third-country nationals and the system of issuing residence permits. All provisions of the law on Hungarians Living in Neighbouring Countries adopted in June 2001, including those concerning migration, will have to be applied in accordance with the *acquis* from the date of accession (*see also chapter 27 - Common Foreign and Security Policy*). Readmission agreements will have to be aligned.

From a legal point of view, Hungarian **asylum** legislation is already largely in line with the *acquis*. In addition, the relevant infrastructure to implement the *acquis* properly has been established or up-graded and the institutional framework has been reinforced. Further efforts are necessary to improve the integration of refugees into society.

In the area of **police co-operation**, the initialling of a co-operation agreement with Europol constituted an important step towards strengthened co-operation. However, in this area further efforts are needed to implement the *acquis*. In the legislative area, a bilateral agreement between the Ministry of Interior and the Chief Public Prosecutor's Office should be concluded in order to process requests received within the framework of the international exchange of information and to obtain data outside the criminal procedure. On the implementation side, a uniform digital home-affairs communications network should be set up to provide the infrastructure conditions for the Schengen Information System. Stronger inter-ministerial co-operation and improved communication between the various agencies involved is needed. There is also a need to establish clearly, which law enforcement agency is to be responsible for new types of crime such as hi-tech crime and money laundering.

In the area of the **fight against organised crime**, the framework for cross-border co-operation in the investigation of crimes still needs to be set up, and international agreements have to be reviewed.

In the area of the **fight against fraud and corruption**, Hungary has made further progress, in particular as regards legislative developments. Hungary is a party to most international conventions concerning corruption. The Council of Europe Civil Law Convention on Corruption has not yet been signed. Hungary will need to effectively implement its newly adopted anti-corruption strategy.

With regard to the protection of the financial interests of the European Communities, Hungary has nearly completed the alignment of its legislation with the *acquis*, in particular with the 1995 Convention on the protection of the financial interests of the European Communities and its Protocols.

In the field of **drugs**, substantial progress can be noted, although the fight against drugs needs to be reinforced. Furthermore, a national Reitox focal point still needs to be set up.

In the area of **customs co-operation**, further efforts are necessary to ensure a comprehensive, efficient and effective co-operation. Hungary will also have to join the Convention on the use of information technology for customs purposes (CIS) and to establish further agreements for international assistance.

Regarding **judicial co-operation**, Hungary will need to further align its legislation, in particular as regards its accession to a number of international conventions related to mutual assistance and co-operation in customs and criminal matters. Further training and additional human resources seem to be necessary to ensure adequate implementation. Hungary also will need to prepare for participation in the European Judicial Network and EUROJUST.

Hungary has ratified all **human rights** legal instruments, which are part of the Justice and Home Affairs *acquis*.

Chapter 25: Customs union

In the reporting period, Hungary further aligned its legislation with the *acquis* and strengthened its implementation capacity.

As regards alignment between the Hungarian legislation and the **EC Customs Code and its implementing provisions**, in January 2001 the legislation on Binding Tariff Information (BTI) and Binding Origin Information (BOI) entered into force. The procedures for processing under customs control and for inward and outward processing were further harmonised with the *acquis*. An amendment to the implementing provisions on simplified procedures also came into force.

Regarding the **customs *acquis* outside the Customs Code**, rules on cultural goods were aligned.

Progress was also made on aligning Hungarian legislation with the new provisions on the common transit procedure (December 2000), on the TIR Convention (April 2001) and on the law on international transport under cover of TIR carnets (June 2001). During the reporting period, the Hungarian Customs and Financial Guard (HCFG) continued to strengthen its **administrative and operational capacity**. It also continued to implement the “Business strategy” for customs, adopted in October 1999. On the basis of this strategy, considerable efforts were made to train the staff, *inter alia*, in the *acquis*, foreign languages and IT. The current staff numbers 7729, unchanged since 1999. The ten county directorates were restructured to form seven regional directorates. The regional deputy directors supervise the three main areas of customs, excise and information technology. The regional directorates were divested of investigation and ex-post control functions. Some restructuring took place also at the national headquarters, with directorates being up-graded or merged.

Efforts have been made to upgrade the Customs Laboratory, including the setting up of a mobile laboratory service and the implementation of the new BTI/BOI systems. The Chemical Testing Institute within the Customs Administration is in charge of decisions on BTI and BOI.

A special unit has been set up to deal with the protection of intellectual property rights. A comprehensive registry system interconnected with the World Customs Organisation’s International Property Rights database and using risk profiles has been established. Progress in enforcement has been registered. Risk analysis teams and groups have been established in the Customs Directorate, the Controllers’ Headquarters, the Department of Special Affairs, the Department of Investigation and Offences and in the Central Law Enforcement Headquarters. The early warning system (EWS) was established in the Directorate of post-controls in September 2000 and has been fully operational since February 2001.

The Customs administration has continued the setting up of computerised systems compatible with the EC systems such as Quota, European Binding Tariff Information (EBTI), etc. The Hungarian IT system (VAMKER), which covers customs clearance, post-clearance procedures, consignment registration and transit, and warehousing procedures has been further developed and is accessible to hauliers. A free phone number and an e-mail service for hauliers have been introduced. The introduction of the electronic presentation of goods to customs authorities has reduced the length of customs procedures significantly.

In the first quarter of 2001, the number of crimes involving customs violations, primarily cigarette smuggling, increased significantly. In the January-March period the customs guards detected 172 such crimes. More than half of them were attempts to export tobacco products illegally.

As regards border crossing points, the Hungarian government took a decision on the development of certain priority borders with the focus on southern borders. In particular the control of border crossing traffic was modernised, and new border crossing points were built. In order to increase the efficiency of traffic control at border crossing points, an action plan has been drawn up for in-depth control and the use of standard control techniques.

Overall assessment

In general, Hungary is already quite advanced in this area. The Hungarian legislation has already to a large extent been aligned with the *acquis* since May 2000. However, in the legislative field, further efforts are needed in warehousing and temporary importation as well as regarding provisions on the time limit and procedures for payment, the customs guarantee system and the customs free zones. The number of free zones, 95 at the moment, needs to be significantly reduced.

As regards the administrative and operational capacity to implement the *acquis*, Hungary continued to train customs officers and to up-grade the relevant equipment. Continuous efforts are still needed in these fields, including language training and training on the relevant areas of copyright and phyto-sanitary legislation, and in the further development of the IT system. The latter remains the main problem area for the Hungarian customs administration, as it must be emphasised that flawlessly functioning EC-compatible IT systems should be in place at least one year before EU accession in order to guarantee interconnectivity with the EC customs computerised systems.

The development of customs control based on risk analysis methods should be continued. The strengthening of the border crossing points should continue, too, in order to ensure an efficient and effective implementation of the *acquis*. This concerns in particular the improvement of detection equipment, e.g. for hazardous goods. Smuggling still remains a problem to be further tackled, especially illegal exports of cigarettes. Hungary should continue its efforts to fight corruption by further strengthening the status of Customs staff. Within Hungary, co-ordination and co-operation between the border guards, the police and the judiciary should be further intensified. Hungary will also need to establish further agreements on international assistance to improve customs co-operation.

Chapter 26: External relations

Hungary has continued to align its legislation with the *acquis* with regard to the Common Commercial Policy and to co-ordinate positions and policies within the WTO with those of the EU, in particular with regard to the preparation of the New Round.

In the area of **common commercial policy**, in 2001 Hungary applied tariffs which average 11.7% on all products, 31% on agricultural products, 15.1% on fishery products and 7.1% on industrial products. By comparison, the EC tariffs²¹ currently stand at 6.3% on all products, 16.2% on agricultural, 12.4% on fishery products and 3.6% on industrial products. Hungary's total exports in 2000 amounted to € 30.5 billion, while its imports accounted for € 34.8 billion. These figures show a 30% increase in total exports and a 32.5% increase in total imports compared to 1999.

In May 2001, new legislation was adopted providing the framework for the creation of the necessary administrative structures required upon EU accession.

Hungary concluded a **Free Trade Agreement** with Croatia that has been applied since April 2001 on a provisional basis. The Free Trade Agreement concluded with Estonia entered into force in April 2001.

As regards the fields of **development policy** and **humanitarian aid**, co-operation and assistance, Hungary has been an active member of the OECD since 1996 and it is adapting its development practices to the principles laid down by the Development Assistance Committee. For the implementation of humanitarian aid initiatives, the authorities co-operate with Non-Governmental Organisations established in Hungary.

Overall assessment

Hungary's trade policy and its participation in international economic organisations are already to a large extent in line with those of the Union.

In order to reach full alignment with GATT and WTO obligations, Hungary will need to join the Agreements on Trade in Civil Aircraft and Government Procurement, where it has observer status, and to the Agreement on Trade in Information Technology Products by the time of its accession to the EU. Further co-operation is also needed to ensure alignment of Hungary's GATS commitments with the EC's commitments and MFN exemptions.

With regard to the WTO Agreement on Textiles and Clothing (ATC), Hungary has co-operated with the EC in the process of third stage notification in order to align its list of integrated products under the ATC to that of the EU, thus avoiding the inclusion of products that have not yet been integrated by the EC.

As regards the capacity for licensing traded goods, Hungary has started to consider the management of quotas, the export/import of dual-use goods, weapons etc. The Licensing and Administrative Office, with a staff of some 200, is already established within the Ministry of

²¹ WTO bound tariffs after full implementation of all concessions including - where possible - estimated ad valorem equivalents of specific and compound tariffs.

Economic Affairs and is *inter alia* in charge of issuing export licenses for arms. Further efforts are needed to reinforce and strengthen the institutions in the field and better co-ordination between the agencies concerned is also required.

Although Hungary's system for export credits is in line with the OECD Arrangement, further alignment with the *acquis* is needed in the area of medium and long-term export credits. Hungary implements the economic sanctions imposed by the UN Security Council. Hungarian legislation and enforcement on arms and dual-use goods are largely in line with the *acquis*.

Besides the new Free Trade Agreements mentioned above and the Europe Agreement, Hungary has concluded such agreements with Bulgaria, the Czech Republic, Poland, Romania, the Slovak Republic and Slovenia within the framework of CEFTA, with all EFTA countries and with Israel, Latvia, Lithuania and Turkey.

Concerning bilateral agreements with third countries, any international agreement that is incompatible with the obligations of membership will have to be re-negotiated or renounced prior to accession. Hungary is requested to keep the Union fully informed about existing trade agreements with third countries and of the content of negotiations aimed at the conclusion of any new trade agreement with a third country.

Hungary's alignment with and future participation in the common commercial policy is administered by the Ministry of Industry and Trade. The administrative infrastructure which needs to be in place as regards customs services, is addressed under *chapter 25 - Customs union*. Development and humanitarian aid are administered by the Ministry of Foreign Affairs. For the purpose of Hungary's future financial contribution to the European Development Fund, Hungary's management of its national budget organisation and management of flow of funds to the EC budget is addressed under *chapter 29 – Financial and budgetary provisions*.

The amount allocated for humanitarian aid is around HUF 20 million (around € 77,000). The largest recipients of Hungarian humanitarian assistance are located in Europe, in particular Hungarian communities living in countries neighbouring the Republic of Hungary.

With regard to institution building in relation to development policy and humanitarian aid, the Ministry of Foreign Affairs is preparing an outline to the government. The outline will cover the setting up of a new unit, the determination of its duties and competencies, the objectives to be realised and the budgetary implications.

Chapter 27: Common foreign and security policy

Since the last Regular Report, Hungary has continued to align its foreign policy with that of the European Union and has participated constructively in the framework of the Common Foreign and Security Policy, in particular as regards the Kosovo crisis.

The **political dialogue** established by the Europe Agreement proceeded smoothly on a regular basis and Hungary continues to orient its foreign and security policy towards the Union. Through the meetings at the level of Political Directors, European Correspondents and Working Groups, it co-operated actively in this field.

Hungary has closely followed the development of the European Security and Defence Policy (ESDP) as a part of the CFSP and has actively participated in the exchanges in this context with

the EU, in EU+15 format (i.e. non-EU European NATO members and candidates for accession to the EU) and in EU+6 format (i.e. non-EU European Members of NATO).

The first official NATO-EU ministerial meeting was held in 2001 during the spring term Ministerial Meeting of the North Atlantic Council in Budapest.

Hungary played an active role in the first Capabilities Commitment Conference in Brussels in November 2000 and offered 350 soldiers to the Rapid Reaction Force, which is yet to be set up. This offer includes a mechanised artillery battalion and Mistral air defence missile battery as well as 59 combat transporters.

In addition, Hungary will contribute 107 policemen to the European Union's crisis management contingent of 5,000, to be set up in 2003. Over the past twelve years 460 Hungarian policemen have participated in peacekeeping missions. Fifty of them are still serving under the flags of the United Nations, the OSCE and the WEU in Albania, Bosnia and Herzegovina, Western Sahara and the Sinai Peninsula. In August 2001, Hungary also sent 41 civilian employees of two companies belonging to the Defence Ministry to participate in the destruction of ammunition and weapons collected under the NATO mission in FYROM called "Essential Harvest".

As regards alignment with **EU statements and declarations**, Hungary has regularly aligned its position with those of the Union and has, when invited to do so, associated itself with the Union's **Joint Actions and Common Positions** and other CFSP instruments, including negative measures. Since October 2000, Hungary has associated itself with eight Common Positions, including three on the Former Republic of Yugoslavia.

Hungary has continued to develop good-neighbourly relations with surrounding countries and promoted regional co-operation.

However, the Law on Hungarians living in neighbouring countries raised controversies with some of these neighbouring countries as it was adopted by Parliament in June 2001 without due consultations. While the objective of the Law is to support Hungarian minorities in neighbouring countries and to maintain their cultural heritage, some of the provisions laid down in this Law apparently conflict with the prevailing European standard of minority protection, as determined in a Report adopted on 19 October 2001 by the Council of Europe's Commission for Democracy through Law (Venice Commission). According to this Report, unilateral measures granting benefits to kin-minorities living in and citizens of other States are only legitimate if the principles of territorial sovereignty of States, *pacta sunt servanda*, friendly relations among States and the respect of human rights and fundamental freedoms, in particular the prohibition of discrimination, are respected. Also, as foreseen in its Article 27 (2), the Law will need to be aligned with the *acquis* at the latest upon accession, since it is currently not in line with the principle of non-discrimination laid down in the Treaty (articles 6, 7, 12 and 13).

As the Law itself represents framework legislation, it will not be applicable without the adoption of implementing decrees. Hungary will therefore need to comply with the above principles and hold the necessary consultations in order to agree with its neighbours also as regards future implementing legislation. Consultations with the Romanian and Slovakian Governments started in summer 2001, so far without concrete results. Following the adoption of the Venice Commission's Report, including by Hungary itself, Hungary has however committed itself to comply with the Report's findings.

Hungary continued to play a particularly active role in the South East European Stability Pact. As of July 2001, Hungary co-chaired Working Table No. 3 of the Stability Pact on democratisation and human rights. Hungary also contributed to the democratisation process and stability in the Federal Republic of Yugoslavia and offered to share its experience acquired along the democratic transition in the framework of the “Szeged Process”.

From June 2001, Hungary assumed the rotating presidency of the Visegrád dialogue. The four Prime Ministers agreed in a meeting in Krakow in May 2001 to double their contributions to the International Visegrád Fund that is aiming at the fostering of regional co-operation.

Hungary also continues to participate in the South East European Co-operative Initiative (SECI) and the Central European Initiative (CEI). At the CEI summit in Budapest in November 2000, the Prime Ministers renewed the statute and agreed to set up the CEI Co-operation Fund, which will start operation in January 2002 with a budget of 300 000 Euro.

Overall assessment

Overall, Hungary’s foreign policy is aligned to a large extent with the Union's Common Foreign and Security Policy.

Regarding negative measures, Hungary’s practice seems to be in conformity with that of the EU. As far as dual-use goods are concerned, Hungary’s regulations are largely in line with EU rules.

Hungary has aligned itself to the content and principles contained in the EU Code of Conduct on Arms Exports, but further efforts are necessary to ensure the implementation of its criteria.

Concerning the administrative capacity to implement the provisions relating to the CFSP, the Ministry of Foreign Affairs is increasingly involved in the related activities and its structure has been further strengthened. The State Secretariat for European Integration (SSI) assumes the responsibility for second pillar issues. The Hungarian Ministry of Foreign Affairs has both a Political Director and a European Correspondent. The ministry is connected to the Associated Correspondents' Network information system through which the EU communicates within the CFSP with the associated partners.

Chapter 28: Financial control

During the period covered by this Regular Report some progress has been made in this area.

As regards Hungary’s **Public Internal Financial Control** system, the tasks and the organisation of the Treasury were further modernised establishing a clearer division of functions. The institutional framework of *ex-ante* control was strengthened through the establishment of a network of county Directorates of the Public Finance Office (PFO).

As regards **external audit**, new legislation was adopted in March 2001 on the activities of the State Audit Office (SAO), the supreme audit institution. The mandate of the State Audit Office was extended in 2001 to fully cover EC funds up to the end user. By amending the Central Bank Law, the State Audit Office will also be able to audit the Hungarian National Bank. The SAO is undergoing a substantial training programme (more than 300 staff) in the fields of financial and performance audit, also including training in auditing EC funds. Efforts have also been made in the field of IT, resulting in the creation of a network linking the SAO headquarters

with its territorial offices. The SAO has adopted the basic general international standards of the Lima Declaration and the INTOSAI Auditing Standards.

Progress has been achieved by Hungary regarding **control of structural action expenditure**. A new Decree on Financial Planning was adopted, creating the legislative framework for the management and control of Community funds. With regard to EC pre-accession funding, although a Government resolution on the accreditation of the SAPARD Paying Agency to SAO has been passed, progress in the area of control and audit of SAPARD funds has been limited..

No further developments can be reported in the field of the **protection of EC financial interests**.

Overall assessment

Hungary has already made significant steps in the development of legislation and set up the necessary internal control and external audit bodies. It has created the legal framework for the development of an *ex-ante* financial control structure. However, it is not entirely clear whether the *ex-ante* controls also relate to procurement and contracting aspects.

Internal auditing across the public administration is understaffed and inadequately prepared for its future role. The functional independence of the internal auditors should be guaranteed and developed. A detailed needs analysis should be carried out in order to clarify the role and competencies of the Ministry of Finance, the Treasury and the GCO especially regarding internal audit area. In addition, the line ministries' internal audit capacities should be strengthened.

As to external audit, the basic requirements for the efficient functioning of the State Audit Office seem to be met, but attention now needs to be focussed on manuals and training in the fields of systems based and performance audits. The SAO submits its reports to the Parliament. Some legislative changes are still required to set up a revised procedural system in order to ensure the follow-up of its recommendations. The State Audit Office has the power to audit state owned enterprises. In the case of the National Bank, this power is limited to the audit of the relationship between the Bank and public finances.

Substantial progress is needed in the field of fully decentralised management and control of pre-accession funds (EDIS). This requires, *inter alia*, a comprehensive description ("audit trail") of the systems applied for procurement, contracting and payments.

In the area of control and recovery of EC funds, Hungary has established the basis of a system to ensure the protection of EC financial interests, but more expedient procedures are needed. A government decree, which entered into force in January 2001, provides an institutional system for the management of pre-accession funds, rules of financial control and the treatment of irregularities, penalties and sanctions.

Hungary should start co-operating as soon as possible with OLAF through the designated contact point for the protection of the EC financial interests.

Chapter 29: Financial and budgetary provisions

Hungary has taken further steps over the reporting period, in particular as regards the **national budget and EC co-financed measures**. The Law on Public Finance of 1992 was amended in December 2000. The amendments introduced reinforced the multi-annual planning system and set up the biennial central budget for 2001-2002. The state budget now also contains a separate table summarising the funds related to EU accession. Despite some methodological inconsistencies, this has significantly improved the transparency of EU related spending.

The reorganisation of the Hungarian State Treasury (HST) continued with the extension of its responsibility to all public expenditure and income centres. A fully computerised and integrated on-line system is now in place recording all transactions, including commitments and international assistance funding.

The State Debt Management Centre is responsible for the transparency of debt management. In addition, the General Government Financial Office was set up and is in charge of the execution of the state budget through part of the State Treasury.

As regards **Own Resources and administrative infrastructure**, the preparatory work for calculation has been started within the Ministry of Finance. This should enable Hungary to apply the ESA 95 methodology used by the EU. Regarding GNP, the National Statistical Office has continued to co-operate closely with Eurostat. Harmonisation of the methodology is progressing.

Overall assessment

Hungary has a budgetary system, which is now largely in line with its counterparts in the Community. The main legal provisions are laid out in the Law on Public Finance of 1992, as amended. Some further improvements are needed, in particular to bring the calculation of GDP into line with ESA 95 standard.

Budgetary techniques to deal with co-financing measures focus mainly on the functioning of extra-budgetary funds and on transfers to local governments. Multi-annual programming was already introduced in 1997. Since then, the current draft budget has had to contain plans for the following two budgets, using multi-year expenditure estimates from the various ministries. Projections covering the major macro-economic indicators are presented, and an explicit annual target is set for the budget deficit.

The Treasury, complemented by the Central Financing and Contracting Unit, administers the National Fund for the management of the EC pre-accession funds. The arrangements for the pre-accession funds are nearly finalised. Further efforts are needed to enable Hungary to meet the Structural Funds requirements with regard to co-financing and multi-annual programming.

The management of own resources will be under the control of the Ministry of Finance and the Hungarian Central Statistical Office, which performs GNP measurements and estimates. Modelling and projections of GNP are carried out under the Economic Analysis Department of the Ministry of Finance. Procedures for managing customs and VAT issues are in place.

The basic central co-ordination structure for the proper collection, monitoring and payment and control of funds to and from the EC budget has been set up. Administrative capacity should be

strengthened in the context of the relevant policy areas described elsewhere in this report such as Customs, Taxation, Regional Policy, Agriculture, and Financial Control. In particular, for the sake of effective calculation, collection and control of Community own resources the Ministry of Finance and the Tax and Financial Control Administration should be further reinforced. The control modules of the Joint Initiative for improving national administration systems still need to be taken into consideration. In relation to the control of future EC Own Resources, there is also a need to develop an effective instrument for the fight against fraud, notably in the area of VAT and customs duties.

Appropriate administrative steps should be taken by Hungary to ensure adequate co-ordination between the various authorities involved in the application of the system of Own Resources.

3.2. Translation of the *acquis* into the national language

Applicant countries are required to translate the various legal texts constituting the *acquis* into their national languages by the time of their accession. Primary and secondary legislation alone represents a considerable volume of acts, roughly estimated at 60,000-70,000 pages of the Official Journal. To help the candidate countries in this process, assistance is being provided under the Phare programme. With the help of TAIEX, a centralised Translation Co-ordination Unit has been created in each of the ten candidate countries of Central and Eastern Europe.

The Ministry of Justice is responsible for the translation of the Community *acquis* into the Hungarian language. The necessary financial means were allocated in the national budget of 2001-2002 (around € 1.15 million, or HUF 300 million)..

During the last twelve months terminological issues constituted an important part of the translation process. The Terminology Database, set up in September 2000, contains Hungarian equivalents of a large number of EC terms prepared by the Unit. It has both Internet and Intranet interfaces. The first, covering already consolidated terminology, is accessible to the public, while the second one is for internal use and contains all the glossaries and terms created during the process of revision but not yet approved by the Unit.

The Translation Co-ordination Unit of the Ministry of Justice carries out the final revision and consolidation of the relevant terminology. The number of linguist lawyers employed by the Ministry on a permanent basis has been increased from 7 to 9 and 4 new posts for terminologists with linguistic training have been created.

The number of translated pages amounts currently to 51 500, and the volume of revised translations has reached 45 000 Official Journal pages. Without prejudice to the outcome of the accession negotiations, sustained efforts are required in this area.

Due attention must also be given to the training of conference interpreters.

3.3. General evaluation

Hungary continued to make progress in aligning and implementing the *acquis* in many areas. In the reporting period, the country has moved steadily towards achieving a degree of administrative capacity needed to satisfactorily implement the *acquis*.

Continued good progress could be noted concerning the *internal market*. In this area, the major part of the *acquis* has been gradually adopted, and basic administrative structures are in place. As regards the free movement of goods, the alignment process has continued in respect of harmonised and “new approach” product legislation, and Hungary has been able to apply for full membership in the European standard bodies CEN and CENELEC. Work should be continued to ensure a coherent and comprehensive market surveillance system. With regard to public procurement, efforts will be needed to achieve full alignment and to ensure transparency and enforcement of the current rules at all levels of government and in all sectors, in particular in motorway construction. In the field of services, banking and insurance legislation has largely been aligned, and the supervisory authority appears to be working satisfactorily. Capital movements were almost fully liberalised. The adoption of an important new law on the fight against money laundering, which aims at, *inter alia*, phasing out anonymous savings books in order to meet the recommendations of the Financial Action Task Force (FATF), is pending at Parliament. In the field of *company law*, the Hungarian legislation with regard to industrial and intellectual property rights is already largely in line with the *acquis*; Hungary has a relatively good enforcement record. In *competition policy*, substantial and procedural rules for state aid control were further aligned with the *acquis*. Further efforts are needed to align state aid schemes, in particular the fiscal aid schemes. Both anti-trust and state aid enforcement bodies are working satisfactorily.

Alignment of VAT and excise duty levels continued in the area of *taxation*. However, appropriate IT systems allowing for the exchange of electronic data with the Community and the Member States have still to be developed. In the area of *customs*, in particular, the administrative and operational capacity was strengthened through training and modernisation of the equipment. Hungary still needs to work on the compatibility of its IT system with the EC customs computerised systems in order to ensure interconnectivity by the time of accession. In the area of *economic and monetary union*, the independence of the National Bank was consolidated with the adoption of a new law. With regard to *industrial policy* and *small and medium-sized enterprises*, Hungary made further progress by the adoption and implementation of the Széchenyi Plan. The issue of the restructuring of the Hungarian steel industry has progressed in the reporting period.

Significant progress was also made in the area of *environment*, notably through the adoption of legislation on Environmental Impact Assessment, on water, waste, industrial pollution control and risk management, on chemicals and on radiation protection. The administrative capacity in this sector was also improved, but needs further strengthening, in particular as regards the clear distribution of tasks between the ministries involved.

As to *agriculture*, progress in the reporting period was limited to the food safety and veterinary sectors, while the inspection arrangements in the veterinary and phyto-sanitary areas still need to be updated. Further efforts are needed to establish in time the necessary procedures and structures for Hungary’s participation in the Common Agricultural Policy. Legal alignment needs to be sustained in the area of *transport*, and efforts are needed to carry out the restructuring of the rail sector that is indispensable to prepare for the implementation of the market access *acquis*. In addition, appropriate institutions will have to be set up in order to enforce the *acquis* adequately. In the *energy* sector, only limited progress was made. The necessary legal framework for the participation of Hungary in the internal energy market still needs to be created. No progress could be noted with regard to the *audio-visual* sector.

Considerable progress was made in the area of *social policy and employment*, notably through the adoption of the revised Labour Law. As to social dialogue, confidence-building measures are needed to enhance real dialogue.

In relation to *regional policy*, Hungary has been making good progress in preparing for programming Structural Funds and in defining the implementation structures, but administrative capacity as well as financial and budgetary procedures need to be further strengthened. Effective inter-ministerial co-ordination mechanisms should also be set up, and an even wider application of the principle of partnership should be ensured.

The progress made in legal terms in the *telecommunications* sector needs to be followed up by appropriate enforcement measures.

In the area of *Justice and Home Affairs*, significant progress was achieved through further alignment with the *acquis* in the fields of visa policy, migration and asylum. The fight against fraud, corruption, money laundering and organised crime was made more efficient through the adoption of additional legislation and reinforced institutional structures. As regards external borders, a strategy on the integrated development of border crossing points was adopted. The Schengen Action Plan addresses the main issues of the *acquis*.

In the area of *common foreign and security policy*, some of the provisions laid down in the Law on Hungarian minorities living in neighbouring countries apparently conflict with the prevailing European standard of minority protection. Hungary should therefore find an agreement with its neighbouring countries with a view to complying with the recent findings of the Report of the 'Venice Commission'. Also, as foreseen in its Article 27 (2), the Law will need to be aligned with the Community *acquis* at the latest upon accession, since it is currently not in accordance with the principle of non-discrimination laid down in the Treaty.

As to *financial control*, some progress has been made both as regards external audit and public internal financial control. However, the administrative capacity in general and the functional independence of the auditors in the internal audit sector should be further strengthened. As to *financial and budgetary provisions*, further efforts continue to be needed in order to meet Community requirements with regard to co-financing and multi-annual programming.

Hungary made further progress in building up its administrative capacity to apply the *acquis* in most areas. However, with regard to the administrative and judicial capacity, further efforts will have to be made in particular in areas such as state aid control, audio-visual, market surveillance, transport and agriculture. Further efforts are also required in establishing the necessary administrative capacity to ensure the sound, efficient and controllable management of EC funds.

Hungary has continued to address its short-term Accession Partnership priorities with the exception of certain items in the field of agriculture, audio-visual policy, free movement of goods and competition policy. In addition, Hungary has implemented a number of medium-term priorities in the areas of social policy and employment, environment and Justice and Home Affairs (on asylum matters and visa policy).

C. Conclusion²²

In its 1997 Opinion, the Commission concluded that Hungary fulfilled the political criteria. Since that time, the country has made considerable progress in further consolidating and deepening the stability of its institutions guaranteeing democracy, the rule of law, human rights and respect for and protection of minorities. Over the past year, further efforts have been made in this direction. Hungary continues to fulfil the Copenhagen political criteria.

In the area of public administration reform, positive steps were taken with the introduction of a new legal framework increasing accountability and efficiency of the administration. In addition, better salaries and career possibilities have made the civil service more attractive. Efforts also continued in the area of training, which has become an important element of the career structure.

Within the judiciary, the overall efficiency of Courts further improved after the introduction of additional measures in the area of institution building, notably the modernisation of IT systems, procedures, continued training and new staff. However, the continued overloading of the Supreme Court reduces its ability to provide guidance to lower courts and to unify the Courts' practice. The scarce budgetary resources make it difficult to implement the remaining elements of the judicial reform.

The fight against corruption remained high on the political agenda and new legislation on asset declaration and more severe punishment was adopted to address the issue. Corruption however remains a problem, and the new measures would need to be implemented quickly to make the fight more effective.

As regards human rights and freedoms, progress can be reported with regard to asylum, where the situation considerably improved due to faster and better procedures and more appropriate reception facilities. However, there is a need to address police behaviour, notably with regard to reported cases of ill-treatment. In the area of public service media, a solution needs to be found regarding the composition of the Supervisory Boards of Trustees.

New policy instruments and measures were adopted for the Roma minority. This process was accompanied by a significant increase of budgetary means for the further implementation of the medium-term action programme, already adopted by the Government in 1999. Support measures in 2001 mainly focused on the areas of education, employment, social policy, legal protection and culture. In this context, it will be important to enhance efforts to fight against widespread discrimination and to fully implement and enforce the legislation already in place. The Roma minority should also be given the possibility to participate more actively in public life.

Hungary had implemented the short- and medium-term priorities of the 1999 Accession Partnership priorities which related to the continued implementation of the medium-term action programme for the Roma and the increase of budgetary means for this purpose, as well as the further reform of public administration and of the judiciary.

²² See "Making a success of enlargement: Strategy Paper and Report of the European Commission on the progress towards accession by each of the candidate countries", COM (2001) 700.

Hungary is a functioning market economy. Provided that it fully maintains and implements its reform programme in a consistent manner, it should be able to cope with the competitive pressure and market forces within the Union in the near term.

The macroeconomic situation continues to be sound, with high GDP growth underpinned by a rising investment share, further declining unemployment and favourable current account development. Railway restructuring continued through a major bailout and debt restructuring. It has adopted a more appropriate monetary and exchange rate framework, which is contributing to lower inflation.

However, fiscal policy has become expansionary in 2001. Together with recent non-transparent fiscal practices, the uncertainty over the further reform of the pension system and the delays in the reform of the health care system have raised some concern about the continuation of consolidation and the medium-term sustainability of public finances. The authorities will need to maintain fiscal discipline to ensure that fiscal policy supports the new monetary policy framework and the external balance. This would contribute to lower inflation. The health care reform should be undertaken swiftly.

Hungary continued to make progress in aligning and implementing the *acquis* in many areas. In the reporting period, the country has moved steadily towards achieving a degree of administrative capacity needed to satisfactorily implement the *acquis*.

Continued good progress could be noted concerning the *internal market*. In this area, the major part of the *acquis* has been gradually adopted, and basic administrative structures are in place. As regards the free movement of goods, the alignment process has continued in respect of harmonised and “new approach” product legislation, and Hungary has been able to apply for full membership in the European standard bodies CEN and CENELEC. Work should be continued to ensure a coherent and comprehensive market surveillance system. With regard to public procurement, efforts will be needed to achieve full alignment and to ensure transparency and enforcement of the current rules at all levels of government and in all sectors, in particular in motorway construction. In the field of services, banking and insurance legislation has largely been aligned, and the supervisory authority appears to be working satisfactorily. Capital movements were almost fully liberalised. The adoption of an important new law on the fight against money laundering, which aims at, *inter alia*, phasing out anonymous savings books in order to meet the recommendations of the Financial Action Task Force (FATF), is pending at Parliament. In the field of *company law*, the Hungarian legislation with regard to industrial and intellectual property rights is already largely in line with the *acquis*; Hungary has a relatively good enforcement record. In *competition policy*, substantial and procedural rules for state aid control were further aligned with the *acquis*. Further efforts are needed to align state aid schemes, in particular the fiscal aid schemes. Both anti-trust and state aid enforcement bodies are working satisfactorily.

Alignment of VAT and excise duty levels continued in the area of *taxation*. However, appropriate IT systems allowing for the exchange of electronic data with the Community and the Member States have still to be developed. In the area of *customs*, in particular, the administrative and operational capacity was strengthened through training and modernisation of the equipment. Hungary still needs to work on the compatibility of its IT system with the EC customs computerised systems in order to ensure interconnectivity by the time of accession. In the area of *economic and monetary union*, the independence of the National Bank was consolidated with the adoption of a new law. With regard to *industrial policy* and *small and*

medium-sized enterprises, Hungary made further progress by the adoption and implementation of the Széchenyi Plan. The issue of the restructuring of the Hungarian steel industry has progressed in the reporting period.

Significant progress was also made in the area of *environment*, notably through the adoption of legislation on Environmental Impact Assessment, on water, waste, industrial pollution control and risk management, on chemicals and on radiation protection. The administrative capacity in this sector was also improved, but needs further strengthening, in particular as regards the clear distribution of tasks between the ministries involved.

As to *agriculture*, progress in the reporting period was limited to the food safety and veterinary sectors, while the inspection arrangements in the veterinary and phyto-sanitary areas still need to be updated. Further efforts are needed to establish in time the necessary procedures and structures for Hungary's participation in the Common Agricultural Policy. Legal alignment needs to be sustained in the area of *transport*, and efforts are needed to carry out the restructuring of the rail sector that is indispensable to prepare for the implementation of the market access *acquis*. In addition, appropriate institutions will have to be set up in order to enforce the *acquis* adequately. In the *energy* sector, only limited progress was made. The necessary legal framework for the participation of Hungary in the internal energy market still needs to be created. No progress could be noted with regard to the *audio-visual* sector.

Considerable progress was made in the area of *social policy and employment*, notably through the adoption of the revised Labour Law. As to social dialogue, confidence-building measures are needed to enhance real dialogue.

In relation to *regional policy*, Hungary has been making good progress in preparing for programming Structural Funds and in defining the implementation structures, but administrative capacity as well as financial and budgetary procedures need to be further strengthened. Effective inter-ministerial co-ordination mechanisms should also be set up, and an even wider application of the principle of partnership should be ensured.

The progress made in legal terms in the *telecommunications* sector needs to be followed up by appropriate enforcement measures.

In the area of *Justice and Home Affairs*, significant progress was achieved through further alignment with the *acquis* in the fields of visa policy, migration and asylum. The fight against fraud, corruption, money laundering and organised crime was made more efficient through the adoption of additional legislation and reinforced institutional structures. As regards external borders, a strategy on the integrated development of border crossing points was adopted. The Schengen Action Plan addresses the main issues of the *acquis*.

In the area of *common foreign and security policy*, some of the provisions laid down in the Law on Hungarian minorities living in neighbouring countries apparently conflict with the prevailing European standard of minority protection. Hungary should therefore find an agreement with its neighbouring countries with a view to complying with the recent findings of the Report of the 'Venice Commission'. Also, as foreseen in its Article 27 (2), the Law will need to be aligned with the Community *acquis* at the latest upon accession, since it is currently not in accordance with the principle of non-discrimination laid down in the Treaty.

As to *financial control*, some progress has been made both as regards external audit and public internal financial control. However, the administrative capacity in general and the functional independence of the auditors in the internal audit sector should be further strengthened. As to *financial and budgetary provisions*, further efforts continue to be needed in order to meet Community requirements with regard to co-financing and multi-annual programming.

Hungary made further progress in building up its administrative capacity to apply the *acquis* in most areas. However, with regard to the administrative and judicial capacity, further efforts will have to be made in particular in areas such as state aid control, audio-visual, market surveillance, transport and agriculture. Further efforts are also required in establishing the necessary administrative capacity to ensure the sound, efficient and controllable management of EC funds.

Hungary has continued to address its short-term Accession Partnership priorities with the exception of certain items in the field of agriculture, audio-visual policy, free movement of goods and competition policy. In addition, Hungary has implemented a number of medium-term priorities in the areas of social policy and employment, environment and Justice and Home Affairs (on asylum matters and visa policy).

D. Accession Partnership and National Programmes for the Adoption of the *Acquis*: Global assessment

The purpose of the Accession Partnership is to set out in a single framework:

- the priority areas for further work identified in the Commission's Regular Report;
- the financial means available to help candidate countries implement these priorities;
- the conditions which will apply to this assistance.

Each candidate has been invited to adopt a National Programme for the Adoption of the *Acquis*. This sets out how the country in question envisages to deal with the Accession Partnership, the timetable for implementing the Partnership's priorities, and implications in terms of human and financial resources. Both the Accession Partnerships and the National Programmes for the Adoption of the *Acquis* are revised on a regular basis, to take account of progress made, and to allow for new priorities to be set.

1. Accession Partnership

In the following assessments the main sub-headings are indicated in bold type and further key concepts taken from the Accession Partnerships highlighted in Italics.

Short-term priorities

Hungary already met quite a number of short-term 1999 Accession Partnership priorities in 2000, such as the priority regarding taxation (i.e. amendment of law on excise duty for wine). In the area of employment and social affairs, the Joint Employment Review was finalised, and guidelines for a European Employment Strategy were prepared. With regard to environment, the law on waste management was adopted in 2000. By now, most implementing legislation in the pharmaceuticals sector has been adopted, too, and substantial further alignment has been achieved with regard to the Customs Code. As far as the chapter on agriculture is concerned, the short-term priority mentioned in the 1999 Accession Partnership on phytosanitary issues was addressed by the adoption of the plant protection law. Therefore, only those short-term priorities are mentioned hereafter, which were reported in the Regular Report of 2000 as having not or only partially been addressed:

Economic Criteria: *The macroeconomic situation* continues to be sound. Based on past structural reforms and careful macro-economic management, economic growth has reached its highest level since the beginning of transition. Although privatisation is nearly completed, foreign direct investment remains the motor of growth and productivity gains. Inflation is still relatively high, and only recently the authorities have responded by changes to the exchange rate and monetary policies, focussing on the further reduction of inflation. The current account improved substantially. Fiscal consolidation continued in 2000, but fiscal policy risks becoming expansionary in 2001. After a promising start, *healthcare reform* has been delayed. The present system is showing major shortcomings, such as the continuing high fixed cost of maintaining an inefficient over-hospitalised infrastructure. The delivery of services is deteriorating as the equipment is outdated and doctors and nurses are underpaid. The budget outflow into the

healthcare fund accounted for 0.8% of GDP in 2000. A rapidly ageing population aggravates the problem and poses a serious risk to public finances in the long term. In general, *land markets* are developing in Hungary. A large part of the land used by larger individual farms or companies is leased and partly even purchased. Lease contracts improve in terms of duration and sophistication, improving tenure security for the farms and thereby incentives for investment. As concerns the restructuring of the *steel industry*, Hungary advanced its reform. Indeed, the Hungarian Government withdrew in June 2001 its request for the extension of 5 years of 'grace' under Protocol 2 of the Europe Agreement for granting state aids to the steel industry for restructuring purposes. **Overall, this priority was met.**

Internal Market

- Some progress was made to reinforce existing *market surveillance and conformity assessment structures*, even though continued efforts are required. Legislative action was taken to prohibit the opening of new *anonymous accounts* and to phase out existing ones, but the implementation needs to be brought forward. Hungary made efforts to increase transparency of *state aids* by enlarging the scope of aids subject to prior notification to the *state aid monitoring authority*. However, this scope still needs to be widened further, and the coverage of the *state aid inventory* has not been completed. The monitoring authority is increasingly involved in state aid decision-making, but has no power to block illegal aids. In the area of *telecommunications*, the *Regulatory Authority's independence* and powers (notably dispute settlement) will be strengthened with the recently enacted new Law on telecommunication which is intended to transpose the 1999 *acquis*. Rapid progress will now be needed with regard to the punctual implementation of the law in view of the liberalisation scheduled for 1 January 2002 as well as with regard to secondary legislation. Despite the efforts of the government to progress in the area of the *audio-visual acquis*, the proposed law on Radio and Television Broadcasting (the so-called Media Act) was not adopted by Parliament as it needed a two-thirds majority. The proposal notably provided for rules governing *monitoring activities* and effective control over media operators as well as for the definition and promotion of European works, rules on advertising, sponsoring and teleshopping, exclusive *broadcasting rights* and certain rules relating to copyright. In the area of *Value Added Tax* the regime was further harmonised in November 2000 by introducing gradual alignment of the scope of products covered by a reduced VAT level. Hungary will need to review the scope of reduced rates, including the abolition of the zero-rate system. **Overall, this priority has been met to a large extent.**

Economic and Monetary Union

- In June 2001 a new law was adopted on the central bank which consolidated the *independence of the National Bank in particular with regard to government borrowing*. **Therefore this priority was met.**

Agriculture

- Hungary has intensified its preparations for aligning with the *acquis* in the *veterinary field*. The amendments to the Veterinary Act entered into force in July 2001, introducing the principle of regionalisation and animal passports as well as defining the tasks of state and private veterinarians. The amendments to the law also cover the principle of full compensation for producers and the rules concerning veterinary checks in the internal

market, although these provisions will only enter into force on the date of accession. The government adopted a strategy on the development of *external border* posts in January 2001. Progress in upgrading the Border Inspection Posts at Letenye, Roszke and Zahony was impeded by the difficulties to acquire the land.

- Concerning the modernisation of *meat and dairy products plants to meet EU hygiene and public health standards*, the Hungarian Veterinary Service carried out an evaluation of the food safety status of fresh meat establishments last year. Out of the 471 existing plants, 228 are high capacity of which 64 fully comply with EU requirements. The remaining 164 plants were required to draw up a detailed development plan and start eliminating identified deficiencies upon March 2001 and finish the upgrading at the latest in December 2007. Hungary introduced EU rules on the specific risk material (SRM) in April 2001. Since then, the application of SRM rules in all slaughterhouses, regardless of their capacity, is compulsory in Hungary. A monitoring programme in compliance with EU rules on TSE testing was launched in March 2001. No progress could however be noted as regards the establishment of a *vineyard register*. The law on statistical surveys of areas under vine was adopted in December 2000 and the statistical survey was carried out between June and October 2001. Subsequently, a fully functioning vineyard register needs to be put in place and constantly updated. **This priority has been partially met.**

Environment

- In the area of *Environmental Impact Assessment*, further progress was made in April 2001 with the adoption of legislation regulating the assessment of the effects of certain public and private projects. In the area of *waste* management alignment covered implementing legislation to the Law on Waste Management. In particular, the areas public service providers for waste management and public service contracts, calculation of fees for municipal waste management services, categories of wastes and hazardous waste treatment were harmonised. Also, disposal of waste oils, disposal of PCB/PCT, use in agriculture of waste water and sewage sludge and the treatment thereof, handling of batteries and accumulators were aligned to a large extent.. As regards *industrial pollution control and risk management*, the directive on the control of major accident hazards involving dangerous substances was aligned in June 2001, but did not yet enter into force. **Therefore this priority has been met.**

Medium-term priorities

Hungary already addressed the following medium-term priorities in 2000: As part of the economic criteria, *SME policy* was further developed with the preparation of the Széchenyi Plan, a National Development Plan. In the energy sector, the *energy efficiency* policy was considerably improved by the introduction of an energy efficiency programme of the government and by further alignment with the *acquis* in this area. Further efforts were made with regard to *nuclear safety*. In the Justice and home affairs sector, the administrative capacity for *border management, asylum and the fight against organised crime* was strengthened. A new *drug* strategy was approved in July. Progressive alignment of Hungarian *visa* legislation continued. The standards of reception facilities for asylum seekers were further improved.

Therefore, only those medium-term priorities are listed below, which were reported in the Regular Report of 2000 as having either not or not entirely been addressed.

Political Criteria

- The *implementation of the medium-term Roma action programme* continued and the Government had increased the budgetary means to implement it. Main measures cover the areas of education, employment, social policy and public health, legal protection and culture. However the means available remain limited in relation to the extent of the social disadvantage affecting the Roma population. In addition, the Government programme does not contain any provision to assess to which extent the envisaged measures are having positive effects on the target population. The situation in the education sector remains of particular concern as in certain areas up to one third of the school population is of Roma origin and the school system lacks human and financial resources to specifically address the educational needs of a large portion of the school population. Despite these important and acknowledged efforts, the integration of the Roma into the economic and social sphere is only at the beginning of what may be a long process. Hence the importance of determined and sustained efforts to fight against discriminatory attitudes, in particular at municipal level, and to address the situation of widespread social disadvantage affecting the Roma minority. **Therefore, this priority was largely met.**

Economic Criteria

- *EU fiscal accounting standards confirm the picture of a gradual consolidation in public finances.* In April 2001, Hungary submitted for the first time fiscal notification tables elaborated according to the EU's 'ESA95' methodology, which should make them more comparable to member states' figures. The main differences with the national definition are a broader concept of the general government sector, for example by the inclusion of the privatisation agency APV, and a shift from cash to accrual calculation basis. Compared with the government's traditional financial accounting method, the ESA95 general government consolidated deficit is 3.4% (instead of 3.7%) of GDP for 2000, while the primary surplus is 2.2% (instead of 1.8%). No further progress was made with regard to the reform of the *health care system*. The *small and medium enterprise* sector continued to develop in a dynamic manner. The Hungarian National Development Plan, the Széchenyi Plan, provided for a specific SME programme aiming at developing the business culture and skills (training, improved access to information), the development of SMEs' business relations (e.g. development of entrepreneurial networks, clusters, co-operation in procurement and international co-operation) and improved access to finance (e.g. schemes that address the different needs of enterprises according to their cycle phase, continuation of the micro-credit programme, guarantee schemes). The plan further proposed certain measures to improve and simplify administrative procedures. Of particular relevance to the SME development are also the separate programmes in the area of sub-contracting and tourism development in the plan. **Hungary largely met this priority.**

Internal market

- In the field of *public procurement*, progress was limited to enforcement and remedies procedures in the utilities sector. As regards the *free movement of goods*, the alignment of standards, certification and conformity assessment is not yet completed, but is well underway, and Hungary should be able to become full member of the European Standardisation Bodies CEN and CENELEC in the near future. Nearly all remaining restrictions on medium and short-term *capital* transactions have been removed, but

anonymous savings books have not yet been eliminated. In the field of *free movement of persons*, the alignment of mutual recognition of professional qualifications and diplomas still needs to be completed, and the administrative structures required for the co-ordination of social security need to be reinforced. Hungary also still needs to ensure full enforcement of *competition and state aid* rules and increase training at all levels of administration. *Customs procedures* were further aligned with the entry into force in January 2001 of legislation on Binding Tariff Information (BTI) and Binding Origin Information (BOI). The procedures for processing under customs control, inward and outward processing were further harmonised with the *acquis*. Also *simplified procedures* came into force. The licences for customs procedures with economic impact were primarily issued in the field of inward and outward processing, warehousing and temporary importation. The introduction of the electronic presentation of goods to customs authorities reduced the time of customs procedure significantly. Further adjustments of the Hungarian Customs Tariff to that of the Community were regularly carried out in line with the EC modifications. During the reporting period, the Hungarian Customs and Financial Guard (HCFG) continued to strengthen its *administrative and operational capacity*. Considerable efforts were made to train the staff, inter alia, on EU rules, foreign languages and IT. The Customs also continued the process of *computerisation* with the adoption of IT systems operated by the Commission. As regards *border crossing points*, the Hungarian government took a decision on the development of certain priority borders with the focus on southern borders. In particular the control of border crossing traffic was modernised, and new border crossing points were built. With regard to legislation, further efforts are needed in the area of customs *free zones*. The number of free zones, 95 at the moment, has to be significantly reduced. **This priority has been largely met.**

Agriculture

- Since last year's regular report, Hungary made limited progress in introducing the legal framework and administrative structures for the establishment of the Common Market Organisations. The Hungarian Government decided that the Agriculture Intervention Centre will play a crucial role in the management of the major common market organisations, but it still needs to be legally endorsed. The role of the Produce Councils in the future common market organisations will need to be defined, since they currently also perform tasks, which will be carried out by the future intervention agency. In April 2001 a Food Safety Strategy was elaborated by the inter-ministerial working committee on *food safety*. It describes the various official bodies involved, their roles, organisation and staffing as well as the institutional changes planned in order to ensure co-ordination between the Ministry of Health, the Ministry of Agriculture and Regional Development and the General Inspectorate of Consumer Protection. An advisory committee has been established within the Ministry of Health. Hungary also plans to set up a Food Safety Agency, but its functions have not yet been specified. **Therefore this priority has been partially met.**

Energy

- No progress could be noted in *preparing for the internal energy market, notably the electricity and gas directives*. The Government had prepared a revised law on *electricity* further liberalising the electricity market, which has however not yet been adopted by Parliament. In the area of institution building, the *independent system operator* (MAVIR, the Hungarian Power System Operator Company) was established in October 2000. In

January 2001 a new *price system* for the period came into force with a view of gradually eliminating the existing price distortions. As a consequence, average consumer gas prices were increased by 12% and average consumer electricity prices were increased by 6% in July 2001. The Government continued to promote *energy efficiency* in line with the energy efficiency programme adopted in late 1999. Under the programme, support is given to energy saving loans, the use of renewable energy sources, the modernisation of district heating supply and consumption systems, improved public energy awareness and the promotion of energy efficiency in transport. The *nuclear safety programme* of the Paks Nuclear Power Plant – supposed to be finished by the end of 2002 - continued to be implemented with more than two-thirds of the actions already finished by the end of 2000. As a result of these measures the core damage probability has decreased by a factor of 10. The Hungarian Atomic Energy Authority (HAEA) is a highly competent organisation, which has the technical capability to deal with the *regulatory* and technical areas of *nuclear safety and radiation protection*. **Therefore this priority has been partially met.**

Transport

- In *road transport*, rules on access to the profession and on safety belts were aligned and some mutual market access was agreed by means of international agreements on occasional international passenger transport, carriage of goods by road and combined transport. Rules on market access, road safety, dangerous goods and taxation remain to be aligned further. In the *railway sector*, the accounting separation of railway infrastructure from railway operations has been completed within the Hungarian Railways Company (MÁV). However, the revision of the rail reform programme adopted in 1999 is progressing rather slowly, possibly delaying further restructuring and legislative alignment. In *air transport*, progress was made on technical requirements and administrative procedures of civil aviation, on computerised reservation systems, licensing of air personnel and air carrier liability. It is also positive that Hungary this year became a full member of the Joint Aviation Authorities. However, negotiations with Hungary on the European Common Aviation Area (ECAA), which would ensure an early application of the aviation *acquis*, have not yet been finalised. In the field of *inland waterways*, registration of vessels, licensing of navigation operations, navigation qualifications, inspectors' qualifications and identification cards, technical requirements for vessels, and designation of bodies for the certification of conformity of vessels. The planned Inland Waterways Fund with the necessary institutional background still needs to be worked out. **Therefore this priority has been partially met, but further alignment is needed in all subsectors.**

Employment and social affairs

- The revised *Labour Law* of July 2001 introduced as an important new element the limitation of working time to a maximum of 12 hours per day and 48 hours per week including overtime. Other amendments to the Law concern the alignment with the *acquis* on collective redundancies, the contract of employment relationship, health and safety of temporary workers, the protection of young people at work, European Works Councils, equal opportunity Directives and anti-discrimination. The revised Labour Law also covered progress related to *equal treatment*, notably in the areas of equal pay and on burden of proof. Efforts to disseminate and put into practice the principle of equal treatment are continuing in all relevant areas. In the area of *health and safety*, new legislation entered into force, aligning with the directives on chemical, physical and biological agents, indicative limit

values, banning of certain specified agents or certain work activities, vinyl chloride monomer, metallic lead, asbestos, and carcinogens. Progress was also made in the areas drilling, mineral-extracting industries and noise. In June 2001, Hungary adopted a 10-year *Public Health* Action Programme, with the final goal to increase life expectancy. In December 2000, new legislation on the regulation of tobacco advertisement entered into force, which partially aligned with the Community tobacco legislation. A programme of re-organising and improving the blood supply system has been launched and a new regional system was established. In the area of *social dialogue*, the government and the social partners were not able to agree on the modification of the Labour Code and the national minimum wage for 2001. In March 2001, the government concluded a three-year agreement with the largest trade union confederation of the public sector. In this context, a new forum for consultation in the public sector called National Labour Council for Public Employees was created. A Joint Employment Policy Review was launched with a view to examine progress made by Hungary in adapting its employment system so as to be able to implement the European Employment Strategy. Hungary seeks to maintain a balance between *social protection* and economic possibilities. In this context, progress was made on reforming invalidity and disability benefits, family support, social assistance, care services and the review of pension reforms already implemented. Improvements in the field of care for the elderly and support for childcare was made through modifications to the law on social administration and social assistance and the law relating to child support. **Therefore, this priority has been partially met.**

Economic and Social Cohesion

- Hungary has further adapted its legislative framework and had defined the *institutional structure* with regard to programming and implementation of *Structural and Cohesion Funds assistance*. Thus, the responsibility for planning and programming remains with the Ministry of Economy while the Office of the Minister without portfolio responsible for Phare has been entrusted with the responsibility of setting up the managing authority for the Community Support Framework. In order to sustain the new programming process and prepare for the future management of Structural Funds, Hungary is re-enforcing the concerned ministries and the agencies with staff and training. Preparations for the *financial and budgetary management* of the Structural Funds and the Cohesion Fund are based on the financial management system established for the pre-accession instruments. The Treasury is expected to assume the role of the future paying authority but would still need to be confirmed. The legal framework for the financial control for public expenditures has been established and the necessary internal and external control bodies have been set up. The Ministry of Finance has been given the responsibility for the overall regulation, supervision and development of the areas of public finance, the treasury system, public internal financial control, and financial audits, including the co-ordination of measures necessary for the consistent implementation of the *acquis*, as well as co-ordination with Community Institutions. Concerning *monitoring and evaluation*, concrete preparations for launching the ex-ante evaluation of the NDP and a macro-economic impact study are under way. An evaluation sub-committee of the Inter-ministerial Committee for Development Policy Co-ordination has been established. A pilot IT monitoring system has been created, with Phare assistance, in the Government Control Office, which needs to be extended to the bodies designated as future managing authorities. **Hungary largely met this priority.**

Environment

- Over the reference period Hungary has made significant progress in this area. The *integration of the environment into other policies* is one of the tasks of the Environmental Council, an advisory body to the Government. Furthermore, the revised National Environment Plan (NEP) contains as one of its priorities the integration of environment into other policies. As regards *nature protection*, some progress was made concerning the alignment in relation to the protection of wild birds. Also prohibition of capture, killing, disturbance, transport, trade etc. of species has been extended to all protected species as well as to all wild birds in Europe by new legislation in May 2001. In the field of *water quality* a detailed national programme for the implementation of the respective *acquis* was drawn up in June 2001. Sensitive areas were designated in January 2001 for the purpose of wastewater collection, and in May 2001 Community legislation on nitrates pollution from agricultural sources was fully aligned. A new information system on *noise* is being created, which will incorporate data from industrial and commercial operations and from traffic. In the field of *genetically modified organisms and chemicals* alignment covered dangerous substances, classification, packaging, labelling, export and import; chemical safety, chemical load fines, restrictions on the marketing and use, assessment of risks to man and the environment; and the prevention of environmental pollution by asbestos. Also in the field of *nuclear safety and radiation protection* further progress was made on the supervision and control of shipments of radioactive waste between Member States and into and out of the Community harmonising during the reference period. As regards *air quality*, the rules on the protection of ambient air and on air quality limit values and emission limit values were further aligned with the *acquis* in July 2001. The development of an air monitoring system with 44 stations and a data reporting system on national level is in progress. An air quality database at the Institute for Environmental Management ensures the uniform data supply in the context of the different reporting requirements. The Institute is also responsible for quality assurance/quality control. In order to run smoothly, a further increase of skilled staff (training is ongoing) and the provision of adequate equipment would be necessary. **Therefore, this priority was met.**

Justice and Home Affairs

- In the area of *visa policy* new visas obligations were introduced for Belarus, Bosnia-Herzegovina, Moldova, Russia and FYROM. The new Law on Entry and Stay of Foreigners adopted in June 2001 introduced new visa stickers further aligning with the *acquis* by January 2002. The law also foresees the exchange of personal data between the co-operating aliens policing authorities and ensures alignment with the requirements of the Common Consular Instructions. These provisions will, however, only be applicable upon accession. The Hungarian on-line system to support the visa procedure has been implemented in additional diplomatic and consular missions of Hungary, bringing its total number to 59. Staff at the security Service of *Law Enforcement Agencies* of the Ministry of Interior that is responsible for the prevention, detection and investigation of corruption cases within law enforcement agencies has been increased by 86. Within the police organisation a specialised mobile unit has been set up against street corruption of police officers. Their tasks include detecting and reporting of officers taking bribes from citizens and starting disciplinary action or criminal procedure against them. In 2000, a total of 800 of such cases were detected of which 200 by this unit. Also training in this area continued.. Over the reference period the Government continued its efforts to modernise the *reception facilities*

for asylum seekers and illegal immigrants. The majority of these facilities now fulfil the minimum standards for health conditions and provide basic care. **Therefore, this priority was met.**

Reinforcement of administrative and judicial capacity, including the management and control of EU funds

- The *continued reform of the Hungarian public administration* is a priority task under the government programme. The relevant legal framework for civil servants ensures their independence and career opportunities. Budgetary means were significantly increased (by more than four times) in order to ensure the smooth implementation of the law in 2001 including a considerable salary increase over the next three years above the annual inflation rate. This important change in the salary structure should help to improve the overall status of civil servants and to attract well-educated staff. As part of the reform, *training* became a priority and civil servants are obliged to pass an examination on *EU related questions*. The Hungarian Institute of Public Administration at the Prime Minister's Office is in charge of this task. Over the reference period Hungary continued to implement the *reform of the judicial system*, which started in 1997. Measures implemented covered the recruitment of additional staff, the rationalisation of court procedures, the training of Hungarian judges and the further modernisation of the Court Information System. However, the Supreme Court is getting more and more overloaded with the majority of cases being appeal cases. The new Regional Court of Appeal, planned to be set up in 2003 in Budapest, should facilitate and speed up the proceedings in the Supreme Court; but budgetary shortcuts could further delay its establishment. However, overall, technical facilities at courts are still inadequate and judges have to spend considerable time with administrative matters connected to their cases. In the area of *fight against fraud*, Hungary further aligned its legislation with the *acquis*. In the framework of amending the penal code the criminal liability of heads of businesses in connection with bribery of foreign public officials and fraud affecting the European Communities' financial interests has been introduced. Furthermore, the passive bribery of foreign national public officials has been established. As a result public officials of international organisations and officials of a foreign country will have to face the same punishment as Hungarian public officials in case of both active and passive form of bribery. Despite all this progress, it seems necessary to employ additional human resources in this area to implement effectively the said legislative measures. In the area of *financial control*, appropriate procedures need to be established for the further decentralisation of financial management and control of EU funds from the Commission to Hungary and towards regional implementation levels. As to external audit, the basic requirements for the efficient functioning of the State Audit Office seem to be met, but now the attention should be focussed on manuals and training in the fields of financial and performance audits. The co-operation between internal audit units and the State Audit Office should also be improved. In the field of *statistics* Hungary already reached an overall high level of alignment. Statistical co-operation with international organisations runs smoothly. Some further efforts are still needed to fine-tune the harmonisation of some statistics, including foreign trade statistics. **Therefore, this priority was met to a large extent.**

2. National Programme for the Adoption of the Acquis

The Hungarian National Programme for the Adoption of the Acquis (NPAA) was first presented to the European Commission in 1998. In the subsequent years the Programme was

reviewed, taking into account progress achieved in the context of the accession preparations as well as the modification of the Hungarian working hypothesis for the date of accession from 1 January 2002 to 1 January 2003. Hungary is strongly determined to complete preparations for membership by the end of 2002. The revised NPAA for 2001 is in line with this commitment, and contains properly updated measures for the remaining two years 2001-2002.

The Programme contains 41 chapters. The NPAA covers the whole *acquis* and follows the structure of the 2000 Regular Report.

The revised Programme includes a brief overview of the current situation in each chapter, focusing on progress achieved in 2000. The Programme presents the planned major steps in *law approximation* with reference to the complete Law Approximation Programme which was updated and approved by the Government simultaneously with this Programme, and contains detailed timetables for the alignment of each piece of the *acquis*. The planned *institution building measures* to establish the required administrative capacity in order to apply the *acquis* are also presented, with timetables for implementation. However, on Justice and Home Affairs the Programme neither contains any information on the efforts that need to be made regarding the reduction of the large backlog of cases before the Supreme Court nor about the implementation of the anti-corruption strategy. No reference is made in the NPAA either to a number of other JHA related issues (law on data protection, frauds, regional drug laboratories, overcrowding prisons), or in the environment chapter to the legislation covered in the chemicals sector, or in the regional policy chapter to the preparations for the Cohesion Fund. In this chapter, the timetable for the National Development Programme should be brought in line with the roadmap provided by the Commission in March 2001; the one for Operational Programmes should be updated, too. The timetable for the implementation of the *acquis* in the anti-trust and state aid sectors should be streamlined, too.

With regard to Institution Building measures, both the setting up of management and payment authorities for the Operational Programmes in the structural funds sector and the future development of the data protection supervisory authority should be outlined in more detail as well as the structure and capacity of the institutions responsible for the sectoral directives within the framework of the chapter on the free movement of persons.

Ministries and other Government agencies have provided detailed plans involving the establishment of new bodies where necessary; restructuring the organisation or the activities of existing bodies in order to improve their ability to perform control, supervisory and monitoring functions; increases in staff; professional training for staff; and technical modernisation. However, contrary to previous NPAAs, this Programme does not contain any figures on the precise increase of staff foreseen in the environment sector.

Finally, the Programme envisages the necessary *acquis*-related infrastructure development and other investments in the relevant sectors. The Programme includes detailed financial plans in each chapter where there are resource requirements: Hungarian budgetary sources, expected EU assistance and other sources are set out in a coherent manner. The financial resources required for the implementation of the Programme are available in the 2001-2002 budget already adopted by the Hungarian Parliament.

The Strategy for Catching up with Europe adopted by the Government in 1999 constitutes the economic policy base of the NPAA, together with the Pre-accession Economic Programme

adopted by the Hungarian Government in April 2001 and presented to the European Commission. The Preliminary National Development Plan for Phare, the Agriculture and Rural Development Plan for SAPARD, the environment and transport strategies for ISPA and the NPAA were brought in line with the NPAA.

The State Secretariat for Integration in the Ministry of Foreign Affairs, having overall responsibility for preparation, is continuously monitoring the implementation of the NPAA in order to prevent any delays.

The Commission will provide detailed comments on the NPAA later this year.

The NPAA covers the remaining issues of the accession preparations. It should be a useful tool to reach a very high degree of preparation for accession.

Annexes

***Human Rights Conventions ratified by the Candidate Countries,
30 September 2001***

<i>Adherence to following conventions and protocols</i>	BG	CY	CZ	EE	HU	LV	LT	MT	PL	RO	SK	SI	TK
ECHR (European Convention on Human Rights)	X	X	X	X	X	X	X	X	X	X	X	X	X
Protocol 1 (right of property)	X	X	X	X	X	X	X	X	X	X	X	X	X
Protocol 4 (freedom movement et al.)	X	X	X	X	X	X	X	O	X	X	X	X	O
Protocol 6 (death penalty)	X	X	X	X	X	X	X	X	X	X	X	X	O
Protocol 7 (ne bis in idem)	X	X	X	X	X	X	X	O	O	X	X	X	O
European Convention for the Prevention of Torture	X	X	X	X	X	X	X	X	X	X	X	X	X
European Social Charter	O	X	X	O	X	O	O	X	X	O	X	O	X
Revised European Social Charter	X	X	O	X	O	O	X	O	O	X	O	X	O
Framework Convention for National Minorities	X	X	X	X	X	O	X	X	X	X	X	X	O
ICCPR (International Covenant on Civil and Political Rights)	X	X	X	X	X	X	X	X	X	X	X	X	O
Optional Protocol to the ICCPR (right of individual communication)	X	X	X	X	X	X	X	X	X	X	X	X	O
Second Optional Protocol to the ICCPR (death penalty)	X	X	O	O	X	O	O	X	O	X	X	X	O
ICESCR (International Covenant on Economic, Social and Cultural Rights)	X	X	X	X	X	X	X	X	X	X	X	X	O
CAT (Convention against Torture)	X	X	X	X	X	X	X	X	X	X	X	X	X
CERD (Convention on the Elimination of All Forms of Racial Discrimination)	X	X	X	X	X	X	X	X	X	X	X	X	O
CEDAW (Convention on the Elimination of All Forms of Discrimination against Women)	X	X	X	X	X	X	X	X	X	X	X	X	X
Optional Protocol to the CEDAW	O	O	X	O	X	O	O	O	O	O	X	O	O
CRC (Convention on the Rights of the Child)	X	X	X	X	X	X	X	X	X	X	X	X	X

X = Convention ratified

O = Convention **NOT** ratified

BG=Bulgaria; CY=Cyprus; CZ=Czech Republic; EE=Estonia; HU=Hungary; LV=Latvia; LT=Lithuania; MT=Malta; PL=Poland; RO=Romania; SK= Slovak Republic; SV=Slovenia; T=Turkey

Statistical data

	1996	1997	1998	1999	2000
Basic data	in 1000				
Population (average)	10.193	10.155	10.114	10.068	10.024
	in km²				
Total area	93.030	93.030	93.030	93.030	93.030

National accounts	1000 Mio Forint				
Gross domestic product at current prices	6.894	8.541	10.087	11.393	12.877
	1000 Mio ECU/euro				
Gross domestic product at current prices	35,6	40,4	41,9	45,1	49,5
	ECU/euro				
Gross domestic product per capita ²³ at current prices	3.500	4.000	4.100	4.500	4.900
	% change over the previous year				
Gross domestic product at constant prices (nat. currency)	1,3	4,6	4,9	4,2	5,2
	in Purchasing Power Standard				
Gross domestic product per capita ²⁴ at current prices	8.600	9.300	10.000	10.700	11.700
Structure of production	% of Gross Value Added²⁵				
- Agriculture	6,6	5,9	5,5	4,8	:
- Industry (excluding construction)	26,3	28,1	28,2	27,7	:
- Construction	4,3	4,6	4,6	4,7	:
- Services	62,8	61,4	61,7	62,8	:
Structure of expenditure	as % of Gross Domestic Product				
- Final consumption expenditure	73,9	72,3	72,4	74,0	73,5
- household and NPISH	51,9	50,3	50,8	52,4	51,5
- general government	22,0	21,9	21,7	21,5	22,0
- Gross fixed capital formation	21,4	22,2	23,6	23,9	24,6
- Stock variation ²⁶	5,8	5,5	6,0	4,6	6,0
- Exports of goods and services	38,9	45,5	50,6	53,0	62,5
- Imports of goods and services	39,9	45,5	52,7	55,5	66,7

Inflation rate	% change over the previous year				
Consumer price index ²⁷	23,5	18,5	14,2	10,0	10,0

Balance of payments	In Mio ECU/euro				
-Current account	-1.339	-848	-2.020	-1.975	-1.620
-Trade balance	-2.110	-1.733	-2.080	-2.054	-2.296
Exports of goods	11.327	17.388	18.447	20.521	27.560
Imports of goods	13.437	19.121	20.527	22.574	29.855
-Net services	1.975	2.026	1.591	1.315	1.939
-Net income	-1.161	-1.263	-1.662	-1.556	-1.705
-Net current transfers	-44	122	130	320	442
-of which: government transfers	-12	-4	-40	-8	-14
- FDI (net) inflows	1.426	1.603	1.260	1.552	1.458

Public finance	in % of Gross Domestic Product				
General government deficit/surplus	-3,2	-6,8	-7,8	-5,4	-3,1
General government debt	:	64,2	62,1	60,5	55,7

²³ Figures have been calculated using the population figures from National Accounts, which may differ from those used in demographic statistics.

²⁴ Figures have been calculated using the population figures from National Accounts, which may differ from those used in demographic statistics.

²⁵ Including FISIM.

²⁶ These figures include changes in inventories, acquisitions less disposals of valuables and the statistical discrepancy between the GDP and its expenditure components.

²⁷ Changes in Methodology: PROXY HICP since 1996 (see methodological notes).

Financial indicators	in % of Gross Domestic Product				
Gross foreign debt of the whole economy	61,1	52,9	55,0	56,1	51,6
	as % of exports				
Gross foreign debt of the whole economy	157,3	116,3	108,7	105,8	82,5
Monetary aggregates	1000 Mio ECU /euro				
- M1	6,0	6,8	7,1	8,3	9,0
- M2	16,0	17,7	18,2	20,8	22,5
- M3	16,2	17,9	18,3	21,0	22,8
Total credit	18,4	26,3	25,9	25,0	27,2
Average short-term interest rates	% per annum				
- Day-to-day money rate	23,8	20,8	18,0	14,8	11,1
- Lending rate	28,2	23,0	20,1	17,2	13,1
- Deposit rate	20,6	17,6	15,4	12,6	9,2
ECU/EUR exchange rates	(1ECU/euro=..Forint)				
- Average of period	193,74	211,65	240,57	252,77	260,05
- End of period	206,91	224,71	252,39	254,70	265,00
	1995=100				
- Effective exchange rate index	85,7	79,6	71,0	66,9	63,3
Reserve assets	Mio ECU/euro				
- Reserve assets (including gold)	7.773	7.634	8.106	10.883	12.065
- Reserve assets (excluding gold)	7.743	7.607	8.081	10.854	12.036

External trade²⁸	Mio ECU/euro				
Trade balance	-1.944	-1.881	-2.407	-2.799	-4.308
Exports	12.529	16.876	20.505	23.487	30.525
Imports	14.473	18.757	22.912	26.286	34.833
	previous year=100				
Terms of trade	97,7	101,2	101,3	98,4	97,3
	as % of total				
Exports with EU-15	69,7	71,2	72,9	76,2	75,1
Imports with EU-15	62,3	62,8	64,1	64,4	58,4

Demography	per 1000 of population				
Natural growth rate	-3,7	-3,8	-4,3	-4,8	-3,8
Net migration rate (including corrections)	0,0	0,0	0,0	0,0	0,0
	per 1000 live-births				
Infant mortality rate	10,9	9,9	9,7	8,4	9,2
Life expectancy :	at birth				
Males:	66,1	66,4	66,1	66,3	67,1
Females:	74,7	75,1	75,2	75,1	75,6

Labour market (ILO methodology)	% of labour force				
Economic activity rate	48,2	48,1	48,4	49,6	50,0
Unemployment rate, total	9,9	8,7	7,8	7,0	6,4
Unemployment rate, males	10,7	9,5	8,5	7,5	7,0
Unemployment rate, females	8,8	7,8	7,0	6,3	5,6
Unemployment rate of persons < 25 years	18,0	15,9	13,5	12,4	12,1
Unemployment rate of persons >= 25 years	8,5	7,5	6,7	5,9	5,4
	as % of all unemployed				
Long-term unemployment rate	49,8	46,5	44,3	44,9	44,2
Average employment by NACE branches	in % of total				
- Agriculture and forestry	8,3	7,9	7,5	7,1	6,5
- Industry (excluding construction)	26,7	27,1	28,0	27,4	26,8
- Construction	6,0	6,0	6,2	6,6	7,0

²⁸ For 1996-1998 period, data were converted by using monthly average exchange rates. From 1999, the conversion is based on the average rates of exchanges of Eurostat.

- Services	59,1	59,0	58,3	58,9	59,7
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Infrastructure	in km per 1000 km²				
Railway network	83	83	85	85	85
Length of motorways	km				
	365	381	448	448	448

Industry and agriculture	previous year=100				
Industrial production volume indices	103,4	111,1	112,5	110,4	118,3
Gross agricultural production volume indices	106,3	96,2	97,9	103,9	96,5

Standard of living	per 1000 inhabitants				
Number of cars	223	227	220	225	235
Main telephone lines	260	304,8	334,7	359,3	347,1
Number of subscriptions to cellular mobile services	46,4	69,5	102,2	161,3	306,9
Number of Internet subscriptions	:	:	:	13,6	22,0

Methodological Notes

Inflation rate

As part of the preparations for the common currency the EU Member States (MSs) have designed a new *consumer price index* in order to comply with the obligations of the EU Treaty. The aim was to produce CPIs comparable between Member States. The main task was to harmonise methodologies and coverage. The result was the Harmonized Index of Consumer Prices (HICP). A similar exercise has been started with Candidate Countries (CC). In respect to enlargement, it is equally important that their economic performance is assessed on the basis of comparable indices. Some progress has already been made towards adapting the new rules. Since January 1999 CCs report monthly to Eurostat so-called proxy HICPs that are based on national CPIs but adapted to the HICP coverage. They are not yet fully compliant with the HICPs of the MSs. In the table, the proxy HICPs are back-calculated to 1995 (rates from 1996).

Finance

Public finance: The government deficit and debt statistics of the Candidate Countries are provisional, in the sense that they do not yet fully comply with EU methodological requirements. Broadly speaking, the general government deficit / surplus refers to the national accounts concept of consolidated general government net borrowing / net lending of ESA95. General government debt is defined as consolidated gross debt at end-year nominal value. The series are available from 1997; the 1996 data are an approximation derived from the IMF's GFS methodology.

Gross foreign debt is of the whole economy, covering both short- and long-term, but excluding equity investment and money market instruments. The source for stock of outstanding debt is OECD, while the source of GDP is Eurostat. For the ratio of gross foreign debt to exports, the national accounts definition of exports of goods and services is used (source: Eurostat). The data for 2000 are Eurostat estimates, based on joint OECD/IMF/BIS/World Bank series.

Monetary aggregates are end-year stock data, as reported to Eurostat. Generally, M1 means notes and coin in circulation plus bank sight deposits. M2 means M1 plus savings deposits plus other short-term claims on banks. M3 means M2 plus certain placements in a less liquid or longer-term form. Not all countries produce an M3 series. Total credit means loans by resident monetary financial institutions (MFIs) to non-MFI residents.

Interest rates: Annual average rates based on monthly series reported to Eurostat. Lending rates refer to bank lending to enterprises for over 1 year. Deposit rates refer to bank deposits with an agreed maturity of up to one year. Day-to-day money rates are overnight interbank rates.

Exchange rates: ECU exchange rates are those that were officially notified to DG ECFIN until 1 January 1999, when the ECU was replaced by the euro. Euro exchange rates are reference rates of the European Central Bank. The effective exchange rate index (nominal), as reported to Eurostat, is weighted by major trading partners.

Reserve assets are end-year stock data, as reported to Eurostat. They are defined as the sum of central bank holdings of gold, foreign exchange, SDRs, reserve position in the IMF, and other claims on non-residents. Gold is valued at end-year market price.

External trade

Imports and exports (current prices). The data is based upon the special trade system, according to which, external trade comprises goods crossing the customs border of the country. Trade data excludes direct re-exports, trade in services as well as licences, know-how and patents. Since 1997, trade data includes trade between industrial customs free zones and foreign markets. Since 1997 also, operative leasing and repair are excluded from external trade turnover. The data for 1996 were recalculated according to the methodological changes in 1997. Value of external trade turnover includes the market value of the goods and the additional costs (freight, insurance etc.).

Trade classification. The customs documentation is the statistical data source of external trade turnover. The data are collected according to the Combined Nomenclature. The earlier data are updated on the basis of the later processing.

The term FOB means that all costs incurred in transport up to the customs frontier are charged to the seller. The term CIF means that the purchaser pays the additional costs. Imports are recorded on CIF basis on the date of custom clearance. Exports are recorded on FOB basis with the date on which the commodities cross the state border.

Terms of trade. "Unit value" index calculation is used for measuring price changes in external trade, with the exception of heterogeneous commodity groups, where the sample method is applied for the price observation. Since the I quarter of 1996 due to the modifications in the calculation of unit value indices and the application of Fisher indices instead of Paasche indices, the quarterly volume indices has been changed.

Imports and exports with EU-15. Data declared by the Republic of Hungary.

Demography

Net migration rate. Crude rate of net migration (recalculated by EUROSTAT) for year X, is: $\text{population (X+1)} - \text{population (X)} - \text{Deaths (X)} + \text{Births (X)}$. This assumes that any change in population not attributable to births and deaths is attributable to migration. This indicator includes therefore also administrative corrections (and projection errors if the total population is based on estimates and the births and deaths on registers). Figures are in this case more consistent. Further, most of the difference between the Crude rate of net migration provided by a country and the one calculated by Eurostat is caused by an under reporting or delay in reporting of migration.

Labour force

Economic activity rate (ILO Methodology). according to the Labour Force Survey (LFS), represents the labour force as a percentage of population at working age (15 years and more), where:

- Labour force: employed and unemployed persons (according to the ILO definitions).

- The employed: all persons aged 15+, who during the reference period worked at least one hour for wage or salary or other remuneration as employees, entrepreneurs, and members of co-operatives or contributing family workers. Members of armed forces are considered as employed.

- The unemployed: all persons aged 15+, who concurrently meet all three conditions of the ILO definition for being classified as the unemployed:

have no work,

are actively seeking a job and,

are ready to take up a job within a fortnight.

LFS monitors only person's aged 15-74.

Unemployment rate (by ILO methodology). Percentage of the unemployed in labour force.

These rates are derived from LFS (Labour Force Survey) observing the ILO definitions and recommendations mentioned below.

Average employment by NACE branches (LFS). This indicator is derived from LFS (Labour Force Survey) observing the ILO definitions and recommendations.

Infrastructure

Railway network. All railways in a given area. This does not include stretches of road or water even if rolling stock should be conveyed over such routes; e.g. by wagon-carrying trailers or ferries. Lines solely used for tourist purposes during the season are excluded as are railways constructed solely to serve mines; forests or other industrial or agricultural undertakings and which are not open to public traffic. The data considers the construction length of railways.

Length of motorway. Road, specially designed and built for motor traffic, which does not serve properties bordering on it, and which:

(a) is provided, except at special points or temporarily, with separate carriageways for the two directions of traffic, separated from each other, either by a dividing strip not intended for traffic, or exceptionally by other means;

(b) does not cross at level with any road, railway or tramway track, or footpath;

(c) is specially sign-posted as a motorway and is reserved for specific categories of road motor vehicles.

Entry and exit lanes of motorways are included irrespectively of the location of the signposts. Urban motorways are also included.

Industry and agriculture

Industrial production volume indices. Industrial production covers mining and quarrying, manufacturing and electricity, gas, steam and water supply (according to the NACE Rev.1 Classification Sections C, D, E).

Index of total industrial production includes the data of all industrial enterprises. The indices by branches refer to enterprises with more than 10 employees.

Gross agricultural production volume indices. Indices were calculated using the fixed price basis applied for national accounts. Until 1996 the prices of 1991, and from 1997 the prices of 1995 serve as fixed price basis in the calculation.

Standard of living

Number of cars. Passenger car: road motor vehicle, other than a motor cycle, intended for the carriage of passengers and designed to seat no more than nine persons (including the driver).

The term "passenger car" therefore covers microcars (need no permit to be driven), taxis and hired passenger cars, provided that they have less than ten seats. This category may also include pick-ups.

Connected main line actually operating or temporarily suspended, main lines that connect terminal equipment to a switching exchange. These include private and institutional main lines, lines of public payphones and telecommunications service lines. Mobile phone lines are excluded. Connected main lines can be classified as dwelling, business and public main lines.

Note: Since the passing of the Hungarian Telecommunication Law, the Hungarian Central Statistical Office (like the countries of the EU) has been collecting data on the main lines. Before 1993, the new Telecommunication Law, statistics surveyed main stations.

Number of Internet connections. Data collection of Internet connections started in 1999.

Sources

Total area, infrastructure, industry and agriculture, external trade, labour market: **National sources.**

National accounts, inflation rate, balance of payment, public finance, finance, demography: **Eurostat.**