

# Hungarian economic particularism and EU law: simply mischievous or bad to the bone?

Marton Varju and Mónika Papp (Lendület-HPOPs Research Group, Hungarian Academy of Sciences, Centre for Social Sciences)

Contact: [varju.marton@tk.mta.hu](mailto:varju.marton@tk.mta.hu)

Authors' note: The research leading up to this article was funded by the Lendület Programme of the Hungarian Academy of Sciences. The authors are greatly indebted to the participants of the conference 'Hungarian particularism in the EU: politico-legal perspectives' held on 15 May 2015 (organised by the Lendület-HPOPs Research Group and the Center for European Union Research, Central European University).

## Abstract:

Hungary's interventions in certain sectors of the national economy raise the possibility of pursuing these violations of EU law not under the normal EU non-compliance framework, but rather under the mechanisms available to address deal-breaking Member State behaviour. The violations are serious, are systematic and follow a certain pattern, and their execution reveals intentions which seem to contradict the fundamental premises of EU membership. This article examines on the basis of the evidence collected regarding Hungary's conduct whether the current strategy of dealing with Hungarian economic particularism should be continued, or the application of Article 7 TEU or the Commission's rule of law framework should be considered.

Keywords: Hungary, economic regulation, particularism, compliance, systematic breach

Word count: 10151

This manuscript has not been submitted for publication elsewhere.

# Hungarian economic particularism and EU law: simply mischievous or bad to the bone?

## Introduction

In recent years, Hungary has gained an unsavoury reputation for being a Member State that habitually prioritizes its own interests over those of the Union and of other Member States. Its conduct, which can be interpreted as a strong form of Member State particularism in the EU, has led to intra-Union conflicts in a number of areas ranging from the novel politico-constitutional system established after 2010 to its unilateral actions introduced as part of Hungary's own policy towards global migration. The economic policy pursued in Hungary after 2010 is also characterized by particularism. The restructuring of certain sectors of the national economy was initiated with the knowledge that the measures adopted violate EU obligations, which violations were committed to secure advantages for local economic operators favoured by the government and/or for the Hungarian State. The infringement and State aid procedures initiated by the Commission together with the preliminary ruling cases decided by the ECJ concerning developments in Hungarian economic regulation, we presume, now provide sufficient information to assess these developments not as isolated cases of EU infringements, but rather as a systematic contradiction by Hungary of its original commitments as a Member State of the Union.

Establishing in law that Hungary's obstruction of EU obligations in the economic domain constitutes a conduct which breaks the deal entered into upon gaining membership in the Union is, however, fraught with legal and conceptual difficulties. Firstly, because of the wealth of legal principles available to deal with even extreme forms of Member State non-compliance, there may not be need to address Hungarian economic particularism as deal-breaking Member State conduct. Hungarian economic particularism can be duly addressed on a case by case basis as a violation of the principles of loyalty and of equal and mutual compliance, and of the prohibitions on unilateral conduct and on acting in bad faith. Secondly, with these in place, the need to apply the different EU mechanisms available to deal with deal-breaking conduct by the Member States – Article 7 TEU or the Commission's rule of law framework – only arises when the systematic or exceptional nature of the violations, or the habitual misuse of law and administration by the government can be, or need to be expressed. Their applicability in a case, such as that of Hungary is, however, uncertain. The political nature of these mechanisms and the high thresholds of their actual application may prevent treating developments in Hungarian economic policy at their real value: as a case of a Member State violating the conditions of its membership in the Union. Finally, there are a number of issues, which arise from the context of the Hungarian case, the assessment of which may ultimately support addressing a case, such as Hungary's controversial interventions in certain markets not as deal-breaking conduct. These issues indicate why, despite gravity and the systematic nature of the infringements, Member State (mis)conduct should be pursued on a case-by-case basis as violations of individual obligations laid down in EU law.

The article is structured as follows. It first looks at developments in Hungarian economic policy after 2010 and their treatment under EU law. Then, it examines what the legal principles governing Member State non-compliance offer in addressing a case, such as Hungarian economic particularism.

This is followed by the analysis of the EU mechanisms available to address Member State deal-breaking conduct and their limitations. Finally, we look at the issues which, despite the need for a more robust legal and political treatment of Member State (mis)conduct, support the use of the normal non-compliance framework. This work does not address the controversies surrounding the introduction after 2010 of a novel politico-constitutional order in Hungary.<sup>1</sup> Nor does it cover the handling of the asylum and migration crisis by the Hungarian government, which has led to claims of violation of EU<sup>2</sup> and international law,<sup>3</sup> and to Hungary's recent legal challenge of the Council's resettlement decision.<sup>4</sup>

### **Particularism in Hungarian economic policy and regulation**

Since 2010, the promotion of local interests, even at the expense of meeting EU obligations, has become a hallmark of Hungarian economic policy in *certain* economic sectors.<sup>5</sup> The Hungarian government under pressure from ailing public finances and a prolonged economic crisis, and pursuing a curious list of policy priorities, developed a taste for adopting measures which, supposedly for the 'national good', aimed at restructuring national markets. This policy direction offers an example of strong Member State particularism in the EU. The notion of particularism, when used in the context of economic relations, denotes State conduct such as the exclusive promotion of one's economic interests, economic nationalism (or patriotism), protectionism, exclusionary practices directed towards foreign economic operators, and the re-enclosure of national markets.<sup>6</sup> In a framework, such as the EU Single Market, Member State particularism manifests in discriminatory and other practices which aim to benefit local economic operators, and also in Member State free-riding and 'beggar-thy-neighbour' policies, which cause disadvantages to the other Member States and to the Union.

Hungarian economic particularism of late, in our interpretation, stands for national practices of economic regulation which intentionally obstruct EU obligations, and which pursue the opportunist aims of inconveniencing the incumbent, predominantly foreign, economic operators in a market and of restructuring those markets to the benefit of local economic operators, or of the State.<sup>7</sup> It involves

---

<sup>1</sup> On the unfolding of these events, see Sonnevend, Jakab and Csink, "The Constitution as an instrument of everyday party politics: the Basic Law of Hungary" in von Bogdandy and Sonnevend (Eds.), *Constitutional Crisis in the European Constitutional Area* (Hart, 2015) pp. 33-110.

<sup>2</sup> <[http://europa.eu/rapid/press-release\\_IP-15-5699\\_en.htm?locale=en](http://europa.eu/rapid/press-release_IP-15-5699_en.htm?locale=en)> (last visited 01 March 2016).

<sup>3</sup> <<http://www.unhcr.org/55f9a70a6.html>> (last visited 05 January 2016).

<sup>4</sup> Case C-647/15, *Hungary v. Council*, O.J. 2015, C 38/43. For a preliminary analysis, see Varju and Czina, "Hitting where it hurts the most: Hungary's legal challenge against the EU's refugee quota system", *VerfBlog*, 2016/2/17, <<http://verfassungsblog.de/hitting-where-it-hurts-the-most-hungarys-legal-challenge-against-the-eu-refugee-quota-system/>> (last visited 08 March 2016).

<sup>5</sup> The first indication perceptible in EU law of a 'realist' turn in Hungarian European politics was the launching of an infringement procedure against Slovakia (Case C-364/10, *Hungary v. Slovakia*, EU:C:2012:630). The symbolic triple infringement procedures initiated against Hungary in 2012 (IP-12-24) showed the realization at the EU level that Hungary is not afraid of moving away from its EU commitments if dictated by its interests.

<sup>6</sup> On economic nationalism as a policy, see, foremost, List, *The National System of Political Economy* (trans. Sampson S. Lloyd), (Longman, 1909), and its interpretation, Levi-Faur, "Friedrich List and the political economy of the nation state", 4 *Review of International Political Economy* (1997), 154-178.

<sup>7</sup> Retrospectively, one of the first Hungarian preliminary ruling cases concerning discrimination in the taxation of second-hand vehicles (Joined Cases C-290/05 and C-33/05 *Nádasdi*, EU:C:2006:652) could be regarded as Hungary knowingly risking the violation of EU law in order to secure the market position of certain domestic economic operators.

the use of a combination of instruments, such as sudden increases in tax burdens, discriminatory taxation, regulation closing down markets without offering a transitional period or compensation to the affected individuals, preferential or discriminatory licensing and concessions, and administrative decision-making processes characterized by a low degree of transparency and an excessive degree of executive discretion. In certain markets, legal regulation was used to coerce economic operators or their consumers to make a particular ‘choice’ – mainly, the choice of abandoning the market – which would then enable the government to achieve its aims. As established by the legal challenges brought against government intervention, the rights and legitimate expectations of the individuals affected were disregarded, public authorities proceeded in an arbitrary manner, and regulatory measures were introduced in bad faith with an intended gap between their declared policy aims and their actual implementation.<sup>8</sup> Furthermore, the quality and transparency of regulation and the related governance processes were kept at a low level in order to ensure that changes can be implemented unopposed and unchallenged, and that by the time their unlawfulness is established their reversal may no longer be possible.

In our view, there is now sufficient evidence to assess Hungary’s misconduct affecting a considerable segment of the Hungarian market<sup>9</sup> as an intended and systematic violation of the deal entered into upon gaining membership in 2004. The intention of prioritising domestic interests over EU obligations was made particularly visible in the recent infringement case concerning the payment of excise duties for the production of ethyl alcohol (*pálinka*) by private individuals.<sup>10</sup> The judgment and the explanations raised by Hungary both confirmed that the national measure, much liked by certain social groups, was adopted in the knowledge that its provisions violate the earlier implemented EU directive. The intentional delaying of the implementation of the Waste Directive<sup>11</sup> seems to have been a crucial factor in the government’s plans for the national enclosure of the waste market. By the time the infringement procedure was closed on account of Hungary implementing the directive,<sup>12</sup> the incumbent, predominantly foreign-owned economic operators had been expelled from the waste collection market and the sector had been re-nationalized.<sup>13</sup> The waste management market was also restructured under the national Waste Management Agency which was responsible for

---

<sup>8</sup> Government conduct was a cynical as passing legislation with titles that mention choices made available to individuals when in fact the outcome and implementation of the measure was to coerce individuals into a particular decision, see Act 2010:C on the freedom to choose private pension funds and Act 2010:CLIV on implementing the freedom to choose private pension funds.

<sup>9</sup> We have not been able to collect sufficient evidence regarding what is suspected to be a habitual distortion of the Hungarian public procurement market (see, however, COM(2015) 266 final, “2015 Reform Programme and 2015 Convergence Programme of Hungary”, at 5-6) and what government practices of declaring public and private investment projects as ‘specifically relevant for the national economy’ (Act 2006:LIII) mean for the Single Market.

<sup>10</sup> Case C-115/13, *Commission v. Hungary*, EU:C:2014:253.

<sup>11</sup> Directive 2008/98/EC on waste, O.J. 2008, L 312/3.

<sup>12</sup> Order in Case C-310/12 *Commission v. Hungary*, EU:C:2013:556.

<sup>13</sup> Art. 81 of Act 2012:CLXXXV holds that licences may only be issued to undertakings which are directly or indirectly controlled by the State or by local councils. Coercion by compulsory price reduction to reconsider business plans was also used, see Act 2013:LIV. The same instrument of compulsory price reduction in the public utilities sector, which in domestic politics was presented as a response to a ‘cost of living crisis’ (*rezsicsökkentés* in the colloquial Hungarian used in the political campaign leading up to the 2014 elections), was used to prepare the renationalization of the energy retail sector. The incumbent economic operators, thus affected, handed back their licences before their expiry, and a new State monopoly was established in 2015 by Regulation 7/2015 of the Ministry for National Development under the name First National Public Utility Corporation.

managing the system of public contracts concluded for waste management services with economic operators.<sup>14</sup> The tenders have so far been won by a particular group of Hungarian undertakings which are now under investigation by the Hungarian competition authority under public procurement cartel charges.<sup>15</sup> In these circumstances, the eventual transposition of the directive served the purpose of conserving in law the new market structure.

#### *Intentional violations in the tax-free remunerations voucher market*

The closure of the market for the provision of tax-free remunerations (non-salary allowances) by public and private employers in the form of paper and electronic vouchers, and the circumstances of opening a new market for electronic vouchers give a clear example of how the Hungarian government may interfere with domestic markets on behalf of its own interests. The market populated by foreign economic operators was closed without offering a genuine transitional period in 2011 by establishing a State monopoly for the paper voucher market, and by means of imposing a 51 per cent tax on the market incumbents whilst reserving the tax-free status previously enjoyed by them for the new market entrant.<sup>16</sup> The new market created for electronic vouchers<sup>17</sup> (the *SZÉP*-card) was regulated in a manner which, in the words of the Commission, *de facto* reserved entry to the market to the three large banks domiciled in Hungary.<sup>18</sup> The conditions for gaining a licence to issue electronic vouchers included, among others, primary establishment and a primary place of management in Hungary.

The infringement case brought by the Commission<sup>19</sup> made it clear that Hungary's intervention constituted an intentional obstruction of EU obligations. The Advocate General's opinion, which examined the infringement mainly under the Treaty fundamental freedoms, seems to suggest that the government must have been aware of the risks under EU law of replacing incumbent market operators with a State monopoly, and of allowing the entry to the new market only of domestic economic operators preferred by the government.<sup>20</sup> As opposed to the Advocate General, the Grand Chamber of the ECJ decided to address the infringement concerning the opening of the new market under the Services Directive,<sup>21</sup> which may be taken as a further confirmation that the violation by Hungary of its EU obligations must have been known to the government on the basis of the clearly worded provisions of that directive. The Court's reasoning also revealed that the Hungarian government, which perhaps in domestic legislation communicates the declared rationales of its policies too confidently, was unable to point to any rational justification for its conduct as far as the issue of market regulation is concerned. It also failed to dismiss the suspicion that its intervention

---

<sup>14</sup> Act 2012:CLXXXV. The agency was shut down by Government Decree 322/2014, and its functions were transferred to the National Environmental Authority. Characteristically for the Hungarian government, in 2014 Act 2011:LXXXV was supplemented by Art. 22/C which retrospectively excluded the application of the Hungarian competition act in regards anti-competitive conduct committed in the 2012-2013 tendering year.

<sup>15</sup> Vj/67/2014.

<sup>16</sup> Act 2011:CLV.

<sup>17</sup> Act 2011:CLVI, Act 1993:XCVI and Government Regulation 55/2011.

<sup>18</sup> Action brought on 10 April 2014 in Case C-179/14, *Commission v. Hungary*, O.J. 2014, C 202/12.

<sup>19</sup> Case C-179/14, *Commission v. Hungary*, EU:C:2016:108. There is an ongoing international investment arbitration case before the ICSID (ICSID Case No. ARB/13/35).

<sup>20</sup> Paras. 89-159 and 220-244, Opinion of Advocate General Bot in Case C-179/14, *Commission v. Hungary*, EU:C:2016:619.

<sup>21</sup> Directive 2006/123/EC on services in the internal market, O.J. 2006, L 376/36.

through law was motivated by the intention to help the State and a group of favoured undertakings to a lucrative market.

The assessment of the Court of the new market created for electronic vouchers established the violation of core provisions<sup>22</sup> of the Services Directive, and rejected attempts at the justification of those violations either on the ground that Hungary had failed to provide any evidence in support of its claims,<sup>23</sup> or that they had clearly failed to meet the directive's requirement of proportionality.<sup>24</sup> The setting up of the new State monopoly in the paper voucher market did not receive a more favourable treatment. Proceeding under Articles 49 and 56 TFEU, the ECJ first dismissed claims that the State monopoly, which collects fees from the market, was not covered by those provisions,<sup>25</sup> and then rejected the public interest grounds raised in justification by Hungary, either, for being irrelevant in the context of the State intervening in a market,<sup>26</sup> or, for not being supported by evidence.<sup>27</sup> The failure of the case prepared by Hungary, especially that of the social policy grounds raised,<sup>28</sup> seems to confirm that legal regulation was used to restructure a market without Hungary being able to give assurances that it pursued genuine policy aims and not just the whim of the government. Unfortunately, the legal circumstances in which the Hungarian government repealed the incumbents from an entire market – in particular, the failure to grant a genuine transitional period, or the use of tax legislation to inconvenience market participants – were not assessed by the ECJ.<sup>29</sup>

#### *Abusive regulation in the private pensions market*

The partial abolishment of the Hungarian private-pensions market was carried through in a similar manner. In 2010, the Hungarian government, facing serious financial difficulties, used legal regulation to force economic operators to abandon the market, which was the private tier of the mandatory pension system, and to redirect its assets to the public tier of that system. This took place without allowing a genuine transitional period for the individuals affected to adapt to the changes, and with the government using openly discriminatory legal measures to coerce market participants and consumers to make the single 'choice' offered to them in law. The subsequent withdrawal of the discriminatory provisions in 2011 does not change this assessment as the presumed purpose of this move was to prevent, just in time and just after the successful restructuring of the market, legal challenges against government policy.<sup>30</sup>

---

<sup>22</sup> Articles 14 and 15: paras. 46-47, 54-67, 81-88, 89-90, 102-107, Case C-179/14, *Commission v. Hungary*.

<sup>23</sup> Paras. 69, 92-94, 115-116, *ibid*, such as the interest of sufficient integration into the local economy, the availability of sufficient experience and infrastructure, and the availability of sufficient guarantees to satisfy consumers and creditors.

<sup>24</sup> Para. 91, *ibid*.

<sup>25</sup> Paras. 147-164, *ibid*.

<sup>26</sup> Paras. 167-170, *ibid*.

<sup>27</sup> Paras. 171-173, *ibid*.

<sup>28</sup> See Act 2012:CIII. In particular, the interest of delivering social policy through State institutions and the redistribution (here, more like rechanneling) of incomes to finance social policy aims.

<sup>29</sup> Para. 174, Case C-179/14, *Commission v. Hungary*, but discrimination and *de facto* national favouritism were.

<sup>30</sup> ECtHR, *E.B. (No. 2) v. Hungary*, Appl. No. 34929/11, judgment of 15 January 2013, which rejected the application but made the criticism that there was no choice involved for individuals as promised by legislation. See the applications rejected by the Hungarian Constitutional Court, *infra* note 31.

The acts adopted towards the end of 2010<sup>31</sup> damaged the prospects of market incumbents by suspending for a year the payment obligations of their clients and offering to them, in parallel, the possibility of abandoning their pension insurers and returning to the public tier. Although these measures were adopted with the intention of expressing publicly that market prospects are damaged by the choices taken by consumers, it is evident that the changing of market circumstances through these measures led to consumers anxious to protect their pension savings making the single reasonable choice of abandoning the market. The ultimate push for consumers (citizens) came in the form of the subsequently withdrawn<sup>32</sup> Act 2010:CLIV which threatened those that had decided to remain in the market with the loss of their entitlements in the public tier of the mandatory pension system from 31 January 2011. The curtailment of the relevant review competences of the Hungarian Constitutional Court, which took place only a short time before the adoption of the first of these measures,<sup>33</sup> further supports that the government was indeed determined to move ahead with its policy without having regard to its negative impact on individuals. The Commission never pursued this matter in law,<sup>34</sup> which may have to do with the earlier mentioned circumstance that the legally most controversial measure was kept in force for just enough time to convince citizens to leave the market.

#### *Arbitrary intervention in the tobacco market*

The radical restructuring of the market for tobacco products followed the same pattern of government intervention. In the retail market, the entry of new economic operators, some of which also had interests in the wholesale market, and the exclusion of incumbent economic operators were achieved without granting a genuine transitional period through the application of legal measures which not only opened the door for the arbitrary use of public powers, but also failed to ensure that the proprietary rights and legitimate expectations of the affected individuals were adequately protected.<sup>35</sup> As opposed to the Constitutional Court, which deferred to the government's policy discretion in this matter,<sup>36</sup> the Court of Human Rights in Strasbourg found that the exclusion of incumbent economic operators from the market in this manner violated Convention rights.<sup>37</sup>

The entry into the wholesale market of a new economic operator, the market position of which is protected by a concession, was administered in similarly boisterous conditions. The legal preparation and the actual carrying out of the concession process raise doubts as to whether the selection of the concession holder and the parallel reduction of market opportunities for its competitors were based on objective and, from the perspective of the operation of the tobacco market, relevant criteria.<sup>38</sup>

---

<sup>31</sup> Acts 2010:C and Cl.

<sup>32</sup> Act 2011:CXCIV.

<sup>33</sup> Act 2010:CXIX. The Constitutional Court lacking the necessary competences rejected all applications contesting the constitutionality of the government intervention as inadmissible, Decisions 3291/2012, 3292/2012, 3293/2012, 3294/2012, 3295/2012, 3296/2012 and 3243/2012.

<sup>34</sup> Its position was weakened by the fact the according to the Hungarian government the closure of this market and the channelling of its assets to the public purse was necessitated by the Commission's controversial decision earlier in 2010 to reject the request of Hungary and 8 other Member State to take into account the costs of pension system consolidation in calculating budget deficits under Article 128 TFEU.

<sup>35</sup> Act 2012:CXXIV.

<sup>36</sup> Decision 3194/2014.

<sup>37</sup> ECtHR, *Vékony v. Hungary*, Appl. No. 65681/13, judgment of 13 January 2015.

<sup>38</sup> Act 2014:XCIV. The act introduced the notion of 'trustworthy' economic operators among the conditions of gaining a concession.

Since the government's intervention affected an entire national market, it is not surprising that the Commission decided to prepare an investigation into these changes.<sup>39</sup> The tobacco industry's special tax (healthcare contribution), which was introduced in parallel with these developments, provided that customary fiscal instrument used when preparing markets for their subsequent restructuring.<sup>40</sup> The application of the progressive elements of the tax, which seem to disfavour certain economic operators while favouring others, was ordered to be suspended by the decision of the Commission initiating an investigation into the tax under State aid law.<sup>41</sup>

#### *Regulatory practices in bad faith in the gambling market*

The gambling market suffered a similar regulatory restructuring. The exclusion of incumbents from the slot machines market and the placing of that market under the control of certain economic operators were prepared by the fiscal instrument which, without providing a genuine transitional period, quintupled the tax on slot machines operated in amusement arcades, but not in casinos, and introduced a new flat-rate tax on that activity.<sup>42</sup> This was followed by the legal measure, which again without granting a transitional period and without offering compensation, prohibited the operation of slot machines outside of licensed casinos.<sup>43</sup> In parallel with these changes, the modification of the Act on gambling liberalized the online gambling market,<sup>44</sup> and in connection with the granting of gambling concession introduced special, relaxed rules for so-called 'trustworthy gambling service providers'.<sup>45</sup>

The ECJ's assessment of these changes in *Berlington* gave a clear condemnation of the government's practices. The new tax burdens were held to violate the Treaties in case it is established before the national court that the effect of those burdens is to restrict the operation of slot machines to casinos and to exclude amusement arcades from that activity.<sup>46</sup> The prohibition of operating slot machines outside of licensed casinos was found to violate EU law on the ground that the prohibition itself excluded amusement arcades from that market.<sup>47</sup> This latter rule was also held to violate Directive 98/34/EC for being a technical specification which should have been notified to the Commission.<sup>48</sup>

Concerning the justifiability of the restrictions introduced in the slot machines market, although Hungary's interference seemed *prima facie* legitimate,<sup>49</sup> the ECJ entertained doubts as to whether the restrictive Hungarian policy was entirely consistent and systematic taking into account the fact that the modifications of the Act on gambling opened up significant new opportunities in the market.<sup>50</sup> The ultimate condemnation of Hungary's intervention was provided in the assessment of the related fundamental rights issues, where the Court, with a cross-reference to the earlier

---

<sup>39</sup> IP-15-5375.

<sup>40</sup> Act 2014:XCIV.

<sup>41</sup> SA.41187.

<sup>42</sup> Act 2011:CXXV.

<sup>43</sup> Act 2012:CXLIV. The measure was upheld as constitutional by the Constitutional Court which decided to defer to the policy discretion enjoyed by government in this area, Decision IV/03576/2012.

<sup>44</sup> Act 2013:CXXVI.

<sup>45</sup> Act 2013:CLXXXV.

<sup>46</sup> Paras. 37-42, Case C-98/14, *Berlington*, EU:C:2015:386.

<sup>47</sup> Paras. 50-63, *ibid.*

<sup>48</sup> Paras. 93-100, *ibid.*

<sup>49</sup> Para. 56, *ibid.*

<sup>50</sup> Paras. 64, 67-70, *ibid.*

mentioned Strasbourg ruling on the restructuring of the tobacco market,<sup>51</sup> found the violation of the principles of legal certainty and the protection of legitimate expectations. In its view, when the Member States revoke 'licences that allow their holders to exercise an economic activity, it must provide, for the benefit of those holders, a transitional period of sufficient length to enable them to adapt or a reasonable compensation system.'<sup>52</sup> It also established that 'a trader who has made costly investments in order to comply with the scheme adopted previously by the legislature could see his interests considerably affected by the withdrawal of that scheme before the date announced, all the more so if that withdrawal takes place suddenly and unforeseeably, without leaving him enough time to adapt to the new legal situation.'<sup>53</sup>

#### *Arbitrary practices in the food retail market*

Similar patterns characterized the government's interventions in the domestic food retail sector, the beneficiaries (local retail chains) and the sufferers (foreign-owned supermarket chains) of which are quite clearly distinguishable. Discriminatorily selective fiscal burdens, which give advantages to certain economic operators while disadvantaging their competitors, are again among the regulatory instruments used.<sup>54</sup> Hungary as a norm defends these taxes as having a progressive rather than a selective nature. These defences have not been seen favourably under EU law. While it is accepted that progressive indirect taxes do not *per se* violate EU law, progressive elements which lead to direct or indirect discrimination prohibited under EU law,<sup>55</sup> or which violate State aid law on account of their selective nature<sup>56</sup> are illegal. The progressive food-chain supervision fee imposed on the food retail sector in 2014<sup>57</sup> is now under investigation by the Commission under State aid law, the decision of which ordered its suspension.<sup>58</sup> Hungary reacted instantly to the criticism and moderated the progressive nature of the fee by repealing its 0 per cent rate favouring predominantly local retail chains.<sup>59</sup>

With entry into the food retail market being less regulated than in other markets, the Hungarian government had to come up with more innovative, but perhaps less effective forms of exclusionary intervention than granting new licences and concessions, or establishing a State monopoly. These include the practice implemented in parallel with the radical restructuring of the tax-free remuneration vouchers market that for a considerable amount of time only Hungarian established retail chains were licensed to accept the new State vouchers as a legal tender.<sup>60</sup> The parallel

---

<sup>51</sup> *Vékony v. Hungary*, Appl. No. 65681/13.

<sup>52</sup> Paras. 74-91, especially, paras. 85 and 87, Case C-98/14, *Berlington*.

<sup>53</sup> *ibid.*

<sup>54</sup> See, from above, the tobacco industry healthcare contribution, the taxes imposed on operators of slot machines, and the 51 per cent tax in the vouchers market. The media market was affected by its own progressive tax (the provisions of Act 2014:LXXIV on the so-called advertisement tax), which is now under investigation under State aid law (SA.39235). It is also investigated under the freedom of establishment (IP-15-4598).

<sup>55</sup> Paras. 37-41, Case C-385/12, *Hervis*, EU:C:2014:47; paras. 37-42, Case C-98/14, *Berlington*; the investigation into the advertisement tax under freedom of establishment, *supra* note 54.

<sup>56</sup> See the case of the tobacco industry healthcare contribution, *supra* note 41 and the case of the advertisement tax, *supra* note 54.

<sup>57</sup> Act 2014:LXXIV.

<sup>58</sup> SA.40018.

<sup>59</sup> Act 2015:XLVI.

<sup>60</sup> <[http://nol.hu/gazdasag/erzsebet\\_utalvany\\_utan\\_szep\\_kartyat\\_is\\_elfogadhat\\_\\_a\\_tesco-1315548](http://nol.hu/gazdasag/erzsebet_utalvany_utan_szep_kartyat_is_elfogadhat__a_tesco-1315548)> (last visited 25 Feb. 2016).

modification of the Act on commerce by Act 2014: CXII, which penalizes undertakings in the retail sector with an annual net income of 15 billion HUF with a compulsory suspension of their commercial activities if they fail to report profits in two successive years, is now under investigation by the Commission (letter requesting information sent in February 2016). Planning law offered another means of interfering with the market positions of economic operators in the food retail market. New, stricter rules were introduced for the planning of commercial premises,<sup>61</sup> which were then applied under broad ministerial powers in procedures lacking transparency predominantly to the benefit of local food retail chains.<sup>62</sup>

### **Hungarian economic particularism and EU law: simple non-compliance or a deal-breaker?**

The earlier discussed developments in Hungarian economic policy were pursued in EU law following the standard avenues – infringement and State aid procedures, and legal challenges before national courts – available to deal with the failures of the Member States to comply with their EU obligations. The choice of these avenues, as demonstrated above, has yielded results but there remains the nagging question whether considering the apparent trend-like patterns of government intervention, which include the intentional obstruction of EU obligations, the opportunistic favouring of domestic economic interests, and arbitrary and abusive uses of law and administration, Hungary's non-compliance should instead be treated as deal-breaking conduct. In certain sectors of the national economy, Hungary seems to systematically and knowingly violate core obligations laid down in core EU policies which suggest that in this context it treats these sectors as not forming part of the Single Market.

In order to explore whether this choice is indeed available, first the extent of the obligation of compliance imposed on the Member States<sup>63</sup> needs to be analysed. Determining what principles covering what Member State (mis)conduct are covered by the EU non-compliance framework is essential to establish whether in a case, such as Hungarian economic particularism, the EU should look for more robust avenues to police what seems like a systematic violation of EU obligations. Secondly, provided that the nature and the weight of violations justify their use, it needs to be determined whether the current frameworks available in EU law to address deal-breaking conduct by the Member States are indeed suitable to deal with such acute instances of disobedience. Apart from the practical limitations of these mechanisms, account must be taken of the particular circumstances, which may arise in cases, such as that of Hungary, which by complicating the assessment of deal-breaking conduct may point towards the better utility of the normal EU non-compliance framework even when the conditions of EU membership are put into jeopardy by developments at the national level.

#### *The obligation of compliance*

---

<sup>61</sup> Act 2012: CLVII. The Commission closed the infringement procedure initiated in this matter on 25 February 2016 (Infringement number 20132086).

<sup>62</sup> <<http://tldr.444.hu/2015/11/30/az-elelmiszerpiacot-akartak-atrendezni-a-plazastoppal>> (last visited 22 Feb. 2016). The decisions taken by the minister were only made public following a FOI request by investigative journalists.

<sup>63</sup> It is anchored primarily in Article 4(3) TEU.

The obligation of compliance finds its broadest basis in the commitment made by the Member States<sup>64</sup> that the fulfilment of their obligations in the Union, in which they decided to participate on a voluntary basis, will not be treated as optional.<sup>65</sup> In the EU, once obligations are agreed upon and adopted in law, the Member States forego their right of disobedience, and they are obliged to give effect to their self-imposed obligations.<sup>66</sup> In the foundational jurisprudence of the ECJ, this consequence of EU membership was expressed in the Court interpreting Member State obligations as ‘unconditional’ and ‘irrevocable’.<sup>67</sup> The obviousness and certainty given by law to the obligations of the Member States was assessed in the literature as being essential for ensuring the stability and continuity<sup>68</sup> of common policies and for preventing Member States from causing harm to other Member States.<sup>69</sup> It was suggested by the ECJ that compliance ensures to everyone’s benefit that EU policies prevail with uniform force throughout the Union and, as a consequence, the common objectives for which the Union was established are achieved.<sup>70</sup>

### The principle of loyalty

The Treaty basis of Member State compliance is provided in Article 4(3) TEU which demands loyal and sincere cooperation from the Member States. The loyalty principle binds the Member States ‘in all the areas corresponding to the objectives of the Treaties’.<sup>71</sup> It thus covers nearly every dimension of Member State conduct within the Union reaching well beyond their core obligations in the implementation of EU policies. Article 4(3) TEU also applies in domains where the Member States have retained their competences, or where the Member States, in absence of EU regulatory involvement, enjoy autonomy or discretion in regulating and administering society and the market.<sup>72</sup> It requires that the Member States take all appropriate measures to ensure the fulfilment of the obligations arising out of the Treaty,<sup>73</sup> facilitate the achievement of the Union’s tasks, and abstain

---

<sup>64</sup> Article 1(1) TEU holds that the Union was established by the Member States to enable them to pursue in the framework of common policies certain shared interests for which purpose they transferred to it the necessary competences.

<sup>65</sup> See the discussion on the terms ‘voluntary’ and ‘optional’ in the context of EU membership by Dickson and Eleftheriadis, “Introduction: the puzzles of European Union law” in Dickson and Eleftheriadis (Eds.), *Philosophical Foundations of EU Law* (OUP, 2012), pp. 1-24, at 12.

<sup>66</sup> In the literature on legal integration, law is regarded as an agent of integration (see, *inter alia*, Eriksen, *The Normativity of the European Union* (Palgrave, 2014), pp. 26-43) which is able to give assurance that the voluntarily undertaken commitments of the Member States are in fact honoured. The idea of heavily legalized transnational governance (the use of legal formalism in determining Member State obligations) appeared as early as the Schuman Declaration, Weiler, “Deciphering the political and the legal DNA of European integration: an exploratory essay” in Dickson and Eleftheriadis, *op. cit. supra* note 65, pp. 137-158, at 150.

<sup>67</sup> Para. 18, Case 106/77, *Simmenthal*, EU:C:1978:49.

<sup>68</sup> Ensures their ‘effectiveness’ in the terminology used by the ECJ, see para. 21, Case 148/78, *Ratti*, EU:C:1979:110.

<sup>69</sup> ‘Transnational legality helps prevent “free riding” and provides stability and continuity to any *acquis* even in periods of political instability and wavering commitment’, Weiler, *op. cit. supra* note 66, at 150-151.

<sup>70</sup> Case 6/64, *Costa*, EU:C:1964:66 and para. 18, Case 106/77, *Simmenthal*. See Pescatore, *The Law of Integration* (Sijthoof, 1974), at 50.

<sup>71</sup> Opinion 1/03 EU:C:2006:81.

<sup>72</sup> *Inter alia*, para. 3, Joined Cases 51 to 54/71, *International Fruit Company NV*, EU:C:1971:128; para. 20, Case C-453/00, *Kühne & Heitz NV*, EU:C:2004:17; paras. 56-57, Joined Cases C-231/00, C-303/00 and C-451/00, *AIMA*, EU:C:2004:178.

<sup>73</sup> The Member States must take all measures to guarantee the application and effectiveness of EU law, para. 46, Case C-354/99, *Commission v. Ireland*, EU:C:2001:550.

from any measure which could jeopardize the attainment of the objectives of the Treaty.<sup>74</sup> In some of the early jurisprudence, the principle was linked to the original commitment made by the Member States upon gaining membership when it held that loyalty stands for the obligation of the Member States to recognize the consequences in their internal order of their accession to the Union.<sup>75</sup>

#### The equal and mutual compliance principle

The Member States aiming to test their possibilities under the Treaties need to bear in mind that the obligation of compliance stands for the equal and mutual observation by every Member State of their EU obligations. This extension of the principle follows from the earlier introduced component of the case law which holds that without equal and mutual compliance the realization with uniform force of common policies throughout the Union could be jeopardized.<sup>76</sup> Some of the early jurisprudence went beyond this idea of policy effectiveness, and offered a positive, more broadly framed footing for Member State compliance and for the requirements of equality and mutuality within the obligation of compliance. The value of this case law is, however, doubtful as it was not followed in subsequent case law.<sup>77</sup> In the relevant rulings, the ECJ interpreted the Union as an arrangement in which profiting from the advantages of common action comes with the cost for its members of respecting its rules.<sup>78</sup> It also suggested that equal compliance is an expression of the groundrule that the Member States in the Union are equal<sup>79</sup> and that their nationals must be treated equally in every Member State.<sup>80</sup> In other cases, the Court's reasoning also made reference to the idea that equal and mutual compliance serves as an incentive for the Member States to meet their obligations as it promises that they can expect and trust other Member States to do the same.<sup>81</sup>

#### The prohibition of unilateral conduct

As a corollary to the equal and mutual compliance principle, EU law prohibits unilateral conducts by the Member States in the Union. This prohibition addresses the Member States choosing to knowingly and willingly contradict in pursuance of their own interests, and to their own advantage and possibly to the disadvantage of other Member States, their voluntarily undertaken commitments in the Union.<sup>82</sup> In *Costa*, the ECJ made it explicit that the Member States must not unilaterally depart

---

<sup>74</sup> Para. 21, Case 22/70, *Commission v. Council*, EU:C:1971:32.

<sup>75</sup> Para. 11, Case 30/72, *Commission v. Italy*, EU:C:1973:16 and paras. 6-8, Case 50/76, *Amsterdam Bulb*, EU:C:1977:13.

<sup>76</sup> *Supra* note 70.

<sup>77</sup> Paras. 143 and 147, Opinion of Advocate General Kokott in Case C-370/12, *Pringle*, EU:C:2012:675.

<sup>78</sup> Para. 24, Case 39/72, *Commission v. Italy*, EU:C:1973:13 and para. 12, Case 128/78, *Commission v. UK*, EU:C:1979:32. In a more constructive interpretation, the benefits of cooperation can only be realized by individual Member States in case they, together with other Member States, comply with their common obligations.

<sup>79</sup> Laid down in Article 4(2) TEU.

<sup>80</sup> Para. 24, Case 39/72, *Commission v. Italy* and para. 12, Case 128/78, *Commission v. UK*.

<sup>81</sup> According to the Court, it is irrelevant from the perspective of Member State compliance that meeting EU obligations imposes different burdens on the Member States depending on the state of national regulation and governance. It argued that if the obligation at issue (the harmonization measure) applies equally to all Member States this form of differentiation among the Member States does not constitute unlawful discrimination, *Tridimas, The General Principles of EU Law*, 2<sup>nd</sup> ed. (OUP, 2006), at 95 referring to para. 20, Case C-331/88, *Fedesa*, EU:C:1990:391.

<sup>82</sup> Member State unilateral conduct was held to be capable of 'defeating' the effectiveness of EU obligations, para. 30, Case 2/74, *Reyners*, EU:C:1974:68. The Member States cannot justify unilateral opt-outs from their obligations on the basis of the difficulties faced when complying with them, para. 10, Case 128/78, *Commission*

from their EU obligations.<sup>83</sup> The judgment in *Simmenthal* confirmed this, and declared that the obligations of the Member States are unconditional and irrevocable and the Member States are, thus, prevented from changing their mind as far as their legal obligations of the time are concerned.<sup>84</sup> The ECJ, referring to ‘the principle of precedence of Community law’, also confronted the Member States with the idea that their unilateral disobedience has the effect of undermining their earlier commitments and the effectiveness of the related common policies.<sup>85</sup> A later ruling made it explicit that the incomplete and selective application of EU law by the Member States is prohibited even when they have opposed the adoption of the EU measure in question, or they consider it to be contrary to their ‘national interests’.<sup>86</sup>

The Member States have also been reminded by the ECJ that their obligations are not of a reciprocal nature, which means that they may not unilaterally adopt, ‘on their own authority’, corrective or protective measures in order to ‘obviate’ any breach of EU law either by an EU institution, or by another Member State.<sup>87</sup> The Court also mentioned that the Member States are prevented from ‘taking initiatives’ in breach of their obligations in case the EU institutions act in violation of the principle of loyalty.<sup>88</sup> The jurisprudence also denies that the Member States would be able to justify their misconduct by identifying the disadvantages caused to them by other Member States failing to meet their obligations.<sup>89</sup> The above mentioned early jurisprudence, which seems to have been abandoned, also made it explicit that the conduct of individual Member States is ‘of common concern’ for all Member States in the Union, especially when they threaten common policies.<sup>90</sup> It was also held that unilateral Member State conduct pursuing local interests threatens the foundations of the EU legal order and undermines the balance of benefits and obligations which follows from EU membership.<sup>91</sup> In these cases, the Court even suggested that such behaviour constitutes a ‘failure in a duty of solidarity accepted by the Member States’.<sup>92</sup>

#### The prohibition of acting in bad faith

As a principle, under Article 4(3) TEU the Member States must act and cooperate in good faith. The ensuing prohibition on acting in bad faith, although its actual enforcement is restricted by-and-large

---

v. *UK* and paras. 8-9, Case 141/78, *France v. United Kingdom*, EU:C:1979:225. The consideration of such difficulties may only take place ‘subject to compliance’ with the relevant EU rules and with ‘the legitimate interests of the other Member States’, *ibid*.

<sup>83</sup> Case 6/64, *Costa*. Kumm saw this development as practical and desirable, but questioned whether it was conceptually necessary in the construction of the EU legal order, Kumm, “The moral point of constitutional pluralism: defining the domain of legitimate institutional civil disobedience and conscientious objection” in Dickson and Eleftheriadis, *op. cit. supra* note 65, pp. 216-146, at 229.

<sup>84</sup> Para. 18, Case 106/77, *Simmenthal*.

<sup>85</sup> Paras. 17-18, *ibid*.

<sup>86</sup> Para. 9, Case 128/78, *Commission v. UK*.

<sup>87</sup> *Inter alia*, para. 26, Case C-45/07, *Commission v. Greece*, EU:C:2009:81; para. 39, Case C-205/98, *Commission v. Austria*, EU:C:2000:493; paras. 34-35, Case C-14/96, *Denuit*, EU:C:1997:260.

<sup>88</sup> Para. 26, Case C-45/07, *Commission v. Greece*.

<sup>89</sup> Para. 45, Case C-115/13, *Commission v. Hungary*.

<sup>90</sup> Paras. 14-16, Joined cases 6 and 11/69, *France v. Commission*, EU:C:1969:68.

<sup>91</sup> Paras. 24-25, Case 39/72, *Commission v. Italy* and para. 12, Case 128/78, *Commission v. UK*.

<sup>92</sup> Paras. 9 and 12, Case 128/78, *Commission v. UK*, a duty which imposes the obligation on individual Member States ‘of remedying the effects of its own omissions’, and contains the prohibition of taking ‘an undue advantage to the detriment of its partners’.

to the behaviour of the Member States in infringement procedures,<sup>93</sup> provides a positive, more substantive component of Member State compliance which the predominantly formal interpretation of the requirement of adherence to legal obligations is unable to express. In its classic definition, acting in bad faith stands for the hindering and the obstruction of the Union's activities, and also for the Member States rejecting to help the Union in carrying out those activities.<sup>94</sup> Another definition holds that the principle prevents the Member States from contradicting the Union, which stands for the obligation to refrain from violating the original commitment made voluntarily by the Member States under what is now Article 1(1) TEU, and which also includes the prohibition on undermining the adequate functioning ('*bon fonctionnement*') of the Union.<sup>95</sup> Basically, the Member States are required to take responsibility for their membership.<sup>96</sup> A recent definition of the principle, which distinguishes it from the obligation of loyal cooperation, holds that the Member States are expected to act in an honest and proactive way when implementing their EU obligations,<sup>97</sup> and that they must actively overcome the difficulties of meeting their EU obligations.<sup>98</sup> It is unclear, however, whether these important qualifiers of Member State behaviour are enforceable in general in law against Member State misconduct.

### *Breaking the deal*

The earlier overview of what limitations are placed on the conduct of the Member States under EU law showed that the obligation of compliance is interpreted predominantly as a formal requirement of adherence to legal obligations, which has an inherently negative content disallowing certain Member State conduct, and which is used to address individual Member State violations separately. The positive dimensions of compliance, which explain why the Member States should meet their obligations in the collective framework of the Union and incentivizes them to do so, and which regards the Member States not as passive members of, but rather as active contributors to the Union whereby they do not scheme systematically against it, but continue to bear responsibility for their earlier commitments, are not expressed particularly strongly in law. For Hungarian economic particularism, which is characterized by the systematic treatment of certain sectors of the national economy as if they no longer formed part of the Single Market and in which law and administration are habitually (mis)used so as to secure opportunistic advantages at the local level, this may entail that the worst components of government conduct as well as its systematic nature may be left unexplored in case it is treated under the remit of the obligation of compliance. There is a danger

---

<sup>93</sup> *Inter alia*, paras. 28-31, Case 272/86, *Commission v. Greece*, EU:C:1988:433; paras. 25-28, Case 240/86, *Commission v. Greece*, EU:C:1988:173; paras. 12-17, Case C-65/91, *Commission v. Greece*, EU:C:1992:388.

<sup>94</sup> Temple-Lang, "The core constitutional law of the Community – Article 5, EC Treaty", Speech given in 1995 as Director of DG Competition, <[http://ec.europa.eu/competition/speeches/text/sp1995\\_024\\_en.html](http://ec.europa.eu/competition/speeches/text/sp1995_024_en.html)> (last visited 30 Nov. 2015), which expanded the analysis provided in Temple Lang, "Community constitutional law: Article 5 EEC Treaty", 27 CML Rev. (1990), pp. 645-681.

<sup>95</sup> Constantinesco, "L'Article 5 CEE de la bonne foi à la loyauté communautaire", in Capotorti *et al.* (Eds.), *Du droit international au droit de l'intégration: Liber Amicorum P. Pescatore* (Nomos, 1987), pp. 97-114, at 118-119.

<sup>96</sup> *Ibid.*

<sup>97</sup> Klamert, *The Principle of Loyalty in EU Law* (OUP, 2014), at 42.

<sup>98</sup> *ibid.*

that the motivations and intentions of the Hungarian government, the calculated nature of infringements,<sup>99</sup> and the apparent trend-like nature of government intervention remain uncovered.

In order to give recognition in EU law to what we regard as the defining characteristics of Hungarian economic particularism, which seem to indicate that there is something fundamentally wrong from the perspective of EU law, Hungary's conduct may need to be investigated as an example of a Member State breaking the original deal entered into upon its accession to the Union. In the Treaties, the possibility of addressing Member State deal-breaking conduct is regulated foremost in Article 7 TEU. It enables, in case of a violation of the common values of the Union laid down in Article 2 TEU, the activation against the Member States of either a preventive mechanism when there is a 'clear risk of a serious breach' of the Union's values, or a sanctioning mechanism when there is a 'serious and persistent breach' of those values. In the preventive mechanism, the Member State may receive a warning from the other Member States in the Council. The sanctioning mechanism enables the Council to suspend certain rights exercised by the Member States under the Treaties, including voting rights in the Council.

In 2014, the Commission introduced its own mechanism to deal with deal-breaking Member State conduct affecting specifically the rule of law as a core value of the Union.<sup>100</sup> Responding to the so called 'Copenhagen dilemma',<sup>101</sup> the Commission aimed to establish a framework which can offer a more comprehensive response to problems encountered in the Member States than the 'ad hoc solutions' adopted by the EU, and which is more accessible than the mechanisms under Article 7 TEU, which have 'not always been appropriate in ensuring an effective and timely response to threats to the rule of law'.<sup>102</sup> The new framework is thus positioned between infringement procedures and Article 7 TEU, and it focuses on violations of a systemic nature which cannot be addressed effectively through the national mechanisms available to enforce the rule of law.<sup>103</sup> As opposed to infringement procedures, it is not limited to addressing issues which at the same time constitute a violation of a specific provision of EU law, and it may be applied to cover 'situations of concern' which fall outside the scope of EU law.<sup>104</sup> The Council reacted to the Commission's proposal by introducing a more modest framework of an annual dialogue in the General Council.<sup>105</sup>

---

<sup>99</sup> The introduction in the Fourth Amendment to the Fundamental Law of the power to levy special taxes so as to cover the pecuniary liabilities arising from international court rulings condemning Hungary indicates that the government had foreseen that its interventions in the economy may be questionable under EU law. Under pressure from the Commission, the provision was repealed by the Fifth Amendment.

<sup>100</sup> COM(2014) 158 final, "A new EU Framework to strengthen the Rule of Law". Initiated first in 2016 against Poland, MEMO/16/62 2016.

<sup>101</sup> The Union has more effective means to enforce its common values and norms against the candidate countries than against its Member States. See 2011/2069(INI), Parliament Resolution on the state of fundamental rights in the EU (2010-2011) and 2012/2130(INI), Parliament Resolution on the situation of fundamental rights in Hungary.

<sup>102</sup> Point 3, "A new EU Framework".

<sup>103</sup> It is not an alternative to Article 7 TEU, but rather precedes and complements the mechanisms regulated therein. It is without prejudice to the Commission's powers to address specific situations in infringement procedures.

<sup>104</sup> Point 3, "A new EU Framework", which also follows from the Commission's interpretation of Article 7 TEU in COM(2003) 606 final, "Art. 7 of the Treaty on European Union: Respect for and promotion of the values on which the Union is based".

<sup>105</sup> 16862/14 COR 1, Council Conclusions on ensuring respect for the rule of law.

Addressing Hungarian economic particularism under Article 7 TEU is, however, fraught with a number of difficulties. Firstly, there are obvious political limitations on the use of the legally regulated mechanisms of Article 7 TEU<sup>106</sup> as a result of which, as suggested by the Commission, they may not be available to address developments at the national level when that would be necessary.<sup>107</sup> The Commission's communication on Article 7 TEU confirmed the political nature of Council decisions taken under this provision, and it highlighted that the procedure leading up to those decisions involves intensive informal dialogue with the Member State concerned so as to find a diplomatic solution to the situation.<sup>108</sup> In case of Hungary, even the particularly visible systemic departures from European values in the post-2010 constitution-making process<sup>109</sup> were unable to trigger the application of Article 7 TEU. The Council's annual dialogue framework is likely to prove to be equally political, and the Commission's rule of law mechanism is sufficiently muffled by the inclusion of numerous procedural stages so as to delay, and potentially avoid, making what is an essentially political decision that the rule of law has been systematically threatened by developments in a Member State.

Secondly, the thresholds for the applicability Article 7 TEU are very high.<sup>110</sup> It has been suggested that Article 7 TEU 'can only be used in the most outrageous and acute factual constellations' which, according to the commentators' view at that time, supersede the political and legal regression experienced currently in any of the Member States.<sup>111</sup> In the Commission's view, the risk of a breach or an actual breach has to 'go beyond a specific situation and concern a more systematic problem',<sup>112</sup> and the mechanisms may be activated in case of a 'simultaneous breach of several values', or of 'a systematic repetition of individual breaches'.<sup>113</sup> The Commission's own rule of law framework seems to operate with a threshold lower than that of Article 7 TEU as it may be initiated so as to 'prevent the emergence of a systemic threat to the rule of law (...) that could develop into a "clear risk of a serious breach" within the meaning of Article 7 TEU.'<sup>114</sup> The Commission has made it clear, however, that the framework is available to address systemic rather than individual breaches, which is defined as basic orders and structures at the national level being threatened as a result of the adoption of new measures or of widespread practices.<sup>115</sup> While Hungarian economic particularism, as introduced above, may indeed meet these conditions, especially that of systematic practices threatening the rule of law in Hungary,<sup>116</sup> mainly because of its limited scope it may not have reached the level of

---

<sup>106</sup> Sadurski, "Adding bite to a bark: the story of Article 7, EU enlargement, and Jörg Haider", 16 *Columbia Journal of European Law* (2010), 385-426; Williams, "The indifferent gesture: Article 7 TEU, the Fundamental Rights Agency and the UK's invasion of Iraq", 31 *EL Rev.* (2006), 3-27.

<sup>107</sup> *Supra* note 102.

<sup>108</sup> "Art. 7 of the Treaty on European Union", at 10. See also the potential game-changing citizens' initiative concerning the initiation of an Article 7 TEU procedure against Hungary, IP-15-6189.

<sup>109</sup> See 2015/2700(RSP), Parliament Resolution on the situation in Hungary.

<sup>110</sup> Point 3, "A new EU Framework", they 'underline the nature of these mechanisms as a last resort'.

<sup>111</sup> Closa, Kochenov and Weiler, "Reinforcing rule of law oversight in the EU", RSCAS Research Paper No. 2014/25, at 7.

<sup>112</sup> "Art. 7 of the Treaty on European Union", at 7-8.

<sup>113</sup> *ibid.*

<sup>114</sup> Point 4, "A new EU Framework". It aims to resolve threats to the rule of law 'before the conditions for activating the mechanisms foreseen in Article 7 TEU would be met'.

<sup>115</sup> *ibid.*

<sup>116</sup> The definition given to the rule of law by the Commission in Annex 1, "A new EU Framework" covers most of the legal and administrative malpractices followed in Hungary as discussed above.

acuteness required by both of these mechanisms. This conclusion is also supported by the issues examined next which weaken the case for the application of these mechanisms.

### *Assessment issues*

There are a number of issues arising from the Hungarian case, the assessment of which suggests that in cases, such as Hungarian economic particularism, despite the nature and the weight of the violations, the normal non-compliance framework may be more suitable than the mechanisms available to address deal-breaking conduct.<sup>117</sup> The main point is that besides the limitations examined above there are circumstances which make infringement and State aid procedures dealing with infringements on a case by case basis the preferred choice for EU decision-makers. The ensuing discussion of these issues indicates the dilemmas faced when deciding whether Member State (mis)conduct should be pursued under the mechanisms provided by Article 7 TEU or by the Commission's rule of law framework.

The first and perhaps most pressing issue is that even gross Member State misconduct can be contrasted with compliance data suggesting an overall exemplary Member State performance in the Union. With a truly vast range of EU obligations in place, it is difficult to argue that even flagrant and systematic violations affecting particular EU policies constitute a systemic threat to the values of the Union. In the case of Hungary, the compliance data show a top-performing Member State which as a norm duly reacts to the criticisms formulated under EU law.<sup>118</sup> Furthermore, the earlier analysed examples of economic particularism took place in *certain* markets, while in other segments of the national economy EU rules and the interests of EU economic operators have been keenly observed. This follows from a conscious choice made in the wake of the global financial and economic crisis in Hungarian economic policy, presumably in retained competences, to leave export-oriented producing sectors with high employment potential undisturbed from government interferences, and to intervene in pursuance of redistributive or other more unsavoury objectives in the inward-looking non-producing sectors (retail and services) of the economy.

The second issue concerns the fact that infringements can take place in areas which may fall within retained competences, affect obligations in grey, developing areas of EU law, or they may concern domains which fall in EU law under Member State discretion or autonomy. Especially in pressured times, the Member States may justifiably claim the right to experiment with policies and regulation on the fringes of their EU obligations, try inelegant, unconventional policies which may need to be adopted in haste to ensure that governments stay in control, or to push the boundaries of the policy leeway they think to enjoy under EU law. Hungarian economic particularism may in part be explained by these considerations. As already mentioned, the choice to favour exporting sectors over those of the national services and retail economy is considered to be a matter, at least by the government, which falls within the economic policy competences retained by Hungary. This provided, in particular, the basis of Hungary's decision to secure public revenues by imposing special fiscal burdens in the

---

<sup>117</sup> The Commission has accepted that infringement procedures can effectively address 'certain rule of law concerns', Point 3, "A new EU Framework".

<sup>118</sup> Single Market Scoreboard 2014-2015 for Hungary, <[http://ec.europa.eu/internal\\_market/scoreboard/\\_docs/2015/09/member-states/2015-09-hungary\\_en.pdf](http://ec.europa.eu/internal_market/scoreboard/_docs/2015/09/member-states/2015-09-hungary_en.pdf)> (last visited 15 Jan. 2016).

latter sectors.<sup>119</sup> The introduction of these progressive indirect fees and taxes affected other retained competences as well, namely the competence to increase the share of indirect taxes over direct taxes in the Hungarian tax structure. The aims pursued by this direction on local tax policy – fostering competitiveness and economic growth – coincide with those of the Union. The Hungarian government placing a tighter grip on public finances may also claim that it was developing policies in areas, such as social policy or gambling regulation, where it enjoys broad policy discretion, and where the exact boundaries of EU obligations are determined on a case-by-case basis.

There is also the issue that in most of the examples examined above Hungary was able to point to a legitimate ground in the general interest capable of justifying the violation of EU law. The legal measures adopted referred, although not necessarily in good faith, to objectives, such as increasing diversity and, thus, enhancing competition in the retail sector, the protection of the built environment, food safety, fighting criminal activities, or stabilising public finances. With this in mind, explanations of Hungarian economic particularism which suggest gross misconduct and a clear violation of the values of the Union, such as Hungary aiming to expel foreign economic operators and hand their markets over to their domestic competitors, wanting to secure public finances at whatever private and public cost, or granting through law competitive advantages to national economic operators, may only be advanced with due care. Even though the government was not particularly successful at supporting its claims with evidence and at establishing the relevance of these grounds, depending on the case at hand the violation of EU obligations was not nearly as evident as may be required under the mechanisms available to address deal-breaking Member State conduct.

Finally, pursuing even gross Member State misconduct through the usual avenues available to address non-compliance has a number of advantages. The choice of micromanaging individual Member State infringements enables an adequate assessment of the different legal positions and policy arguments. The Member State concerned can explain its conduct which may be particularly important in case of unconventional policy instruments or policies adopted in the grey areas of EU obligations. The EU non-compliance framework is devoid of the potential political drama and tensions of the politically more exposed procedures available to address deal-breaking conduct, which also means that it involves less humiliation for an already alienated Member State. It also offers multiple avenues for investigating Member State conduct, with the Commission having at its disposal multiple, well-rehearsed soft and hard instruments to negotiate with or put pressure on the Member State concerned, and there are painful financial sanctions and other repercussions available in law to address misconduct. The Hungarian example has shown that following the EU's intervention to enforce compliance obligations, the intensity of which could be adjusted to the infringement in question, the impugned measures are suspended and violations are remedied. The ultimate advantage is that infringement and State aid procedures can be trusted to recognize and address the hiatuses and malpractices in law and administration at the Member State level, which lie at the core of Member State misconduct.

## **Conclusions**

---

<sup>119</sup> These fiscal burdens were analysed above as instruments for making foreign economic operators to reconsider their business plans or leave the market.

This article, having analysed and revealed the intentions and patterns of government interventions in certain sectors of the Hungarian economy, discussed whether particularism in Hungarian economic policy after 2010 should be assessed as Hungary breaking the deal entered into upon its accession to the Union and be treated accordingly. It argued that while the principles available to deal with Member State non-compliance cover a wide range of Member State misconduct, the true nature of Hungarian economic particularism may only be adequately expressed under the framework offered by Article 7 TEU or the Commission's rule of law mechanism. It highlighted, nevertheless, that the applicability of these mechanisms is severely limited, and that there are circumstances the assessment of which may support addressing Hungarian economic particularism under the normal non-compliance framework of the Union. It seems, therefore, that qualifying Member State misconduct as deal-breaking conduct has its disadvantages, and that citizens, the other Member States and the Union may receive better outcomes when systematic intentional and opportunistic obstructions of EU obligations are pursued in law as individual infringements of concrete EU obligations.