

## Notes for the Helsinki Commission Briefing on Hungary, April 9, 2019

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**THIS VERSION: April 5, 2019**

Since its decisive electoral victory in 2010, Fidesz has embarked on a distinctly *authoritarian* political project, as articulated in Viktor Orbán's speech on July 26, 2014 in Romania. There, he singled out Singapore, China, India, Turkey, and Russia as "stars of international analysts"; touted the idea of illiberal democracy; and suggested that Hungary needed to part with Western European "dogmas," especially with the liberal notion that people "have the right to do anything that does not infringe on the freedom of the other party."<sup>1</sup>

Fidesz policies have been consistent with the message of that speech. They have pushed Hungary down the path of kleptocratic authoritarianism along the Turkish and Russian lines: packing of courts, a gradual tightening of restrictions on civil society organizations, mobilization of public opinion against imaginary external enemies, and the concentration of media ownership in few hands close to the ruling party. True, Fidesz relies on strong popular support – yet the party received only 50 percent of the popular vote in the most recent elections of 2018, which translated into a two-thirds supermajority in parliament thanks to quirks of Hungary's electoral law.

Moreover, even the openly autocratic governments of Turkey and Russia rely on substantial popular support.<sup>2</sup> Popular support does not justify crude majority rule, dismantling checks and balances, attacking civil society, distorting markets, and concentrating power in the hands of a narrow political elite. This note focuses on three aspects of Hungary's development: (1) measurable decline in institutional quality, (2) patterns of politically organized corruption, (3) instances in which Hungary's government has openly defied the US interests in Central Europe.

### **The unflattering trends**

Freedom House has famously downgraded Hungary from "free" to "partly free" last year, prompting ire from the Hungarian government. The government's spokesperson, Zoltán Kovács, accused the organization of double standards, called its methodology politically motivated, and blamed the result on George Soros' machinations.<sup>3</sup>

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<sup>1</sup> Viktor Orbán, "Prime Minister Viktor Orbán's Speech at the 25th Bálványos Summer Free University and Student Camp" (speech, Romania, July 26, 2014), <http://www.kormany.hu/en/the-prime-minister/the-prime-minister-s-speeches/prime-minister-viktor-orban-s-speech-at-the-25th-balvanyos-summer-free-university-and-student-camp>.

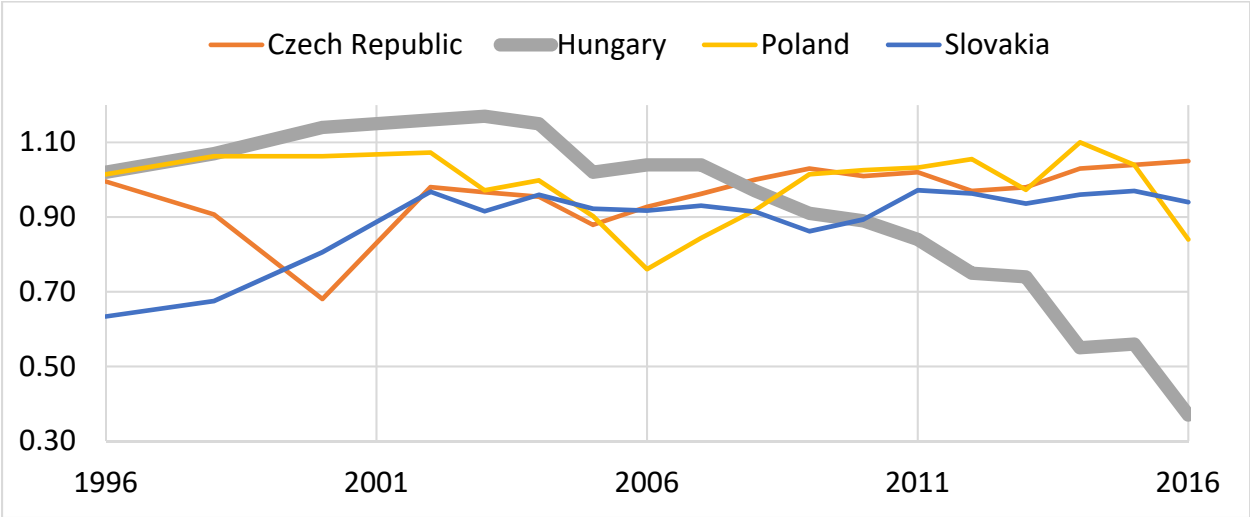
<sup>2</sup> Furthermore, just like in Turkey and Russia, the most recent parliamentary election in Hungary had a number of irregularities. See, for example, Eva S. Balogh, "Widespread Suspicion About Electoral Fraud in Hungary," *Hungarian Spectrum*, April 10, 2018, <http://hungarianspectrum.org/2018/04/10/widespread-suspicion-about-electoral-fraud-in-hungary/>.

<sup>3</sup> MTI, "Kovács Zoltán: Egy Újabb Soros-Szervezet Intézett Nyílt Támadást Magyarország Ellen," *Magyar Idők*, January 16, 2018, <https://www.magyaridok.hu/belfold/kovacs-zoltan-egy-ujabb-soros-szervezet-intezett-nyilt-tamadast-magyarorszag-ellen-2688142/>.

However, the steady erosion of governance and political freedom can be observed in a variety of other data sources, which appear immune to such criticisms. Those include not only the Worldwide Governance Indicators (WGI) published by the World Bank—an organization that takes a notably technocratic approach towards questions of institutions, rule of law, and governance—but also metrics developed by right-of-center organizations such as the Heritage Foundation and the Cato Institute.

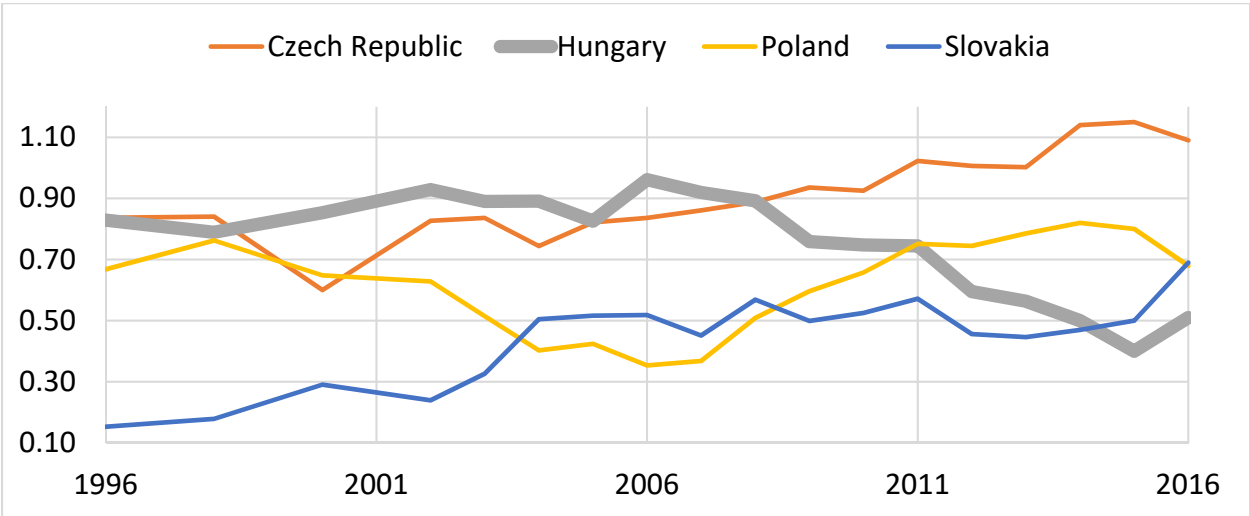
Figures 1–3 show a steady deterioration on voice and accountability, rule of law, and control of corruption, placing Hungary firmly at the bottom of the region.

**Figure 1. Voice and Accountability**



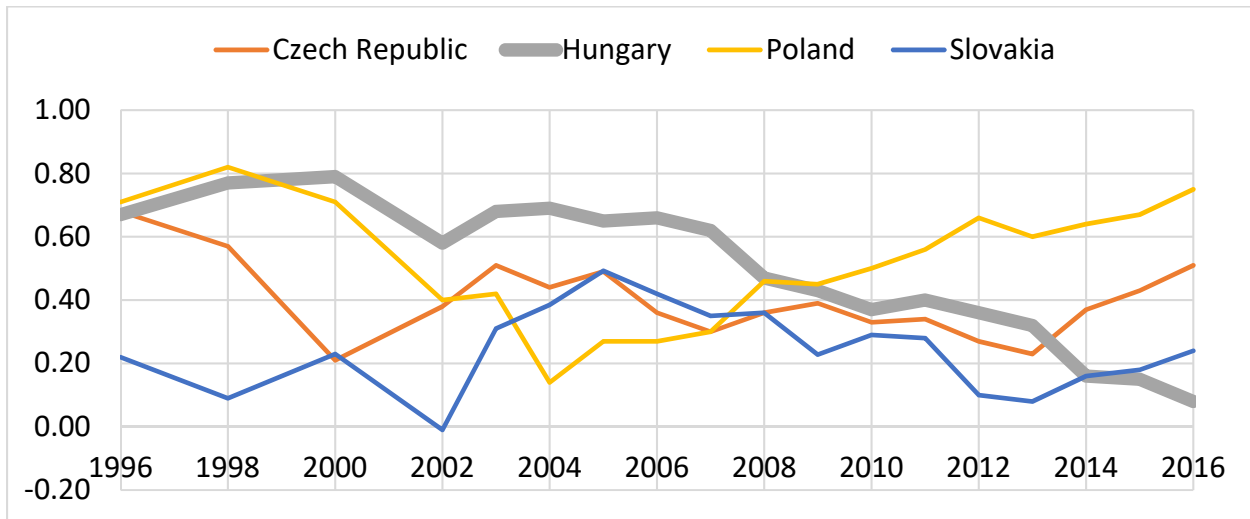
Source: World Bank.

**Figure 2. Rule of Law**



Source: World Bank.

**Figure 3. Control of Corruption**



**Source: World Bank.**

In its Index of Economic Freedom, the Heritage Foundation, hardly a bastion of pro-Soros sentiments, now places the protection of property rights in Hungary and Poland in or near “mostly unfree” territory.<sup>4</sup> The same index suggests a decline in its government integrity measure in both countries over the past year, placing Hungary well into “repressed” territory, with a dramatically worse score than it had in 2009.

Or consider the Human Freedom Index, published by the pro-free-market Cato Institute, which measures personal and economic freedoms. There, Hungary took a plunge from 28th to 44th place between 2010 and 2015.<sup>5</sup> PiS-led Poland does not share the extent of Hungary’s entrenched patronage and corruption, but evidence from the World Justice Project suggests the beginning of a similar downward slide on metrics

### **Corruption**

Economic growth across Central Europe depends heavily on the inflow of EU funds. In Hungary’s case, those account for 4.6 percent of GDP over 2006–15—the most from all member states—and for 80 percent of public investment. EU funds have been a mixed blessing throughout the region.<sup>6</sup> In Hungary, this has been doubly so because of the poor procurement rules and the concentration of decision-making authority over disbursement of funds in the prime minister’s office.

When it comes to procurement, Hungary is the only EU country that still relies heavily on unannounced “negotiated procedures.”<sup>7</sup> Those allow the government to strike a deal with any company without going

<sup>4</sup> Heritage Foundation, *2018 Index of Economic Freedom*, 2018, <https://www.heritage.org/index/visualize>.

<sup>5</sup> Cato Institute, *Human Freedom Index: Country Profiles*, 2017, <https://object.cato.org/sites/cato.org/files/human-freedom-index-files/2017-hfi-country-profiles-2.pdf>.

<sup>6</sup> See Dalibor Rohac, “How the European Union Corrupted Eastern Europe,” *National Review*, May 26, 2014, <https://www.nationalreview.com/the-agenda/how-european-union-corrupted-eastern-europe-dalibor-rohac/>.

<sup>7</sup> European Commission, “Hungary Country Profile,” in *Public Procurement—A Study on Administrative Capacity in the EU* (European Commission, 2016), [http://ec.europa.eu/regional\\_policy/sources/policy/how/improving-investment/public-procurement/study/country\\_profile/hu.pdf](http://ec.europa.eu/regional_policy/sources/policy/how/improving-investment/public-procurement/study/country_profile/hu.pdf).

through an open competition. And even on open tenders, the highest rates of procedures involve only a single bidder. Evidence of rampant corruption and political patronage is strong.

The EU's anti-fraud office, OLAF, routinely recalls funds for irregularities and fraud. In fact, irregularities were found in all 35 projects that OLAF reviewed in Hungary between 2011 and 2015.<sup>8</sup> Prominently, the government was ordered to repay €283 million for a new metro line in Budapest.<sup>9</sup> Earlier in 2018, OLAF announced it will seek to recover more than €40 million for overpriced municipal lighting projects, awarded to a company owned by Viktor Orbán's son-in-law, István Tiborcz.<sup>10</sup>

Other prominent examples of graft include Lőrinc Mészáros, the mayor of Felcsút, Orbán's home village. A former gas engineer, he is the eighth-richest man in Hungary and owns 121 companies with his wife. In 2017, his wealth tripled to \$392 million, according to *Forbes*.<sup>11</sup> Eighty-three percent of Mészáros' family companies' earnings are believed to come from EU funds.<sup>12</sup> When asked once to what he owed his success, he responded: "God, luck and Viktor Orbán."<sup>13</sup>

Such cases are not isolated incidents. Although corruption remains a problem across modern democracies, Hungary's government, with its explicit aim of building a politically loyal class of domestic businesspeople, has turned corruption into official policy. Even a new idiom has appeared in everyday Hungarian: "Fidesz-közeli cég," meaning "a near-to-Fidesz company."

Political corruption has affected US companies operating in the country as well. The New York State-based company Bunge Ltd., which produces cooking oil in Hungary, has noticed the widespread fraud surrounding VAT collection in Hungary. Reportedly, it started lobbying the Hungarian authorities to reduce the VAT rate and therefore curb such illegal practices. But Péter Heim, a businessman close to Fidesz, told Bunge that it would be possible only if Bunge made a substantial contribution to Fidesz's political foundation, Századvég.<sup>14</sup> As a result, in 2014, the US Department of State put Heim on a visa ban list, together with Ildikó Vida, head of Hungary's Central Tax Authority (NAV).

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<sup>8</sup> *Hungary Today*, "EU Anti-Fraud Office Accuses Orbán's Son-in-Law of Corruption in Lighting Contracts," February 14, 2018, <https://hungarytoday.hu/eu-anti-fraud-office-accuses-orbans-son-law-corruption-lighting-contracts-57635/>.

<sup>9</sup> Justin Spike, "Anti-Fraud Office Calls for Hungary to Return EUR 283 Million of EU Development Fund," *Budapest Beacon*, December 22, 2016, <https://budapestbeacon.com/anti-fraud-office-calls-for-hungary-to-return-eur-283-million-worth-of-eu-development-funds/>.

<sup>10</sup> *Hungary Today*, "EU Anti-Fraud Office Accuses Orbán's Son-in-Law of Corruption in Lighting Contracts."

<sup>11</sup> Benjamin Novak, "Forbes: Lőrinc Mészáros' Personal Wealth Estimated to Be HUF 105 Billion," *Budapest Beacon*, October 31, 2017, <https://budapestbeacon.com/forbes-lorinc-meszaros-personal-wealth-estimated-huf-105-billion/>.

<sup>12</sup> Katalin Erdélyi, "Companies Connected to PM Orban's Friend Won Public Tenders Worth €1.56 Billion, Most of It Funded by the EU," *Atlatszo*, January 16, 2018, <https://english.atlatszo.hu/2018/01/16/companies-connected-to-pm-orbans-friend-won-public-tenders-worth-e1-56-billion-most-of-it-funded-by-the-eu/>.

<sup>13</sup> Jennifer Ranking, "How Hungarian PM's Supporters Profit from EU-Backed Projects," *Guardian*, February 12, 2018, <https://www.theguardian.com/world/2018/feb/12/how-hungarian-pms-supporters-profit-from-eu-backed-projects>.

<sup>14</sup> *Hungarian Spectrum*, "Hungarian Prosecutors Found the Lone Culprit in the Corruption Scandal," December 19, 2018, <http://hungarianspectrum.org/2015/12/19/hungarian-prosecutors-found-the-lone-culprit-in-the-corruption-scandal/>.

## Does This Matter to the United States?

Contrary to the blasé attitude of the current administration, Hungary's embrace of crony authoritarianism threatens America's long-standing interests in Europe. Not only do US companies find themselves caught in the crossfire of local political fights,<sup>15</sup> but shoddy governance and corruption have provided new openings for revisionist powers.

In Hungary, for example, the Russian nuclear energy monopolist, Rosatom, was awarded a contract for the Paks nuclear power plant—without an open tender. The details of the contract, worth €10 billion and financed through loans from Russia, are classified.<sup>16</sup> China, too, is known to pursue a similar strategy in the region, leveraging political connections and highly visible investment projects to entrench its influence with the aim of extracting future political concessions.<sup>17</sup>

Besides the well-known visible manifestation of this trend has been Hungary's deteriorating relations with Ukraine, placing Hungary at odds with most its NATO allies and European partners. In 2014, after Russia had cut off natural gas supplies to Ukraine, Hungary followed suit, notwithstanding the EU's concerted efforts to provide Ukraine with energy.<sup>18</sup> Hungary's government opposed Ukraine's participation at the NATO summit in Brussels in July of 2018.<sup>19</sup>

Hungary's government also refused to extradite two suspected Russian arms dealers, Vladimir Lyubishin Sr. and Vladimir Lyubishin Jr., to the United States on the basis of an existing extradition treaty. The two are suspected of organizing arms shipment to Mexican drug cartels (including advanced missile systems) and trafficking of cocaine to the United States—they could face a jail time of up to 25 years in the United States. While awaiting a decision on their extradition to the United States, Russian government filed its own extradition request. The Ministry of Justice, which has the final word on this matter, decided to honor the Russian request and on August 10, 2018 the Lyubishins were dispatched to Moscow.<sup>20</sup>

Earlier this year, the government of Hungary concluded an agreement with the International Investment Bank (IIB), a relic of the Cold-War era currently based in Moscow, to move its headquarters to Budapest. Besides Russia, which owns almost one half of the bank's capital, the IIB's membership includes five

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<sup>15</sup> Prominent examples include the fine imposed on the US-owned broadcaster TVN24 for its coverage of anti-PIS protests, later canceled by the Poland media regulator. See Reuters, "Poland Annuls 1.5 Mln Zloty Fine on TVN24 over Coverage of Protests in Parliament," January 10, 2018, <https://www.reuters.com/article/poland-politics-tvn/poland-annuls-1-5-mln-zloty-fine-on-tvn24-over-coverage-of-protests-in-parliament-idUSL8N1P55WB>.

<sup>16</sup> EurActiv, "2018 Start for Expansion of Russia-Backed Hungarian Nuclear Plant," August 28, 2017, <https://www.euractiv.com/section/energy/news/2018-start-for-expansion-of-russia-backed-hungarian-nuclear-plant/>.

<sup>17</sup> Dalibor Rohac, "China's Economic Input in Eastern Europe Will Bear Political Fruit," *Financial Times*, November 1, 2017, <https://www.ft.com/content/086c1674-c788-11e6-8f29-9445cac8966f>.

<sup>18</sup> BBC News, "Hungary Suspends Gas Supplies to Ukraine," September 26, 2014, <https://www.bbc.com/news/business-29374151>.

<sup>19</sup> Myroslava Gongadze, "Ukraine to Take Part in NATO Summit Despite Hungarian Objection," *Voice of America*, July 5, 2018, <https://www.voanews.com/a/nato-summit-ukraine/4466125.html>.

<sup>20</sup> Panyi, Szabolcs, "Lord of War in Budapest: The DEA busted two Russian arms dealers and Hungary extradited them to Moscow." *Direkt36.hu*, November 23, 2018, <https://www.direkt36.hu/en/ket-orosz-fegyverkereskedot-csaltak-torbe-magyarorszagon-amerikai-ugynokok-de-az-orban-kormany-moszkvanak-adta-oket/>.

current EU and NATO nations (Czech Republic, Slovakia, Hungary, Romania, and Bulgaria), Vietnam, Mongolia, and Cuba.

The perceived benefit to European members lies in providing financing for infrastructure projects that would not get funded through usual EU channels. That financing is tiny, however: IIB has extended €9 billion in cumulative financing over its entire existence.<sup>21</sup> Such financing comes with risks since the IIB is by no means a traditional multilateral development bank but rather an instrument of Russian power projection – a Trojan horse aimed at driving Eastern Europe away from the West.

Given the IIB's status as an international organization, Hungary will have to allow all "advisors and experts acting in the Bank's interest" to enter the country – and therefore the Schengen Area. But those can include Russian nationals currently included on sanction lists. It is not difficult to imagine how this might strain diplomatic and economic relations between Budapest, Brussels, and Washington. The IIB could extend loans to projects that involve entities sanctioned by either the United States or the EU – not to speak about the possibility that it serves simply as a cover for Russian intelligence operations in Europe.<sup>22</sup>

## Conclusion

The decline of rule of law, and the rise of corruption and patronage in Hungary, alongside its murky geopolitical allegiances, is a challenge to America's interests in the region. The United States stood by Central European nations as they liberated themselves from the shackles of Soviet rule and communist ideology and joined the ranks of self-governing nations with full-fledged market economies. The United States cannot become a cheerleader for policies that are aiming to undo the progress achieved since 1989—and neither it can afford to stay silent.

As a first step, Congress should recognize the challenge and make it clear, in the form of a bipartisan resolution, that the creeping authoritarian practices—particularly the purges within the judiciary and attacks on civil society and media—do not have friends or supporters in Washington. US companies operating in Central Europe need to know they have the US government's backing when they encounter local corruption. The administration and Congress should not shy away from imposing sanctions against local officials who have been demonstrably involved in corrupt dealings, especially if it involved American companies.

It is also time to see beyond the knee-jerk attacks on George Soros. One does not need to agree with his politics to see that the efforts to "sweep out" organizations funded by him have been deeply damaging to the region—not least by the impact they have had on the New York–incorporated CEU and by feeding anti-Semitism.<sup>23</sup> The CEU's de facto departure from Hungary is a blow to America's cultural pull, intellectual presence, and soft power in the region.

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<sup>21</sup> International Investment Bank, *Basic Facts*, [https://iib.int/files/iib\\_basic\\_facts\\_1.pdf](https://iib.int/files/iib_basic_facts_1.pdf).

<sup>22</sup> See Clay R. Fuller and Dalibor Rohac, "It is time for America's Eastern European allies to withdraw from Putin's fake multilateral bank." AEI Ideas, March 9, 2019, <https://www.aei.org/publication/it-is-time-for-americas-eastern-european-allies-to-withdraw-from-putins-fake-multilateral-bank/>.

<sup>23</sup> Dalibor Rohac, "Stop Obsessing over George Soros and the Koch Brothers," *CapX*, December 6, 2017, <https://capx.co/stop-obsessing-over-george-soros-and-the-koch-brothers/>.

Most importantly, at the time of NATO's 70<sup>th</sup> anniversary, it is time to consider seriously reforming the organization from a one-way ratchet to a two-way street. Countries such as Hungary or Turkey, which are deviating from the alliance's shared values, have to face a credible mechanism of escalating sanctions within the alliance, culminating with their expulsion. But that is not only a question of institutional design but also of political leadership from Washington. I hope that today's conversation can help catalyze it.