

IRREGULARITIES OF EU COHESION FUNDS: THE HUNGARIAN PERSPECTIVE

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ABSTRACT: *In practice, during the actual use of EU cohesion funds – not only in Hungary, but also in all EU member states – unlawful acts, omissions and acts contrary to the funding contract are usually taken. There are several forms and reasons of breaching a funding rule, which can be committed not only by a beneficiary, but also by the financial supporter.*

Such breaches and omissions are called irregularity, its examination and legal consequences are specified partly in EU law, partly in national law. In Hungarian law the irregularity procedure is such a special procedure that is governed by civil law and administrative law jointly, the border line is hard to define. Although the practical experiences show that irregularities are not always attributable to the beneficiaries, the problem has deeper roots. The institutional system and its operation, the legal rules – which all are established by the state – (may) play a great role in the commitment of irregularities. Serious legal questions are raised regarding the irregularity procedures however, the academic life deals less with it than it would be necessary. However, the easy understanding of the present complex regulation would be particularly relevant in practice, during the actual use of subsidies and when beneficiaries are exercising their rights. These made necessary the practical summary of the Hungarian experiences from the last 15 years with the purpose of drafting a guideline for preventing future irregularities. This is the topic of the present study.

KEYWORDS: EU cohesion funds; irregularity procedure; funding contract; funding legal relationship, financial supporter and beneficiary

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1. INTRODUCTORY THOUGHTS

Since the end of 80's the cohesion subsidies arising from the Structural Funds of the European Communities/Union has an overall regulation on EU level by defining the main priorities and expectations, while the detailed rules were determined by the

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Member States within the framework of community rules. It was the member states' responsibility to establish the necessary institutional system and tendering procedure. This solution necessarily resulted in the development of different systems and regulations in each Member State. This duality in regulation and the operation of various systems has remained until today¹.

This study puts emphasis on the presentation of the Hungarian regulation and practice.²

Such unique solutions are observed in the Hungarian regulation that raise up serious legal theoretical questions. On the other hand, it was verified that such factors play a role in commitment of irregularities that also appear in several other EU Member States. This has a special influence on the occurrence of irregularities from the perspective of legislation and institutional system as well.

2. LEGISLATION FACTORS

In our view, *the law regulation the cohesion policy is extremely complex, diversified and hardly transparent*, which results in uncertainty and various interpretation options. This problem effects not only the beneficiaries but also the financial supporter, and not only in Hungary but also on EU level. Orientation within the legal rules makes the proper use of funds and compliance with rules difficult for the beneficiaries. On the financial supporter's side, it hinders the development of unified practice and expectations, since often even the employees of the financial supporter do not have a clear view on the system.

As written in the first footnote, the European Union sets up the general regulation of funds in the form of *regulations*. Regulations are directly applicable and binding on all

¹ Regulation (EU) No 1303/2013 of the European Parliament and of the Council on the ESIF-Funds and repealing Council Regulation (EC) No 1083/2006
 Regulation (EU) No 1301/2013 of the European Parliament and of the Council (ERDF regulation)
 Regulation (EU) No 1304/2013 of the European Parliament and of the Council (ESF regulation)
 Regulation (EU) No 1300/2013 of the European Parliament and of the Council (CF regulation)
 Regulation (EU) No 1305/2013 of the European Parliament and of the Council (EAFRD regulation)
 Commission Delegated Regulation (EU) No 480/2014 on supplementing the Regulation (EU) No 1303/2013 of on the ESIF-Funds

² Main law on the topic:
 Council Regulation (EC) No 1083/2006 laying down general provisions on the European Regional Development Fund, the European Social Fund and the Cohesion Fund and repealing Regulation (EC) No 1260/1999;
 Regulation (EU) No 1303/2013 laying down common provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund, the European Agricultural Fund for Rural Development and the European Maritime and Fisheries Fund and laying down general provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund and the European Maritime and Fisheries Fund and repealing Council Regulation (EC) No 1083/2006;
 4/2011. (I. 28.) Governmental Decree on the organization of funds arising from European Regional Development Fund, the European Social Fund and the Cohesion Fund in the 2007-2013 programming period;
 272/2014. (XI.5.) Governmental Decree on the organization of funds arising from certain European Union funds in the 2014-2020 programming period;
 Act XVII of 2007 on certain procedural issues concerning the agricultural, agricultural and rural development, fisheries funds and other actions

Member States and their natural persons, legal entities. However, – at least in case of cohesion funds – their content mostly phrases expectations against the Member States, on the national rules. Consequently, the Member States are responsible for adopting national law within the EU framework rules. At the comparison of Hungarian and EU regulation a peculiarity (more properly: contradiction) catch our eyes: *while the EU regulation has a clearly public law appearance, in the Hungarian regulation the private law growingly dominates.*

Accordingly, the detailed rules on use of EU funds are regulated by national law which provide wide public law powers to the financial supporter. There is no doubt that the subsidies are regulated by public law. However, more and more times private law rules are applicable for the funding contracts signed on the granted money and in the funding relationship, at least in Hungary.

In the financial period 2007-2013 *private law* was applicable only to subsidies arising from the Cohesion Fund, European Regional Development Fund and the European Social Fund, agricultural funds were subjected to *administrative law*. Out of the latter one, European agricultural fund for rural development *became also subjected to private law* in financial period 2014-2020. This has a great significance from more aspects. On one hand, the financial supporter is put into coordinate position while still owning extra public law powers. On the other hand, civil courts become entitled to dispute resolution instead of administrative courts, therefore beneficiaries have different opportunities to exercise their rights than before.

Concerning irregularities and irregularity procedures this means the followings. In administrative law regulation the irregularity decision passed by the financial supporter is deemed as an administrative decision and may be supervised at (administrative) court procedure. In private law regulation the irregularity decision is considered as a civil law declaration to which no legal remedies are attached. In a civil law based legal relationship only the other legal actions made by the financial supporter matter (e.g. cancel the funding contract, prohibits the transfer of money, etc.), and the beneficiary can contest ‘only’ these legal actions, not exactly the irregularity decision.

It is particular, that in Hungary there is no entity that would supervise the procedure of the financial supporter as a secondary level body usual in administrative procedures. Furthermore, the judicial practice showed that civil law courts have no competency to supervise the irregularity decisions. However, the administrative law regulation still remains beyond the coordinate relationship between the financial supporter and beneficiary, since during the management of funds the financial supporter still exercises the ‘public power’ ensured by law. *At all cases, when examining any legal questions, the primary task is to determine whether the legal relationship between the financial supporter and beneficiary is governed by civil law or administrative law?* However, this is not an easy task due to the unclear wording of Hungarian legal regulations. Lack of practical handbooks and academic literature hinders the understanding; the only thing legal interpreters can do is to try to study this specially regulated area. Moreover, it is hard to view the legal problems with civil law eyes in a public law based environment, and vice versa. *Judicial practice also seems to become unified only nowadays in this topic*, contradictory judgments and legal interpretations having been passed for many years.

The other specialty in Hungarian legislation is – that can be phrased this time as an unambiguous problem – *passing new legal regulation packages for each 7-year financial period with delay*. On EU level by changing the financial periods not only new budget is accepted, but the area of cohesion policy is re-regulated as well, new ‘legal regulation packages’ are passed for each new 7-year period. This is followed by the national legislation. Usually the EU legislative process is delayed, its closure falls in time after the strict beginning of the financial period. *The reason of delay is arising from the two-step process*: firstly, the EU rules are set out, only after their acceptance may the drafting and finalizing of national law be commenced. Delay in time is recognized already at the first step, however in a strict view EU law is always announced at the beginning of the new period. *Unfortunately, the Member States does not have enough time for their implementation, for working out the detailed national set of rules*. Delay in time can be more easily recognized at the second step: usually nation law is unclear, not detailed and not finalized enough at the beginning of the financial periods, therefore *interpretation problems appear* together with the implementation handled by later changes in law. Of course, this causes great difficulty in the ongoing operative programs and projects, especially if the former practice was not in line with the later guidelines. Accordingly, it is (would be) essential to handle the various institutional, procedural and executive issues by clear and express regulation already at the beginning of the programs. Already at the beginning of the projects, beneficiaries should be aware of all obligations to be fulfilled, they should not be informed on change of rules afterwards, in the middle of a process! According to comparative international literature this problem (expectation) is recognized not only in Hungary, but also in other Member States that joined the EU after 2004.³

3. INSTITUTIONAL FACTORS

EU’s cohesion policy is operating within a *decentralized execution system*. This means that not the provider of funds, the European Committee manages the use of funds (however there are funds directly given by this body to the beneficiaries), rather national bodies established especially with this aim or already existing bodies appointed for this purpose. Union legislation *always provide enough flexibility to the Member States for the establishment of the institutional system*. Union regulations prescribe only that Member

³ See in this topic especially:

- NYIKOS Györgyi – Robert TALAGA: Cohesion policy in transition, comparative aspects of the Polish and Hungarian systems of implementation. Comperative Law Review 18/2014.
- NYIKOS Györgyi: A közbeszerzés és a kohéziós politika viszonya és egymásra hatása a gyakorlatban. In: A közbeszerzés gyakorlata. Szakértők útmutatói ajánlatkérőknek és ajánlattevőknek (Raabe Tanácsadó és Kiadó Kft. 2006)
- NYIKOS Györgyi – SZABÓ Szandra: Szabálytalanságok az EU kohéziós politikában – magyar tapasztalatok és tanulságok. Európai Tükör 2019/1.
- KENGYEL Ákos: A megszokott keretek csapdájában, gondolatok az Európai Unió 2014–2020 közötti költségvetési kiadásairól. KÖZ-GAZDASÁG 2013/1
- NAGY Zoltán: A közzépénzügyi támogatási jogviszony a közjogi és magánjogi szabályozás metszetében. In: Publicationes Universitatis Miskolcinensis, Sectio Juridica et Politica, Miskolc, Tomus XXX/2. (2012)

States shall establish, appoint the managing and monitoring bodies concerning the funds. The regulations determine the compulsory tasks and types of these bodies (e.g. managing authority, certifying authority, audit authority), but it is up to the Member States' decision which type of and how many institutions are established or appointed for performing these tasks.

Parallel to the continuous change of legal regulations *Hungarian institutions handling the funds also went under a continuous change*, concerning their type and quantity. This necessary 'goes hand in hand' with the *frequent change of employees managing the execution process*. Due such deficiency in stability the expertise, experience and partnerships gained during the work of a staff member is being lost. Evaluations shows that preparedness of staff is one of the key factors in a successful development strategy, which is/was criticized often in Hungary. Unfortunately, staff members working in the system do not have an overall view on the operation of the entire system, therefore it is unable to operate properly. In fact, the lack of common knowledge base can be observed. No one is dealing actively with knowledge capital, furthermore there is no actor that would take care of the development of knowledge capital in the institutional system.

Beyond the lack of resources (capital, budgetary support) *another source of unpreparedness of beneficiaries* is that those functions of the institutional system that should directly support the beneficiaries do not work efficiently. According to practical experiences the scale of funds is increasing year by year, involving new beneficiaries to the system and financing growing projects. However, significant projects are a challenge also to such beneficiaries who earlier already performed Union projects successfully.

A *more stable organizational structure*, that is not changing much from financial period to financial period, would serve a more effective operation of the Hungarian system. Paying more attention to the stability of human resource and to maintain their competency became also necessary. The area of cohesion policy is extremely complex, its understanding and overview needs thorough knowledge. Moreover, the interpretation of frequently changing law, the new legal regulation packages at each financial period needs lot of time even for those having such knowledge. Consequently, the stability and qualification of human resource plays an emphasized role in the tendering procedures and the monitoring process of the performed projects. A smoothly operating, transparent executive and monitoring system with unified practice seems to be necessary in development policy and irregularity procedures in Hungary.⁴

⁴ See in this topic especially:

- Annual informative papers of the Hungarian Court of Auditors concerning the use of EU funds
- HUTKAI Zsuzsanna: Az uniós források felhasználásának gyakorlata, szabályozási háttér. Pro Publico Bono – Magyar Közgazgatás 2013/3.
- GYÖRİNÉ SZABÓ Gabriella: A 2014–2020-as köhéziós források felhasználásának hazai vállalásai az uniós kötelezettségek szorításában. KÖZ-GAZDASÁG 2015/4.
- SZABÓ Szandra: Uniós támogatásokkal kapcsolatos szabálytalanságok kialakulásában közrejátszó háttérfaktorok. Bibó Jog- és Politikatudományi Szemle Folyóirat 2020. évi II. szám

4. CONCLUSION

A Member State has two main tasks in connection to use of EU funds: passing the national legal rules that are harmonizing with EU law and setting up an institutional system that will handle the distribution, the use of money. Since 2004, when Hungary joined the EU, various problems are experienced and several unique solutions are observed in the legislation. Although the rules of EU fund usage are much detailed, according to the experiences show that this does not secure the proper and lawful use of money. In Hungary, the changes affecting the law and institutional system is quite frequent, even during a financial period. Amending the system to harmonize with the requirements set out in EU regulations may be acceptable, but transparency and easy overview should be provided to the actors acting on the side of beneficiaries (beneficiaries, consultants, companies preparing the tender applications, etc.) and to those actors exactly applying the law. In the long run, it would be definitely advantageous if:

- persons and entities on the side of beneficiaries should not get to know a new organizational system in each financial period,
- change of financial period would not result in problems and uncertainty, furthermore
 - from the side of state entities an experienced staff would support the performance of projects.

All of the aforementioned circumstances enhance the improper use of funds and increase the risk of irregularities. In fact, we can declare that a beneficiary of the EU fund commits the irregular use of subsidies, but from a wider perspective often the defaults of the system lead it until then.

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- NYIKOS Györgyi: *A közbeszerzés és a kohéziós politika viszonya és egymásra hatása a gyakorlatban*. In: A közbeszerzés gyakorlata. Szakértők útmutatói ajánlatkérőknek és ajánlattevőknek (Raabe Tanácsadó és Kiadó Kft. 2006)
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