



Working Paper

Rule of Law Conditionality

Niels Kirst



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*Niels Kirst**

Abstract: Over the last decade, the European Union's (EU) rule of law instruments have grown exponentially. This development was commensurable to the rule of law challenges that the EU faced within the Member States – Hungary and Poland being the main perpetrators. However, more instruments have not led to better results. Instead, the EU has turned to budget conditionality as the ultima ratio in the rule of law crisis. Financial conditionality has become the EU's instrument of choice to safeguard the rule of law in the Member States. This chapter analyses the so-called Rule of Law Conditionality Regulation – Regulation (EU) 2020/2092 -- and situates it within the Post-Pandemic EU framework of Economic Governance.

Keywords: Budget Conditionality, Conditionality Regulation, EU Constitutional Law, Hungary, NGEU, RRF, Rule of Law Backsliding

* This paper is forthcoming in Federico Fabbrini & Christy Petit (eds), *Research Handbook on Post-Pandemic EU Economic Governance and NGEU Law* (Elgar 2024).

1. Introduction

Over the last decade, the European Union's (EU) rule of law instruments have grown exponentially.¹ This development was commensurable to the rule of law challenges that the EU faced from several Member States – Hungary and Poland being the main perpetrators.² However, more instruments have not led to better results. As Christina Fasone points out, “[t]he growing set of rule of law instruments is not necessarily promoting better results, as the detachment between the theory and the practice of the rule of law seems to prove.”³ As a result, financial conditionality has become the EU’s instrument of choice to safeguard the rule of law in the Member States. This chapter analyses the main conditionality instrument that the EU adopted at the end of 2020 – the Regulation (EU) 2020/2092 on a general regime of conditionality for the protection of the Union budget (the Conditionality Regulation).⁴ The chapter argues that due to the failure of legal mechanisms and lack of political will, the EU has shifted rule of law protection to the budgetary realm. With the Conditionality Regulation, the EU walks a fine line by protecting fundamental values via budgetary means. In the short term, this strategy seems to work. In the long term, however, it must be proven to be sustainable.

This chapter is structured as follows. Section 2 sheds light on the history of the rule of law Conditionality Regulation. It explains how the regulation came about and summarises the approval process and its challenges. Section 3 analyses the Conditionality Regulation's core features. Section 4 examines the interrelation between the Conditionality Regulation and the NGEU Recovery Fund. Section 5 analyses the only application of the regulation so far against the Member State of Hungary and its political implications. Finally, the Conclusion summarises and evaluates the Conditionality Regulation.

¹ Laurent Pech, ‘The Rule of Law in the EU: The Evolution of the Treaty Framework and Rule of Law Toolbox’ No. 7 Reconnect Working Paper, and Carlos Closa and Dimitry Kochenov (eds), *Reinforcing Rule of Law Oversight in the European Union* (Cambridge University Press (CUP) 2016).

² Armin von Bogdandy and Michael Ioannidis, ‘Systemic Deficiency in the Rule of Law: What it is, What has been done, What can be done’ 51 *Common Market Law Review* 59, and Laurent Pech and Kim Lane Scheppele, ‘Illiberalism Within: Rule of Law Backsliding in the EU’ (Cambridge, United Kingdom) [Cambridge University Press (CUP)] Vol. 19 *Cambridge Yearbook of European Legal Studies* pp. 3 .

³ Christina Fasone, Adriano Dirri and Ylenia Guerra, *Established EU Rule of Law Instruments: State-of-the-Art Working Paper* (RED SPINEL - Milestone 5, 2023) p. 5.

⁴ *Regulation (2020/2092) on a general regime of conditionality for the protection of the Union budget (Conditionality Regulation)* (16 December 2020) (Official Journal of the European Union (OJ) 2020).

2. History of the Rule of Law Conditionality Regulation

The idea to link the rule of law and the EU budget originated in 2017 at the European Commission's DG JUST.⁵ The idea emerged after recognising the inefficacy of existing measures like the Article 7 TEU procedure in halting rule of law backsliding in the Member States.⁶ The idea was further developed and supported by academic contributions emphasising the need for EU budget conditionality.⁷ In its vision for the new seven-year budget 2021-7, the Commission acknowledged the need for a rule of law Conditionality Regulation that would link the funds of the EU to rule of law standards.⁸ This was clearly outlined in the Commission's Communication of 2 May 2018.⁹ On the same day, the Commission put forward the first legislative proposal for a regulation addressing systemic deficiencies in the rule of law via the budget.¹⁰

Following the ordinary legislative procedure, the European Parliament (EP) swiftly adopted a formal position on this proposal in April 2019.¹¹ However, in 2019, progress stalled as the Council of the EU (Council) was hesitant towards it and did not adopt a negotiating position. Momentum shifted in 2020 by adopting the new Multiannual Financial Framework (MFF) and the Next Generation EU Fund (NGEU) in response to the Covid-19 pandemic. In the historic European Council Summit of July 2020, the Member States agreed that a conditionality regime should be introduced together with the MFF and the NGEU.¹² This finally gave the political backing by the European Heads of State for a conditionality regime linked to the EU budget.¹³

⁵ Markus Becker, 'EU Commissioner Pushes for Hard Line on Poland (7 March 2017)' *Spiegel International* (Hamburg, Germany) <<https://www.spiegel.de/international/europe/eu-commissioner-pushes-for-hard-line-on-poland-a-1137672.html>> , and Eszter Zalan, 'Justice commissioner links EU funds to 'rule of law' (31 October 2017)' *EU Observer* (Brussels, Belgium) <<https://euobserver.com/eu-political/139720>> .

⁶ Pech and Scheppele.

⁷ Gábor Halmai, 'The Possibility and Desirability of Rule of Law Conditionality' Vol. 11 *Hague Journal on the Rule of Law* pp. 171, and Alexander Mattelaer, *Exploring the Boundaries of Conditionality in the EU* (European Policy Brief, 2018).

⁸ *Communication from the Commission to the European Parliament, the European Council, the Council: A Modern Budget for a Union that Protects, Empowers and Defends, The Multiannual Financial Framework 2021-2027 (2 May 2018)* (European Commission Press Service 2018).

⁹ *Ibid.*

¹⁰ *Proposal for a Regulation of the European Parliament and of the Council (2018/0136) on the protection of the Union's budget in case of generalised deficiencies as regards the rule of law in the Member States (2 May 2018)* (European Commission Press Service 2018).

¹¹ *European Parliament Legislative Resolution on the proposal for a regulation of the European Parliament and of the Council on the protection of the Union's budget in case of generalised deficiencies as regards the rule of law in the Member States (4 April 2019)* (European Parliament 2019).

¹² Special meeting of the European Council (17, 18, 19, 20 and 21 July 2020) – Conclusions (European Council Press Service 2020).

¹³ John Morijn, *The July 2020 Special European Council, the EU budget(s) and the rule of law: Reading the European Council Conclusions in their legal and policy context (23 July 2020)* (eulawlive.com 2020).

At the July Council Summit, the European Council faced a situation where swift and bold actions were needed to kick-start the EU's economic recovery amid the Covid-19 pandemic and the related economic downturn. After intensive negotiations, the Heads of State agreed on the following: a new seven-year budget – the MFF; a recovery fund – the NGEU; an increase of the EU's own resources (from 1.6% to 2.0%) – the Own Resources Decision; and a Conditionality Regulation to uphold the rule of law. Following the seminal July European Council Summit, the German Council Presidency took the legislative dossier and proposed a compromise in September 2020.¹⁴ An agreement was subsequently reached, and the proposal was returned to the EP for further negotiations. Intensive trialogue meetings between the Council, EP, and the Commission eventually led to a conclusive legislative draft published on 5 November 2020.¹⁵

After the provisional agreement on the Conditionality Regulation gained the support of most EP members and Council Member States, Hungary and Poland, both under Article 7 TEU proceedings, threatened to veto the MFF and the Own Resources Decision, which requires unanimity in the Council, potentially derailing the NGEU.¹⁶ While the Conditionality Regulation could pass with a qualified majority, the MFF required unanimous consent, and the Own Resources Decision had additionally to be ratified by each national parliament. Thus, the EU decision-making rules in fiscal affairs gave the Hungarian and Polish governments significant leverage in their negotiating position. Only a new European Council Summit on 11 December 2020 could solve this impasse.¹⁷

During the December European Council Summit, the Heads of State agreed on comprehensive conclusions regarding adopting, applying, and interpreting the Conditionality Regulation.¹⁸ In this unusual declaration, the European Council agreed that the Commission shall develop guidelines on the applicability of the regulation and shall abstain from bringing any case under the regulation until such guidelines are finalised. This happened although the European Council did not have the formal competence to issue such legal commands towards the Commission.¹⁹ The EP strongly condemned this practice and the European Council's conclusions in a parliamentary resolution on 17 December

¹⁴ Maia de la Baume and Lili Bayer, 'Germany seeks breakthrough on linking EU payouts to rule of law (28 September 2020)' *Politico Europe* (Brussels, Belgium) <<https://www.politico.eu/article/germany-seeks-breakthrough-on-linking-eu-payouts-to-rule-of-law/>> .

¹⁵ *Draft provisional agreement between European Parliament and Council on the rule of law (5 November 2020)* (European Parliament Press Service 2020).

¹⁶ *Joint Declaration of the Prime Minister of Poland and the Prime Minister of Hungary (26 November 2020)* (Government of the Republic of Poland Press Service 2020).

¹⁷ *European Council meeting (10 and 11 December 2020) – Conclusions* (European Council Press Service 2020).

¹⁸ See Recital 2 point a) till point k) in *ibid.*

¹⁹ Alberto Alemanno and Merijn Chamon, *To Save the Rule of Law You Must Apparently Break It (11 December 2020)* (Verfassungsblog.de 2020).

2020, stating that “[...] the European Council shall not exercise legislative functions;”²⁰ and that “[...] any political declaration of the European Council cannot be deemed to represent an interpretation of legislation as interpretation is vested with the European Court of Justice.”²¹ Therefore, the conclusions exposed an interinstitutional conflict between the EP and the European Council, with the subject of controversy being whether the latter overstepped its competencies and assigned role in the Treaties.

However, the European Council's conclusions enabled the EU to proceed with the Conditionality Regulation, the MFF, and the NGEU. "Originally crafted by the German Presidency in close contact with Budapest and Warsaw, this text has enabled the EU25 to overcome the veto posed by Hungary and Poland on the adoption of the entire package, thus reaching a 'mutually satisfactory solution'."²² Yet, many scholars criticised this last-minute compromise for bringing the deal over the line as it violated the EU's constitutional principles.²³ “The interpretative declaration of 10 December 2020 is set to go down in history as a dark page for the rule of law in the Union legal order.”²⁴ The controversial statements, thus, lifted the blockage of the MFF and the Own Resources Decision by Hungary and Poland and enabled the EU to move on with the legislative package. “The final rubber-stamping and implementation of the RoL mechanism was engulfed in fierce institutional debates owing to the Polish and Hungarian veto threat, which was offset with a controversial compromise.”²⁵ Finally, on 14 December 2020, the Council adopted the rule of law conditionality regulation.²⁶ On 16 December 2020, the regulation was adopted by the EP²⁷ and entered into force with its publication in the Official Journal. Therefore, the regulation applied from 1 January 2021 onwards.

Quickly after its adoption and entering into force, Hungary and Poland unsuccessfully challenged the Conditionality Regulation before the Court of Justice.²⁸ The Court of Justice upheld the

²⁰ *European Parliament Resolution on the Multiannual Financial Framework 2021-2027, the Interinstitutional Agreement, the EU Recovery Instrument and the Rule of Law Regulation (17 December 2020)* (European Parliament 2020).

²¹ *Ibid.*

²² Alemanno and Chamon.

²³ *Ibid.*

²⁴ *Ibid.*

²⁵ Fasone, Dirri and Guerra p. 73.

²⁶ *Adoption of the Council's position at first reading and of the statement of the Council's reasons = Outcome of the written procedure completed on 14 December 2020* (Council of the European Union Press Service 2020).

²⁷ Agnese Krivade, Parliament approves the “rule of law conditionality” for access to EU funds (16 December 2020) (European Parliament Press Service 2020).

²⁸ Vlagyislav Makszimov, ‘Hungary, Poland refer controversial rule of law mechanism to court (11 March 2021)’ *EurActiv* (Brussels, Belgium) <<https://www.euractiv.com/section/justice-home-affairs/news/hungary-poland-refer-controversial-rule-of-law-mechanism-to-court/>> .

Conditionality Regulation on 16 December 2021.²⁹ In its judgment, “[t]he CJEU made clear that Article 7 TEU procedures are not the sole options to protect EU values and the adoption of other mechanisms – with reference to appropriate legal bases within the Treaties – is possible as long as they do not have the same subject matter, do not pursue the same objective and do not allow the adoption of identical measures to the ones under Article 7 TEU.”³⁰ After the judgment, the Commission published guidelines on applying the regulation on 2 March 2022.³¹ Only after this, and one and a half years after it entered into force, would the Conditionality Regulation be applied for the first time against the Member State of Hungary.³²

3. The Conditionality Regulation’s Core Features

Regulation 2020/2092 covers breaches of the principles of the rule of law if they are linked to the EU’s budget (Article 4). This is a consequence of the legal basis chosen, namely Article 322(1)(a) TFEU, which concerns the EU budget. The regulation’s scope explicitly covers breaches of the principles of the rule of law that *affect or seriously risk affecting* the EU’s budget in a *sufficiently direct way* (Article 4(1)). A mere violation of the principles of the rule of law in a Member State does not suffice to trigger the mechanism. The link to the EU’s budget or the EU’s financial interest is indispensable.

Article 2(a) specifies that the principles of the rule of law should be understood as referring to the EU values enshrined in Article 2 TEU. It also defines that fundamental rights are only considered under this regulation if judicial protection or equal treatment is affected. The following Article 3 entails an indicative list of examples of what would be considered a breach of the principles of the rule of law. Article 4(2), which lays out the detailed conduct which constitutes a breach of the principles of the rule of law, is the core provision of the regulation. There is, thus, a duplication in Article 3 and Article 4(2). However, Article 3 must be understood as an indicative provision, whereas Article 4(2) is the definitive and operative provision. Moreover, Article 4(2) directly links

²⁹ *Hungary and Poland v Parliament and Council (C-156/21 and C-157/21)* European Court Reports Court of Justice of the European Union, and Niels Kirst and Beatrice Monciunskaitė, ‘Establishing a Link between Solidarity and Responsibility – The Court’s Judgment on the Conditionality Regulation’ Vol. 24 Irish Journal of European Law.

³⁰ László Detre, András Jakab and Tamás Lukácsi, ‘Comparing Three Financial Conditionality Regimes and their Application to Hungary: The Conditionality Regulation, the Recovery and Resilience Facility Regulation, and the Common Provisions Regulation’ No. 2023-23 MPIL Research Paper Series, p. 4.

³¹ *Communication from the Commission: Guidelines on the application of the Regulation 2020/2092 on a general regime of conditionality of the protection of the Union budget (2 March 2022)* (European Commission Press Office 2022).

³² ‘EU triggers rule of law procedure against Hungary (27.04.2022)’ *Deutsche Welle* (Bonn, Germany) <<https://www.dw.com/en/eu-triggers-rule-of-law-procedure-against-hungary/a-61607618>> .

the regulation's two main elements (the principles of the rule of law and the EU's budget) by pointing out potential fields of application. The list of Article 4(2) provides thus a *non-exhaustive* list of examples for applying the regulation.

The regulation's procedure is laid out in Article 6 and comprises several steps. Some procedural steps can be compared to the infringement procedure under Article 258 TFEU, while others are taken from the macroeconomic conditionality rules introduced by establishing the European Monetary Union (EMU).³³ If the Commission believes there is a breach of the principles of the rule of law in a Member State that affects the EU's budget, it will send a reasoned letter to that Member State (Article 6(1)). The concerned Member State can then address the Commission's findings with a reply and/or by proposing remedial measures (Article 6(5)). Finally, the Commission shall consider the Member State's observations before deciding if it wants to submit an implementing act to the Council to freeze Member State funds or terminate the case. There is, however, one caveat to the whole procedure, which can be found in Recital 26. Suppose a Member State believes that the Commission's proposal of an implementing act violates the principle of objectivity, non-discrimination, or equal treatment. In that case, discussing the matter at the next European Council meeting may be exceptionally requested. In these cases, the 'deadline' to decide for the Council is extended to three months.

Article 5 of the regulation provides for the measures that the Commission can propose to enact against a Member State that breaches the principles of the rule of law. The provision builds substantially on the Financial Regulation,³⁴ which governs the disbursement of funds from the EU's budget, and the Common Provisions Regulation administers the EU's structural funds' distribution.³⁵ The article is split into two streams. One stream outlines the measure that can be adopted for (i) funds implemented directly by the EU itself and a second stream, (ii) for funds implemented under shared management.³⁶

There is also the possibility of lifting measures after breaches of the principles of the rule of law have been remedied by the concerned Member State. The procedure for lifting measures can be found in Article 7. With remedial measures, the accused Member State may refute the findings of

³³ Armin von Bogdandy and Justyna Łacny, *Suspension of EU funds for breaching the rule of law – a dose of tough love needed?* (European Policy Analysis, 2020).

³⁴ *Financial Regulation (Regulation 2018/1046)* (Official Journal of the European Union 2018).

³⁵ *Common Provisions Regulation* (Official Journal of the European Union 2013).

³⁶ , *Financial Regulation (Regulation 2018/1046)*, Article 62 thereof.

the Commission and prove that the conditions of Article 4 are no longer fulfilled. The Council is further instructed to review all existing measures annually and consider whether the measures can be lifted. Finally, Article 7(3) foresees the possibility of a Member State recouping funds from the budget that were withheld due to implementing acts. However, the funds will be lost for the Member State after two years when the deficiencies have not been remedied.

4. The Conditionality Regulation and the NGEU Recovery Fund

Besides the Conditionality Regulation, 2021 also marked the advent of the Recovery and Resilience Facility (RRF)³⁷ under which Member States receive funds from the NGEU.³⁸ The NGEU Recovery Fund, conceived in 2020, "[...] constitutes a turning point in the process of European integration, which goes well beyond what happened in response to the euro-crisis."³⁹ It enables the EU to borrow large sums from the financial markets to finance reforms and investments via loans and grants in the Member States. Moreover, it allows the Commission, through predefined milestones (qualitative) and targets (quantitative), to steer national policies and ensure the achievement of EU-wide priorities (a functioning rule of law included). This section will analyse the relationship between the Conditionality Regulation and the NGEU.

Under the RRF, Member States were required to submit a National Recovery and Resilience Plan (NRRP) in 2021, which the Council would approve following careful assessment and recommendation by the Commission.⁴⁰ "Each national plan has been drawn up by governments and validated by the Commission and the Council, and payments of EU grants and/or loans, which run until 2026, depend on the achievement of milestones and targets detailed in the plan."⁴¹ The NRRPs added a further layer of conditionality as the Commission decided to link the disbursement of funds to specific milestones and targets that need to be achieved.⁴² "The operation of the facility introduces de facto conditionality, which is not specific to the rule of law, and which is used to the full in this respect by the European institutions."⁴³ Interestingly, the Commission intertwined

³⁷ *Regulation (2021/241) of the European Parliament and the Council establishing the Recovery and Resilience Facility (12 February 2021) "RRF Regulation"* (Official Journal of the European Union (OJ) 2021).

³⁸ See also S. Baroncelli, "Recovery & Resilience Facility" in Chapter 8 of this edited book.

³⁹ Federico Fabbrini, 'Next Generation EU: Legal Structure and Constitutional Consequences' (Cambridge, United Kingdom) [Cambridge University Press (CUP)] *Cambridge Yearbook of European Legal Studies*, p. 2.

⁴⁰ See also M. Patrin, "Decision-making: Commission & Council" in Chapter 14 of this edited book.

⁴¹ Eric Maurice, 'Rule of law: the uncertain gamble on conditionality (14 March 2023)' Vol. 660 *Fondation Robert Schuman, European Issues*.

⁴² See also N. Moran, "Milestones, Targets & Relation to the Cohesion Policy" in Chapter 12 of this edited book.

⁴³ Maurice.

conditionality-based procedures – the Conditionality Regulation and the milestones – when it started its conditionality strategy towards Hungary in 2022. "The combined use of conditionality instruments linked to the EU budget and the milestones to be achieved in the Recovery Plans thus multiplies the EU's ability to force Member States to change their rule of law practices."⁴⁴ It heightens the pressure on rule of law backsliding Member States.

The NGEU incorporates a rule of law compliance mechanism linked to the rule of law Conditionality Regulation. Article 8 of the RRF Regulation establishes the crucial link between the RRF Regulation and the rule of law Conditionality Regulation by requiring compliance of the implementation of funds with the Conditionality Regulation. It reads as follows.

“The Facility shall be implemented by the Commission in direct management in accordance with the relevant rules adopted pursuant to Article 322 TFEU, in particular the Financial Regulation and the Regulation (EU, Euratom) 2020/2092 of the European Parliament and of the Council.”

Accordingly, “[...] compliance with the Rule of Law Regulation becomes a general condition for each MS to obtain from the European Commission the payment of the agreed instalments.”⁴⁵ Therefore, it is Article 8 of the RRF Regulation in which the worlds of rule of law protection and economic governance meet.⁴⁶ However, Article 8 only refers to the implementation of loans and grants of the RRF and not to the approval of NRRPs by the Commission. Therefore, compliance with the Conditionality Regulation is “[...] not devised as a proper legal prerequisite for the approval of the Plans by the EU institutions.”⁴⁷ It is, thus, an ex-post compliance with the rule of law Conditionality and not an ex-ante compliance. This has consequences for the method of implementing RRF payments. Consequently, “[...] compliance with the Rule of Law needs to be verified by the Commission, which is called upon to condition the actual payments of the RRF funds to a positive assessment on the milestones of the NRRP that are deemed essential under a rule of law perspective.”⁴⁸ If the Member States fulfil the milestones and targets, this implies that compliance with the rule of law requirements has also been satisfied at the same time.

⁴⁴ Ibid.

⁴⁵ Fasone, Dirri and Guerra p. 76.

⁴⁶ Cf. Paul Dermine, *The New Economic Governance of the Eurozone: A Rule of Law Analysis* (Cambridge University Press (CUP) 2022).

⁴⁷ Fasone, Dirri and Guerra p. 77.

⁴⁸ Ibid.

5. The Activation of the Conditionality Regulation to Hungary

Moving from theory to practice, the following section will analyse the Conditionality Regulation's first application towards Hungary. On 27 April 2022, three weeks after the Hungarian parliamentary elections, which Viktor Orban's Fidesz party won by a wide margin, the Commission formally triggered the rule of law Conditionality Regulation for the first time against Hungary.⁴⁹ At that time, there were regular debates about the rule of law in Hungary in the EP ongoing for years,⁵⁰ eight rule of law-related infringement proceedings by the Commission against Hungary,⁵¹ and a pending Article 7 TEU proceeding against Hungary in the Council.⁵² However, none of these instruments has yielded significant results and changed Hungary's fast rule of law decline towards an electoral autocracy and a hybrid regime.⁵³ The timing seems to be intentionally chosen as a moment shortly after the Hungarian parliamentary elections, which signalled that no shift in domestic policy was to be expected over the following years and that the trend of rule of law backsliding would continue with Orban's Fidesz government holding onto power.

The Commission justified the activation of the Conditionality Regulation with “systemic irregularities, deficiencies and weaknesses in public procurement procedures; the high rate of single bidding procedures and the low intensity of competition in procurement procedures; issues related to the use of framework agreements; the detection, prevention and correction of conflicts of interest;

⁴⁹ Marton Dunai, 'Viktor Orban wins new term as Hungary's prime minister, but OSCE criticises campaign (4 April 2022)' *Financial Times* (London, United Kingdom) <<https://www.ft.com/content/482f9cb3-4bdd-4bf7-b776-b8c99b60aaca>> and Vlad Makszimov, 'Hungary: Commission officially launches procedure linking bloc funds to rule of law (27 April 2022)' *EurActiv* (Brussels, Belgium) <<https://www.euractiv.com/section/politics/news/hungary-commission-officially-launches-procedure-linking-bloc-funds-to-rule-of-law/>> . The following section builds on a publication by the author of this dissertation in Niels Kirst, 'The Conditionality Regulation in Action: The Case of Hungary' EU Law Live .

⁵⁰ *European Parliament Resolution on the existence of a clear risk of a serious breach by Hungary of the values on which the Union is founded (15 September 2022)* (Official Journal of the European Union (OJ) 2022).

⁵¹ *Commission v Hungary (C-286/12) (Retirement Age of Hungarian Judges)* European Court Reports Court of Justice of the European Union, *Commission v Hungary (C-288/12) (Independence of the Data Protection Supervisor)* European Court Reports Court of Justice of the European Union, *Commission v Poland, Hungary and the Czech Republic (C-715/17, C-718/17 and C-719/17, Asylum Relocation Decision)* European Court Reports Court of Justice of the European Union, *European Commission v Hungary (C-66/18, Hungarian Higher Education Law)* European Court Reports Court of Justice of the European Union, *European Commission v Hungary (C-78/18, NGO Law)* European Court Reports Court of Justice of the European Union, *European Commission v Hungary (C-808/18, Hungarian Asylum Law)* European Court Reports Court of Justice of the European Union, *Commission v Hungary (C-821/19) (Stop Soros Law)* European Court Reports Court of Justice of the European Union, and *Commission v Hungary (C-769/22) (Hungarian LGBTQ Law)* European Court Reports Court of Justice of the European Union.

⁵² *European Parliament Resolution on a proposal calling on the Council to determine, pursuant to Article 7 (1) of the Treaty on European Union, the existence of a clear risk of a serious breach by Hungary of the values on which the Union is founded (12 September 2018)* (Official Journal of the European Union (OJ) 2018).

⁵³ Jorge Liboreiro and Sandor Zsiros, 'Hungary is no longer a full democracy but an 'electoral autocracy,' MEPs declare in new report (16 September 2022)' *Euronews* (Brussels, Belgium) <<https://www.euronews.com/my-europe/2022/09/15/hungary-is-no-longer-a-full-democracy-but-an-electoral-autocracy-meps-declare-in-new-repor>> .

and issues related to public interest trusts.”⁵⁴ After the Hungarian government was confronted with the accusation of the Commission, Brussels and Budapest entered a dialogue on how to remedy the deficiencies. This included many back-and-forth written exchanges between the Hungarian government and the Commission. As a result, the Hungarian government agreed that it would address the identified rule of law deficiencies with 17 remedial measures to avert the Commission from formally forwarding a proposal for an implementing decision to the Council, which would have the final vote on budget cuts.⁵⁵ Among them were the following: the establishment of a new Integrity Authority, the establishment of an Anti-Corruption Task Force, strengthening the anti-corruption framework, reducing the share of single-bidder procurement procedures, action plan to increase competition in procurement procedures, strengthening cooperation with OLAF, ensuring improved transparency in public spending, and ensuring transparency in the use of Union support by public interest asset management foundations.⁵⁶ It was in the Commission's hands whether it would find the remedial measures and the implementation plan adequate to remedy the concerns.

On 18 September 2022, the Commission found that the measures were insufficient overall, and the College of Commissioners decided to take the next step and drafted a formal proposal for a Council Implementing Decision released the same day.⁵⁷ It proposed to suspend 65% of operational programmes under the cohesion policy foreseen for Hungary, which equalled €7.5 billion of cohesion funds, in case Hungary would not fulfil key implementation steps by 19 November.⁵⁸ Between 18 September 2022 and 19 November 2022, however, the Hungarian government did not adopt sufficient legal changes to satisfy the Commission's demands. Following those developments and amid insufficient reforms by Hungary, the Commission proposed suspending €7.5 billion of cohesion funds under the Conditionality Regulation to the Council on 30 November 2022.⁵⁹ Additionally, the Commission proposed a general ban on the disbursement of funds to the newly established Hungarian foundations of public interest and institutions maintained by them (mainly

⁵⁴ *Council Implementing Decision (2022/2506) on measures for the protection of the Union budget against breaches of the principles of the rule of law in Hungary (15 December 2022)* (Official Journal of the European Union (OJ) 2022) Recital 2.

⁵⁵ *Ibid.*

⁵⁶ Petri Sarvamaa and others, *The 7.5 billion Euro question: Did the Hungarian government implement the necessary reforms to avoid rule of law sanctions? (17 November 2022)* (2022).

⁵⁷ *Proposal for a Council Implementing Decision (2022/0295) on measures for the protection of the Union budget against breaches of the principles of the rule of law in Hungary (18 September 2022)* (European Commission Press Office 2022).

⁵⁸ *Ibid.*

⁵⁹ *Communication from the Commission to the Council: on the remedial measures notified by Hungary under Regulation (2020/2092) for the protection of the Union budget (30 November 2022)* (European Commission 2022).

concerning the areas of education and research universities), and it subjected the disbursement of funds in the future to the fulfilment of 17 remedial measures.

On the same day, however, the Commission also proposed adopting Hungary's NRRP, paving the way for Hungary to receive money from the NGEU. The Commission, therefore, on the one hand, proposed budget cuts to cohesion funds via the Conditionality Regulation, but on the other, opened the door for significant disbursement of funds under the NGEU. However, the proposal for a Council Implementing Decision of the Hungarian NRRP was subject to 27 super-milestones that Hungary was due to fulfil before the first money would flow. The Commission, therefore, tied those two decisions together by proposing budget cuts under the Conditionality Regulation and, second, approving Hungary's NRRP, but with a decisive conditionality criterion built into the disbursement of funds.

Taking a step back and looking at the details of the NGEU, RFF, and NRRP allows a better understanding of how the Commission envisions this two-sided conditionality mechanism. In 2022, the Commission had to assess Hungary's NRRP. This second prong of the Commission's rule of law enforcement against Hungary is built upon the requirement that all NRRPs lay out a plan to achieve the country-specific recommendations of the European Semester. "[...], as underlined in Article 17 [of the RRF Regulation], 'the recovery and resilience plans shall be consistent with the relevant country-specific challenges and priorities identified in the context of the European Semester', and this is a condition for eligibility of the NRRP."⁶⁰ The proposed NRRP by the Hungarian government was formally assessed but technically found insufficient by the Commission on 30 November 2022.⁶¹ The Commission, therefore, communicated a proposal for a Council Implementing Decision on the Hungarian NRRP to the Council subject to 27 super milestones.⁶² On the same day, 30 November 2022, the Commission also officially proposed suspending 65% of operational programmes of the cohesion policy against Hungary under the Conditionality Regulation, which equalled €7.5 billion of cohesion policy money foreseen for Hungary.⁶³ The Commission, therefore, drew the consequences of the inadequate reforms that the Hungarian government had to achieve until 19 November 2022. "On the same day on which the Commission

⁶⁰ Fabbrini.

⁶¹ *Commission finds that Hungary has not progressed enough in its reforms and must meet essential milestones for its Recovery and Resilience funds (30 November 2022)* (European Commission Press Office 2022).

⁶² *Proposal for a Council Implementing Decision (2022/0414) on the approval of the assessment of the recovery and resilience plan for Hungary (30 November 2022)* (2022).

⁶³ *Communication from the Commission to the Council on the remedial measures notified by Hungary under Regulation 2020/2092 for the protection of the Union budget* (European Commission Press Office 2022).

proposed the suspension of the funds under the conditionality mechanism, it also proposed the approval of the Hungarian national recovery and resilience plan (NRRP).⁶⁴ Therefore, the Commission used a two-pronged tactic to target Hungary for its rule of law deficiencies.

Returning to the Conditionality Regulation and the 17 remedial measures, it was now in the Council's hands how it would respond to Hungary's reforms and the Commission's assessment and proposal. First, on 6 December 2022, the Council demanded an updated assessment of the already fulfilled Hungarian remedial measure by 7 December 2022, which the Commission published on 9 December 2022.⁶⁵ On 12 December 2022, only three days after the Commission's final assessment of the Hungarian progress made, the Council voted on the implementing decision put forward by the Commission and decided by a qualified majority to suspend €6.3 billion of cohesion funds from Hungary.⁶⁶ Therefore, the Council mainly followed the Commission's proposal and only slightly amended the amount of the frozen funds. From 65%, it went down to 55% of funding suspension of the budgetary commitments in cohesion funds for Hungary to accommodate the Hungarian government. Therefore, it lowered the funding suspension to 55%, equalling €6.3 billion of cohesion funds for Hungary. The Council made this last-minute change by triggering Article 6(11) of the Conditionality Regulation, allowing it to amend the proposed implementation decision.⁶⁷ This gives the Council a *carte blanche* in deciding the appropriate measure. Substantially, the Council was unsatisfied with Hungary's progress in addressing the rule of law deficiencies found by the Commission. As the Council Implementing Decision stated, “[...], in light of the assessment carried out above, it should be concluded that the remedial measures notified by Hungary, taken as a whole, as adopted and in view of their details, and the ensuing uncertainty about their application in practice, do not put an end to the identified breaches of the principles of the rule of law.”⁶⁸

⁶⁴ Thu Nguyen, *The Hungary Files: Untangling the political and economic knots (8 December 2022)* (Policy Brief, 2022).

⁶⁵ , *Council Implementing Decision (2022/2506) on measures for the protection of the Union budget against breaches of the principles of the rule of law in Hungary (15 December 2022)*.

⁶⁶ *Rule of law conditionality mechanism: Council decides to suspend €6.3 billion given only partial remedial action by Hungary (12 December 2022)* (Council of the EU Press Office 2022).

⁶⁷ Article 6 (11) of Regulation 2020/2092 states, "The Council, acting by a qualified majority, may amend the Commission's proposal and adopt the amended text through an implementing decision." See Niels Kirst, 'Rule of Law Conditionality: The Long-Awaited Step Towards A Solution of the Rule of Law Crisis in the European Union' Vol. 6 *European Papers Insight* pp. 101.

⁶⁸ , *Council Implementing Decision (2022/2506) on measures for the protection of the Union budget against breaches of the principles of the rule of law in Hungary (15 December 2022)* Recital 58.

Nevertheless, on the same day, 12 December 2022, the Council also approved the Hungarian NRRP.⁶⁹ This was necessary as the RRF funding for Hungary would have been entirely lost if the NRRP had not been approved by the end of 2022. "While it decided to suspend cohesion funds under the budgetary conditionality mechanism, the Council adopted Hungary's €5.8 billion NRRP, including twenty-seven "super milestones" on justice, transparency in public procurement, and the fight against fraud, corruption and conflicts of interest."⁷⁰ Therefore, the Council followed the Commission's lead in the two-sided conditionality strategy towards Hungary. On the one hand, it suspended funds under the Conditionality Regulation. However, on the other hand, it formally approved the NRRP tied to strict milestones under the RRF Regulation. On the NRRP, "[t]he Council specified that these milestones must be "fully and correctly" implemented before Hungary can submit its first payment claim."⁷¹

Moreover, it turned out that a political power game between Hungary and the other Member States overshadowed the decisions made by the Council on 12 December 2022. Previously, Hungary had vetoed the Macro-financial Assistance Instrument (MFA+) for Ukraine and the agreed global corporate tax rate in the Council.⁷² Hungary, thus, blackmailed the EU and the other Member States into approving the Hungarian NRRP and lowering the proposed amount withheld under the Conditionality Regulation. Hungary was successful with this strategy.⁷³ In a rapid turn of events, Hungary lifted the veto, and the Hungarian NRRP was approved. In exchange for the approval of the NRRP and the lowering of the funds withheld under the Conditionality Regulation, Hungary lifted its veto on the € 18 bn aid for Ukraine package and a global corporate tax rate.⁷⁴

One year later, in December 2023, Budget Commissioner Johannes Hahn took stock of whether Hungary made any improvements regarding the 17 remedial measures in a Commission Decision.⁷⁵

⁶⁹ *NextGenerationEU: Member states approve national plan of Hungary (12 December 2022)* (Council of the EU Press Office 2022).

⁷⁰ Maurice.

⁷¹ *Ibid.*

⁷² Sam Fleming and Marton Dunai, 'Hungary blocks €18bn worth of EU aid for Ukraine (6 December 2022)' *Financial Times* (London, United Kingdom) <<https://www.ft.com/content/5ac5e2ec-c4b9-404c-b8e5-8b72f96c4568>> .

⁷³ Federico Fabbrini, 'Funding the War in Ukraine: The European Peace Facility, the Macro-Financial Assistance Instrument, and the Slow Rise of an EU Fiscal Capacity' Vol. 11 *Politics and Governance* pp. 52.

⁷⁴ Alice Tidey, 'Hungary agrees deal and lifts veto on €18bn EU aid package for Ukraine (13 December 2022)' *Euronews* (Brussels, Belgium) <<https://www.euronews.com/my-europe/2022/12/13/hungary-lifts-vetoes-on-ukraine-aid-and-corporate-tax-to-lower-frozen-eu-funds>> .

⁷⁵ *Commission Decision on the reassessment, on the Commission's initiative, of the fulfilment of the conditions under Article 4 of Regulation (EU, Euratom) 2020/2092 following Council Implementing Decision (EU) 2022/2506 of 15 December 2022 regarding Hungary (13 December 2023)* (European Commission 2023).

Hungary had not submitted any written notification in the meantime.⁷⁶ Apparently, Hungary did not expect a positive outcome of the reassessment. In a clearly outlined letter to the Chair of the Committee on Budgetary Control of the EP, Commissioner Hahn stated that “the Commission finds that the conditions under Article 4 of the Conditionality Regulation remain fulfilled and the Union’s budget remains at the same level of risk as assessed under the Council Implementing Decision.”⁷⁷ Therefore, Hungary's changes in the past 12 months were inadequate to address the 17 remedial measures fully. The € 6.3 bn, therefore, remains blocked under the Conditionality Regulation. This indicates that Hungary has not significantly progressed on the rule of law in the past 12 months.

It is even more astonishing that, on the same day, the Commission released € 10.2 bn that was previously frozen under the horizontal enabling conditions of the Common Provisions Regulation.⁷⁸ The horizontal enabling conditions allowed the Commission to freeze Cohesion funds to Hungary on top of the Conditionality Regulation and the NGEU.⁷⁹ Commentators saw this Commission decision as a charm offensive to persuade Hungary to give up its veto on accession talks and macro-financial assistance to Ukraine before the European Council Summit in December 2023.⁸⁰ The release of € 10.2 bn to Hungary under the Common Provision Regulation seems opaque when, at the same time, Hungary did not qualify for a release of funds under the Conditionality Regulation, given that the aims under both instruments partly overlap.⁸¹

Overall, this shows that the criteria under the Common Provision Regulation to freeze and unfreeze funds are less objective and somewhat political. They are used as a political bargaining chip by the Commission. It seems like Hungary has once again managed to blackmail the EU by threatening a veto on a crucial policy file in the European Council.⁸² This is an alarming development for democracy, transparency, and the EU's rule of law and puts the Conditionality Regulation's success

⁷⁶ Letter of Commissioner Johannes Hahn to MEP Monika Hohlmeier and MEP Johan Van Overtveldt (13 December 2023) (European Commission 2023).

⁷⁷ Ibid.

⁷⁸ Commission considers that Hungary's judicial reform addressed deficiencies in judicial independence but maintains measures on budget conditionality (13 December 2023) (European Commission 2023).

⁷⁹ The third type of conditionality that Hungary is subjected to are the horizontal enabling conditions under the Common Provision Regulation. Due to space constraints, this instrument cannot be extensively discussed in this chapter. For an overview of the horizontal enabling conditions under the Common Provision Regulation, see Kim Lane Scheppele and John Morijn, *Frozen: How the EU is Blocking Funds to Hungary and Poland Using a Multitude of Conditionalities* (4 April 2023) (VerfBlog 2023).

⁸⁰ Nicolas Camut, ‘Commission unblocks €10.2B for Hungary as EU tries to sway Viktor Orbán on Ukraine (13 December 2023)’ *Politico Europe* (Brussels, Belgium) <<https://www.politico.eu/article/commission-unblocks-e10-2-billion-for-hungary-as-eu-tries-to-sway-viktor-orban-on-ukraine/>> .

⁸¹ András Schwarcz, *Rule of law-related ‘super milestones’ in the recovery and resilience plans of Hungary and Poland* (PE 741.581) (Briefing, 2023).

⁸² Tommaso Pavone, *The EU’s Faustian Bargain* (17 December 2023) (VerfBlog 2023).

into question. Therefore, the Commission's decision to release Cohesion funds to Hungary under the Common Provisions Regulation is unreasonable, undermines the Commission's integrity, and goes against its role as Guardian of the Treaties, according to Art. 17 TEU.

6. Conclusion

The last three years of the rule of law saga in the EU can aptly be characterised as the rise of spending conditionality in the EU.⁸³ While the rule of law enforcement has moved from political to financial instruments, this has by no means reduced the polarisation around the rule of law. As Christina Fasone pointed out, “[t]he rise of spending conditionality and the greater attention for the protection of the EU financial interests have indirectly led to a further politicisation and polarisation of the debate on the rule of law.” This chapter tried to show the legal and political background of the rise of spending conditionality in the EU and set it into the context of the EU’s Post-Pandemic Economic Governance.

The Conditionality Regulation is no panacea for rule of law problems in the Member States as it comes with strings attached. “The conditionality mechanism is only legal because it requires a direct link between rule of law violations and the EU budget to be demonstrated, and the milestones imposed in the recovery plans must have an economic and social justification, as the Recovery and Resilience Facility is legally based on the EU's economic and social competences.”⁸⁴ Therefore, since a sufficiently direct link to the EU budget is indispensable, the Commission is hampered in applying the Conditionality Regulation to all cases of rule of law backsliding in the Member States.

However, making the RRF contingent on the Conditionality Regulation multiplies the EU's power to safeguard the rule of law within the Member States.⁸⁵ Both operate through complementary mechanisms. While the RRF focuses on economic recovery with an implicit expectation of adherence to rule of law principles, the Conditionality Regulation provides a direct and explicit tool to enforce these principles. Both regulations use financial leverage to enforce the rule of law. The

⁸³ See also N. Moran's "Milestones, targets & relation to cohesion policy" in Chapter 12 of this edited book. For an in-depth analysis of the rise of spending conditionality and its constitutional ramifications, see Viorica Vita, 'Revisiting the Dominant Discourse on Conditionality in the EU: The Case of EU Spending Conditionality' Vol. 19 Cambridge Yearbook of European Legal Studies pp. 116, and Päivi Leino-Sandberg and Matthias Ruffert, 'Next Generation EU and its Constitutional Ramifications: A Critical Assessment' Vol. 59 Common Market Law Review pp. 433.

⁸⁴ Maurice.

⁸⁵ Some scholars have criticised this development as these conditionality mechanisms imply the trading of rule of law and democracy for EU funds and recovery. See Louise Fromont and Arnaud Van Waeyenberge, 'Trading rule of law for recovery? The new EU strategy in the post-Covid era' Vol. 27 European Law Journal pp. 133.

RRF does so through the conditional release of funds based on adherence to agreed recovery plans, which implicitly includes respecting EU values (ex-ante). The Conditionality Regulation does so directly by tying EU funding to rule of law compliance (ex-post). Together, these regulations create a broader legal and policy framework within the EU that links financial support to Member States with compliance to fundamental EU values, including the rule of law.