

# HUNGARY

UNITARY COUNTRY

## BASIC SOCIO-ECONOMIC INDICATORS

INCOME GROUP: UPPER MIDDLE INCOME

LOCAL CURRENCY: HUNGARIAN FORINT (HUF)

### POPULATION AND GEOGRAPHY

**Area:** 93 030 km<sup>2</sup>**Population:** 9.788 million inhabitants (2017), a decrease of -0.3% per year (2010-2015)**Density:** 105 inhabitants / km<sup>2</sup>**Urban population:** 71.1 % of national population**Urban population growth:** 0.1% (2017 vs 2016)**Capital city:** Budapest (18.0% of national population)

### ECONOMIC DATA

**GDP:** 274.9 billion (current PPP international dollars), i.e. 28 108 dollars per inhabitant (2017)**Real GDP growth:** 4.0% (2017 vs 2016)**Unemployment rate:** 4.2% (2017)**Foreign direct investment, net inflows (FDI):** -13 484 (BoP, current USD millions, 2017)**Gross Fixed Capital Formation (GFCF):** 21.5% of GDP (2017)**HDI:** 0.838 (very high), rank 45 (2017)

## MAIN FEATURES OF THE MULTI-LEVEL GOVERNANCE FRAMEWORK

Hungary is a parliamentary representative democratic republic. The country has a unicameral parliament composed of the National Assembly, whose members are elected every four years by direct universal suffrage. The Head of State, the President of the Republic, is elected indirectly by the Parliament for a five-year term, and the Head of Government, the Prime Minister, is appointed by the President for a four-year term.

The 1989 constitution, which amended the 1949 constitution, recognised the principle of local self-government, dedicating one full chapter to subnational governments. A strong decentralisation process started with the 1990 Act of Local Government, which defined the communes' right to self-government, and restored the autonomy of municipalities and counties. Local governments were given broad responsibilities and autonomy in terms of financial management.

A new Fundamental law was adopted in April 2011 and enforced in on 1 January 2012, which pronounced the 1959 constitution to be null and void. While it has been amended several times since 2012, the new Hungarian constitution marked the start of a recentralisation process. Provisions concerning local governments are provided in Art. 31 to 35 of the Fundamental Law. It determines the essence of subnational governments, the county and local government, established "to administer public affairs and exercise public power at a local level" (Art. 31). No explicit mention is made of the principle of local self-government, although Art. 32 states that in the management of local public affairs and within the framework of the Acts, local governments shall adopt decrees, make decisions and autonomously administer their affairs. Art. 32 also indicates that local governments determine the rules of their organisation and operation, exercise the rights of ownership with respect to local government property, determine their budgets and autonomously manage their affairs on that basis, deciding on the types and rates of local taxes.

Following the new constitution, a Cardinal Law on Local Governments was enacted in 2011 (Act CLXXXIX of 2011) to define a new multi-level governance framework. The law recentralised several local responsibilities and resources and strengthened central government's oversight over legal compliance and administrative functioning of SNGs. This was reinforced by the launch of an important State Territorial Administration Reform (STAR) in 2010, which reorganised the jurisdictional, organisational and human resource foundation of public service delivery at all levels of the public sector in Hungary. In particular, the STAR reform introduced a new deconcentrated administrative structure in the form of 175 townships (*járás*), including three districts in the capital, in charge of state-administrative tasks. Townships took over many functions exercised previously by municipalities, and are currently also in charge of the legal and financial supervision of SNGs.

## TERRITORIAL ORGANISATION

2018	MUNICIPAL LEVEL	INTERMEDIATE LEVEL	REGIONAL OR STATE LEVEL	TOTAL NUMBER OF SNGS
	3 177 municipalities ( <i>települési önkormányzatok</i> )		19 counties ( <i>megyék</i> ) + Budapest	
	Average municipal size: 3 081 inhabitants			
	<b>3 177</b>		<b>20</b>	<b>3 197</b>

**OVERALL DESCRIPTION.** Hungary is a unitary country with a two-tier subnational governments system, made up of 19 counties, in addition to Budapest, and 3 177 municipal authorities in 2018, with no hierarchical link. Both counties and municipalities are governed by councils composed of representatives (*councillors*) directly elected through secret ballot for four-year mandates. County councils are led by a council President, elected from amongst its members. On the other hand, municipal councils are headed by mayors (*polgarmester*), who are municipalities' executive body, elected by direct universal suffrage for a four-year term.

**REGIONAL LEVEL.** The regional level is organised in 19 counties, which were restored in 1990, and Budapest which has a special status similar to that of a county. Counties are very heterogeneous both in terms of population and of area. While the average size of counties is around 490 000 inhabitants, the least populated county had around 193 000 inhabitants in 2017 (Nógrád) and the two most populated were Budapest (1.75 million inhabitants) and Pest (1.25 million inhabitants). Hungary has the second highest regional disparities in GDP per capita among 30 OECD countries with comparable data, with the Northern Great Plain lagging behind, and Central Hungary leading the way. Regional economic disparities have increased moderately since 2000. Budapest has a special status since 1991 set out in the Local Government Act, and thereby has a two-tier organisation similar to that of a county, with the capital city and 23 city districts (*kerület*). Both levels function in the same way as municipalities, with a mayor and local councils elected by direct universal suffrage. Each district has a council and each city district has a mayor. The capital city has a Lord Mayor and a capital city assembly of elected representatives.

**MUNICIPAL LEVEL.** The municipal level in Hungary is highly fragmented, comprising villages (*kozsegek*), towns (*varosok*) and 23 cities with county status (*megyei jogu varos*), conferred to towns that were county seats in 1990 and cities with more than 50 000 inhabitants if they request this status to the Parliament. Cities with county status are in charge of the responsibilities of the county in their area. They can form city districts with full legal statute and establish city district offices.

Hungarian municipalities have an average size of 3 088 inhabitants (vs 5 900 in the EU28 and 9 700 in the OECD in 2018) and a median size of 815 inhabitants. As of 2016, 91% of municipalities had fewer than 5 000 inhabitants, and even 76% less than 2 000 inhabitants. 30% of the population was living in cities with more than 500 000 inhabitants (compared to 55% on average in OECD countries).

Cardinal Act on local government of December 2011 set 2 000 inhabitants as the critical threshold for local administration. It does not force mergers but stipulates that small municipalities under 2 000 inhabitants must group their administrative services into joint offices or districts or micro-regions. The purpose of the reform was to ensure sufficient administrative and human capacity in small settlements without merging municipalities or restricting municipal autonomy. As of 2017, there were 738 joint offices operating across Hungary, with 83% of municipalities involved in one of them. In addition to these joint offices, Hungary had 1 517 local government associations in 2017, comprising more than 10 765 members. Inter-municipal cooperation has been encouraged since the 1997 Act on the Associations and Co-operation of Local Government.

The State deconcentrated administration at territorial level was reformed in 2010 as part of the STAR reform. The former administrative entities became integrated in the so-called county government offices (or in case of Budapest: district government office). The 20 largest government offices, which form the largest units of territorial administration, operate in county seats, and in Budapest. They coordinate and promote the territorial implementation of government tasks in accordance with legislation and government decisions. District (metropolitan district) offices are the smallest units of territorial administration in 174 cities and 23 districts in Budapest. Their basic task is to manage first-level administrative cases (under county level).

## SUBNATIONAL GOVERNMENT RESPONSIBILITIES

The 2012 Constitutional reform and the Cardinal Law on Local Governments have profoundly transformed SNGs in Hungary, reducing their scope, functions and financing resources. It recentralised several (or parts of) functions in education (primary and secondary education), healthcare (free medical services, hospitals, excluding specialised clinics), social protection (social allowances for the elderly, families, etc.), public hygiene, water works, and administration (document office duties). Counties lost several major competences (healthcare inc. hospitals, social initiatives and secondary education) to be mainly in charge of regional and territorial development, as detailed in the National Development and Territorial Development Concept (EU programming period 2014-2020), which makes them key actors of territorial development. Municipalities are no longer in charge of primary education but they keep several responsibilities in areas such as health care, social protection, environment, housing, community amenities and utilities, culture and sports.

### MAIN RESPONSIBILITY SECTORS AND SUB-SECTORS

	STATE LEVEL	MUNICIPAL LEVEL
1. General public services	Coordination tasks (regarding municipal service provision)	Internal administration; Administrative tasks; Issuance of various permits
2. Public order and safety		
3. Economic affairs/transport	Regional development; Rural development	Road maintenance; Public transport
4. Environmental protection		Environmental health; Waste management; Public parks
5. Housing and community amenities	Land-use planning	Land-use planning; Cemeteries; Street lighting; Maintaining and cleaning of public areas; Parking garages; Housing and property management
6. Health		Primary healthcare; Health protection
7. Recreation, culture & religion		Public library services; Performing art organisations; Protection of local cultural heritage
8. Education		Support to local community education
9. Social protection		Children protection support; Social provision tied to local government ordinances

## SUBNATIONAL GOVERNMENT FINANCE

<b>Scope of fiscal data:</b> county governments, municipalities, associations of local governments and local minority governments.	SNA 2008	Availability of fiscal data: <b>High</b>	Quality/reliability of fiscal data : <b>High</b>
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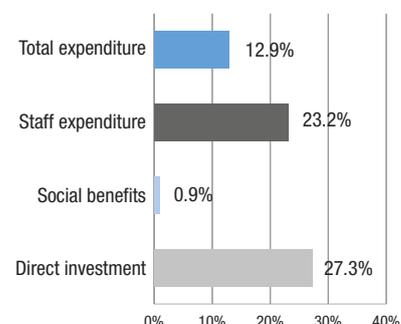
**GENERAL INTRODUCTION.** Despite the political autonomy of local governments, the Hungarian public governance system is now quite centralised on the fiscal side. Following the 2007-08 economic crisis and critical state of subnational finance prior to 2010 in Hungary, the national government undertook - in 2011 - an extensive constitutional reform leading to the recentralisation of resources, responsibilities and related expenditure, and debt. While municipalities have kept some local responsibilities and can levy their own resources through specific local taxes, the counties, are now deprived of any “general competences” and have gradually been excluded from the governance framework. On the other hand, the development of a township system reinforced the financial influence of the central state.

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## SUBNATIONAL GOVERNMENT EXPENDITURE BY ECONOMIC CLASSIFICATION

2016	DOLLARS PPP / INH.	% GDP	% SNG EXPENDITURE	% GENERAL GOVERNMENT EXPENDITURE (SAME EXPENDITURE CATEGORY)
<b>Total expenditure</b>	<b>1 608</b>	<b>6.0%</b>	<b>100%</b>	
<b>Incl. current expenditure</b>	<b>1 360</b>	<b>5.1%</b>	<b>84.5%</b>	
Staff expenditure	676	2.5%	42.0%	
Intermediate consumption	482	1.8%	30.0%	
Social expenditure	35	0.1%	2.2%	
Subsidies and current transfers	162	0.6%	10.1%	
Financial charges	2	0.0%	0.1%	
Others	3	0.0%	0.2%	
<b>Incl. capital expenditure</b>	<b>249</b>	<b>0.9%</b>	<b>15.5%</b>	
Capital transfers	44	0.2%	2.7%	
Direct investment (or GFCF)	205	0.8%	12.7%	

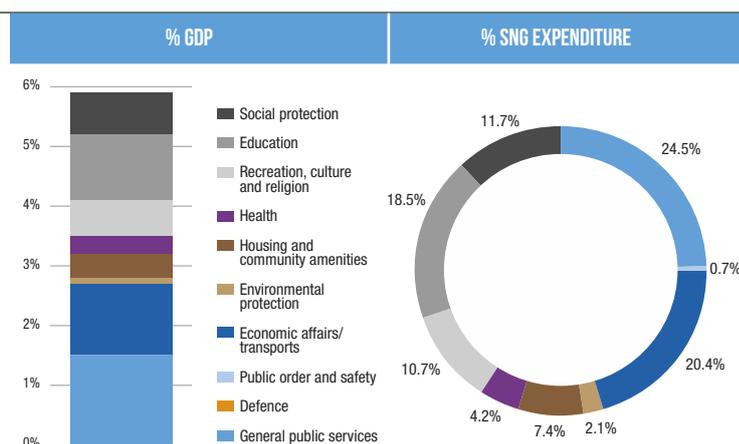


**EXPENDITURE.** As a result of the recentralisation of a large part of SNG responsibilities under the Local Government Act, the share of SNG expenditure in GDP and public expenditure decreased significantly from 2010 to 2016, by respectively 6.5 and almost 12 percentage points, to stand in 2016 well below the OECD average (amounting to 16.2% of GDP and 40.4% of public expenditure) and the EU28 average (15.5% of GDP and 33.4% of public expenditure). The share of SNG staff spending in total public staff spending went from 50% in 2010 to 23% in 2016, resulting from large transfers of personnel from SNGs to the new deconcentrated government offices. SNG staff spending decreased by 7.3% on average per year in real terms between 2007 and 2017.

**DIRECT INVESTMENT.** Following the global crisis and the recentralisation reform, the share of SNGs in public investment has kept decreasing, from 59% in 2011 and 39% in 2013 to 27% in 2016, well below the OECD average (56.9% of public investment) and the EU28 average (51.6%). As a share of GDP, SNG investment also decreased significantly from 2.2% of GDP in 2010 to 0.8% in 2016. SNG investment dropped by 2.5% on average per year in real terms from 2007 to 2017. In 2016, most SNG investing was dedicated to general public services (36%) and economic affairs and transport (25.4%), as well as housing and community amenities and environmental protection. The National Development and Territorial Development Concept (NDTDC), adopted by the Parliament in 2014 after extensive consultation across ministries, county councils and local governments, includes several goals for subnational development, such as the concept of polycentricism, and considers different levels of urban centres, including Budapest and 67 other towns as urban areas with (potentially) international relevance as regional poles, which could have an impact on investment.

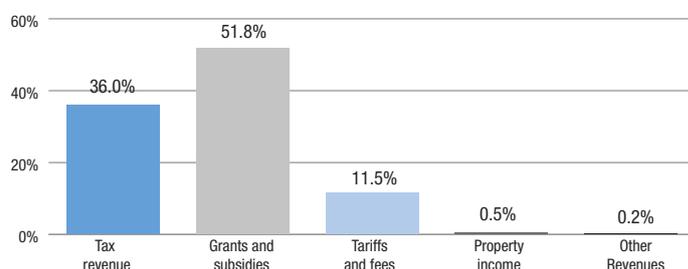
## SUBNATIONAL GOVERNMENT EXPENDITURE BY FUNCTIONAL CLASSIFICATION – COFOG

Main categories of SNG spending in 2016 included general public services (24.5% of SNG expenditure), followed by economic affairs/transport (20.4%), allocated in particular to regional development, road maintenance and public transportation. The sector in which SNGs play the biggest role is housing and community amenities (45.4% of total public spending in this area, or 0.4% of GDP), and to a lesser extent environmental protection (23.6% of public expenditure in this sector). The responsibilities of counties on matters related to health, education, social protection and culture have been continuously narrowing since the 1990s, as those tasks have been taken up by the central State. As a result, the shares of SNG spending in education, health, housing and community amenities, recreation and culture and environmental protection have sharply decreased since 2011.



## SUBNATIONAL GOVERNMENT REVENUE BY CATEGORY

2016	DOLLARS PPP / INH.	% GDP	% GENERAL GOVERNMENT REVENUE (SAME REVENUE CATEGORY)	% SNG REVENUE
<b>Total revenue</b>	<b>1 686</b>	<b>6.3%</b>	<b>14.1%</b>	
Tax revenue	607	2.3%	8.9%	
Grants and subsidies	874	3.3%		
Tariffs and fees	193	0.7%		
Property income	9	0.0%		
Other revenues	3	0.0%		



**OVERALL DESCRIPTION.** The administrative reforms led between 2011 and 2014, carried out in the name of reallocation of tasks between local and central levels and costs savings, modified the system of local finance in Hungary and restrained the fiscal framework for local government financing. The main source of revenues is grants and subsidies, accounting for almost 52% of SNG revenues, above the OECD average (37.2%) and the EU28 average (44.1%). By contrast, the share of tax in SNG revenues is small, below the OECD and EU averages (respectively 44.6% and 41.1%). Municipalities are the only level of SNG to be able to levy taxes. Tariffs and fees provided substantial revenues in 2016, in line with the EU28 average (11.6%).

**TAX REVENUE.** While tax revenues accounted for 36% of SNG revenues (excluding the counties), the share of SNG tax revenue in public tax revenue and in GDP was also well below the OECD average (respectively 31.9% of public tax revenue and 7.1% of GDP) and the EU28 average (respectively 24.0% of public tax revenue and 6.4% of GDP).

Municipalities receive - almost exclusively - own-source taxes, the main local tax being the local business tax (LBT) which amounted to 75.5% of municipal tax revenue in 2016 and 27.2% of SNG revenue. This tax is imposed on companies located or registered in the municipal area and based on corporate gross margins. The rate is determined by the municipality, but capped at 2%. The LBT is the third largest income-generating tax at national scale in Hungary, and plays an important role in the financing of local governments.

Property taxes are the second highest tax received at the subnational level, but has a relative small role in Hungary compared to other OECD countries. Municipal property tax revenue accounted for 17.5% of municipal tax revenue in 2016 and 6.3% of SNG revenue. It amounted to 0.4% of GDP, well below the OECD average of 1.1% of GDP in 2016. Recurrent taxes on immovable property levied by municipalities include a building tax and a land tax, both paid by owners, and based either on area or floor space or on the adjusted market value. As the tax base typically does not depend on market value, revenues from property taxes remain low despite increases in property prices. Tax rates are set by each municipality, up to certain limits based on the consumer price index. It also includes a communal tax on households and a community tax. The number of municipalities levying building tax, land tax and communal tax has grown. In fact, by 2015 over 85% of municipalities had introduced such taxes. Other minor taxes include a vehicle tax (a shared tax), a municipal tourist tax and an environmental protection charge.

**GRANTS AND SUBSIDIES.** The 2011 constitutional reform modified the grants system and reduced their amounts, in accordance to the recentralisation of several local government responsibilities. Transfers to SNGs decreased by 4.6% on average per year in real terms between 2007 and 2017. Overall, grants and subsidies amounted to HUF 661.7 billion, compared to HUF 1 421.7 billion in 2008. As such, funds transferred from the Health Insurance Fund decreased sharply.

A stricter grant system was set up in 2013, shifting from an income-based system of block grants, to a task-based, expenditure-oriented system of earmarked grants for each local authority. Grants are now earmarked, for the vast majority to current expenditure (82.6% of total grants), and mainly in the fields of education, social protection and culture. The reform included the tightening of distribution rules as well as new equalisation criteria based on the tax capacity of each municipality, with the aim of assisting poorer regions, due to striking differences between local governments in terms of local business tax capacity. Thereby, some of the municipalities with low tax-income capacities receive a grant supplement. A mandatory deficit grant was also designed to cover for the deficit of municipalities. Overall, state funding may be granted twice a year to municipalities in difficulty, and grants are voted yearly by the Parliament.

**OTHER REVENUES.** Other revenues for municipalities include mostly user tariffs and fees for public services, which represented around 11.5% of total subnational revenues in 2016, against 14.9% on average in OECD countries but 11.6% in the EU28. Income from property is quite limited, below the OECD and EU28 averages (respectively 2.0% and 1.2% of SNG revenues).

## ■ SUBNATIONAL GOVERNMENT FISCAL RULES AND DEBT

2016	DOLLARS PPP/INH.	% GDP	% GENERAL GOVERNMENT DEBT	% SNG DEBT
<b>Total outstanding debt</b>	<b>135</b>	<b>1.1%</b>	<b>1.1%</b>	<b>100%</b>
Financial debt*	28	0.2%	0.3%	20.7%

\* Currency and deposits, loans and bonds

**FISCAL RULES.** Tighter budgetary restrictions and new borrowing controls were introduced for SNGs in 2011 by the Cardinal Local Government Law, as part of efforts to reduce the national public debt. It forbids any operating deficit, and stipulates that SNGs are responsible for their own financial management. However, there is no national stability pact agreement between the central and local levels.

**DEBT.** The Cardinal Local Government Law set up an authorisation framework for local borrowing in 2012. Following the 2013 reform, the total debt of Hungarian local governments accumulated from 2002 to 2008 was taken over by the central government and consolidated in full between 2011 and 2014. It was done progressively in three stages based on the size of SNGs. The ratio of debt to be taken over was determined on the basis of the number of inhabitants in a particular municipality and the taxation power measured by the local business tax. As a result, the amount and the structure of outstanding debt profoundly changed, SNG debt accounted for 1.1 % of GDP in 2016 compared to 4.5% in 2010, and 1.1 % of public debt. It is made up of other accounts payable for 79% (commercial debt, arrears), the remaining part being financial debt ("Maastricht debt"). Financial debt is mainly composed of loans (92%), the share of bonds being 8%.



Lead responsible: OECD  
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**Socio-economic indicators:** OECD // Eurostat // World Bank // UNDP // UN Desa // ILO // Hungarian Statistical Office.

**Fiscal data:** OECD National Accounts Statistics // OECD Revenue Statistics // OECD (2018) Subnational Government in OECD countries: key data (brochure and database) // Eurostat.

**Other sources of information:** OECD (2019) OECD Economic Surveys: Hungary 2019 // OECD (2018) Regions and Cities at a Glance 2018 // Éva Margit Kovács (2018) The impact of public service capacity on municipal cooperation in Hungary // European Committee of Regions (2016) Division of Powers // Palne Kovacs I. (2015) Regionalism in Hungary, Assembly of European Regions // Steiner E. (2017) Introduction to the Hungarian Local Government System // OECD (2015) Hungary: Reforming the State Territorial Administration // Ministry of National Economy (2015) Hungarian Local Government economic management and financing systems // Lentner C. (2014) The Debt Consolidation of Hungarian Local Governments.