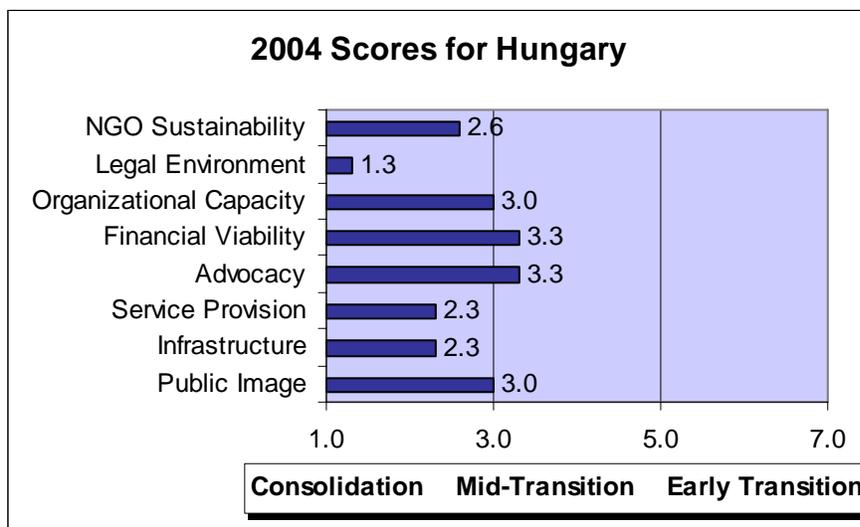


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**HUNGARY**


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**Capital:** Budapest

**Polity:** Parliamentary democracy

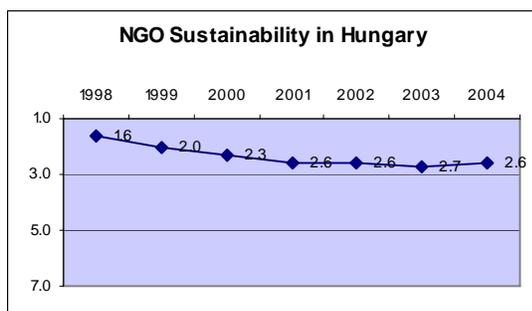
**Population:** 10,000,000

**GDP per capita (PPP):** \$13,900

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**NGO SUSTAINABILITY: 2.6**


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The formal establishment of the National Civil Fund (NCF) was a major development in the Hungarian nonprofit sector in 2004. The Hungarian government pledged to match all funds designated by individual taxpayers to the NCF under the “1% Law” to support the operational costs of civil society organizations in Hungary. The NCF, along with a few other new major sources of funding, such as the Trust for Civil Society in Central and Eastern Europe and the European Union’s Structural Funds, provided some relief this year after the serious liquidity crisis in 2003, which drove many of those NGOs that managed to

survive it to scramble for funding, often to the neglect of other forms of fundraising or constituency development.

The first year of the NCF’s existence has proven to be analytically useful because the turmoil surrounding its operations shed some new light on the state and functional capacity of the nonprofit sector. The first two rounds of applications to its grants provided ample evidence of a lack of strategic planning and financial management (or even just proposal-writing) capacity, as well as concerns about conflicts of interest within the majority of Hungary’s nonprofit organizations. On the other hand, the successful institutionalization of the NCF can also be interpreted as evidence of the Government’s political will to recognize and empower the nonprofit sector. Such an interpretation should, however, acknowledge the continued lack of consultation with the sector by the Government on other serious budgetary or legislative issues.

The “1% Law,” which allows individual taxpayers to allocate 1% of their annual payments to a qualifying NGO of their choice, is now in its 7th year. Increased participation in the program by NGOs and the public is indicative of a gradual rise in the professional capacity of a pool of organizations within the sector that are making serious efforts to mobilize public support for their causes.

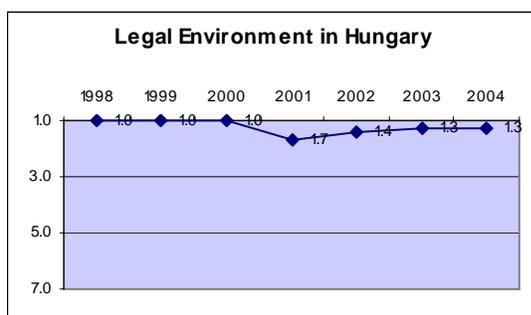
Although the financial situation of the sector improved since the liquidity crisis in 2003, Hungarian nonprofit organizations in 2004 continued to be significantly challenged by organizational sustainability concerns, by their exclusion from political policy-making processes, by difficulties encountered with mobilizing local resources, and by their struggles to respond effectively to changes in the environments within which they operate.

### LEGAL ENVIRONMENT: 1.3

No actual legislative changes were introduced in 2004 to positively or negatively affect the legal environment of NGOs in Hungary. Unfortunately, the Parliament has adopted neither the new Law on Legislation nor the new Law on Volunteerism, which together would have helped address both the lack of an enabling legal environment for public participation as well as critical NGO needs in general. The bills were submitted to Parliament in late 2003 and early 2004, respectively.

framework, including problems with the establishment of foundations, which in its current state encourages people to find purely symbolic founders to register the NGO for them.

Operationally, NGOs are relatively well protected by legislation and are not subject to arbitrary dissolution by the state. Indeed, in some cases, it is arguable that they are *too* well protected, and the state is too willing to support organizations that are dysfunctional, hopelessly unsustainable or bankrupt. On the other hand, the government has perhaps been less interested than its counterparts in neighboring countries in the region to involve the NGO sector in issues directly affecting them (such as budget and tax reforms) and there continues to be a serious lack of negotiation and public participation of any form before the final drafting of legislation.



It is relatively easy for Hungarian NGOs to legally register themselves, although gaps in current legislation still make it very difficult for branches of international NGOs to register. Furthermore, a recent comprehensive study of the legal environment affecting NGOs raised a number of issues about the basic legislative

Local legal capacity is characterized by the presence of adequate legislation, but also by the absence of NGO capacity to take advantage of it. Legal assistance to NGOs is generally available, but expensive and therefore inaccessible for most NGOs beyond meeting their registration needs. Legal assistance outside of Budapest is

even more difficult to find. This is also the case for issues regarding earned income, where legal mechanisms exist, but where problems have arisen with implementation due to a great deal of confusion within the sector about what constitutes taxable “business” activities.

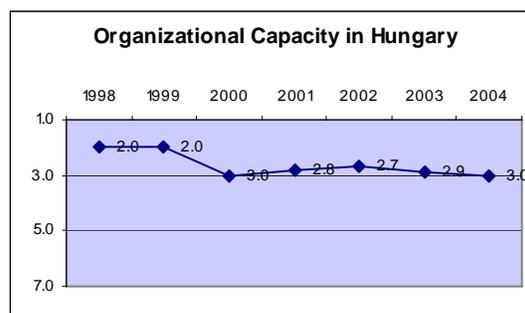
Hungary’s high levels of taxation continue to be seriously burdensome for the non-profit sector. This burden was added to in 2004 with the introduction of the 25% VAT on several services often provided by nonprofits that were previously exempt, such as adult education, which has

increased costs significantly. Although a tax benefits system is in place and is functional, incentives for charitable giving decreased in 2004 with the introduction of an income ceiling level above which taxpayers cannot take advantage of any tax benefits, including tax credits for donations. Furthermore, there does not appear to be a great deal of effort being made by the NGO sector to explore ways of making better use of the tax system for fundraising purposes, which is symptomatic of the sector’s heavy focus on donor sources of funding.

### ORGANIZATIONAL CAPACITY: 3.0

A major source of new funding came in the form of the NCF that was established to support the operational and institutional costs of Hungarian NGOs. However, the process by which that funding was distributed was criticized, particularly with regards to its transparency and the consistency of the decisions made, as well as for the relative lack of substantive requirements for proposals. However, what made the first two rounds of applications for NCF grants unexpectedly dramatic were the high number of applications that were rejected (e.g. 60% of all applications in the first round), largely for applicants’ failure to comply with the overly rigid formal criteria. On the other hand, concerns have been raised about the NCF’s lack of a concrete overall strategy to develop the Hungarian civil society sector, without which the Fund was not properly selective of those organizations that did manage to submit complete applications. As a result, the NCF now supporting a number of NGOs, rather than providing incentives for them to reform or dissolve. Serious cases of conflicts of interest were also common,

which was also evident in the results of the NCF grant applications, where some of the most successful applicants were NGOs enjoying special relationships with one or more members of the decision-making bodies (NCF Council and Colleges).



Over the past few years, the 1% Law has motivated NGOs to build bases of support with the public. However, in spite of the increased level of competition for 1% tax funds, it seems that most NGOs are limiting these constituency-building efforts to the time of the year when people file their taxes. For the rest of the year, NGOs tend to turn their attentions elsewhere and devote

more of their resources to writing proposals for external donor funding opportunities.

The applications for grants from the implementing partners of the Trust for Civil Society in CEE was also a litmus test for the sector and clearly indicated a low capacity for strategic planning among Hungarian NGOs. Many applicants failed to qualify precisely because of their lack of strategic plans. Although there is a small 'elite' group of NGOs that has made serious efforts to develop plans for their sustainability, the majority of NGOs are very donor-driven and structure their short-term planning according to external funding fluctuations. The need to improve planning capacities and management structures is evident throughout the sector, but thus far sector-wide changes have yet to materialize.

The combination of rigorous labor protection offered by the Hungarian Labor Code with high taxation levels for employers has made it very difficult for

NGOs to afford full-time staff and to be flexible enough to respond to market and liquidity fluctuations. As such, the state administration enjoys a relatively unequal competitive advantage over NGOs in providing services to the public. In addition, the abolition of compulsory military/civil service removed over 5000 young people from the labor market, who would otherwise have chosen to complete their service requirements with NGOs.

There is a huge technological gap between urban and rural NGOs, with the latter being less able to access information or communications technology, while the former have adequate access to equipment and office space. The very high prevalence of the use of pirated software is also an object of concern for the sector's legal legitimacy, yet at the same time, the systems of several organizations are vulnerable to virus threats for lack of adequate protection software.

### **FINANCIAL VIABILITY: 3.3**

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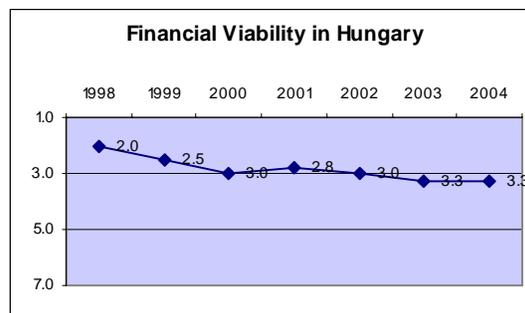
Despite the controversial disqualification of many aspiring grantees in the first two rounds of applications, the NCF distributed 25 million USD after receiving 4,179 applications, of which it gave 18.5 million USD to support the operational costs of 3,478 organizations. At this stage, it is difficult to predict how much the NCF will actually contribute to the long-term financial sustainability of the nonprofit sector, given that the absence of guidelines or restrictions to ensure that those nonprofit organizations who received funding spend accountably and reliably.

A great deal of new funding is also now available in the form of EU structural funds. These funds specifically encourage pooling resources and partnerships between NGOs and local stakeholders, but have proven to be as much of a distraction for NGO fundraising efforts as the NCF funding has been.

Despite the withdrawal of many international donors from Hungary in recent years, and a continued lack of local grant/giving foundations, there are still a number of major funding sources for NGOs to draw from, such as the NCF, EU, Trust

for Civil Society in Eastern and Central Europe, and a few private foundations. Despite this, there is still relatively little willingness on the part of NGOs to diversify their funding bases, and most are content to depend heavily on one or two major donors and hope for the best, a tendency that was ruinous in 2003. Furthermore, all of the changes to the funding environment have made NGOs less motivated to actively fundraise this year than perhaps in the past. Some feel that it would be better to wait until it becomes clearer how the changes will affect them before launching laborious fundraising campaigns, while others are more interested in only targeting NCF grants. At the same time, however, there was a noticeable increase in competition for funding from taxpayers via 1% tax scheme. Although this is an encouraging sign of an increased willingness to engage the public, the earning potential for each participating organization is getting lower and lower as more and more organizations enter the 1% arena to compete. More NGOs are also experimenting with direct mail campaigns, although it is too soon to know how successful these efforts have been.

Larger NGOs have to date developed rather good internal financial management systems, and more and more bookkeepers are available who have experience working with nonprofit organizations. On the other hand, the first two rounds of NCF funding revealed that many smaller NGOs in Hungary have weak and underdeveloped financial management systems. It is difficult to know for certain, though, because so few NGOs make their finances publicly available, and it is only the public benefit organizations that are required to do so by law.

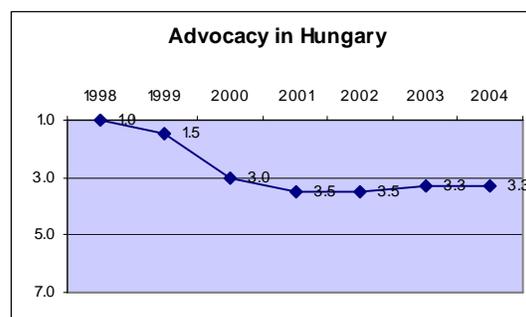


Corporate private philanthropy is slowly emerging in Hungary and this is particularly evident with the creation of private foundations by wealthy Hungarian entrepreneurs. In a 2003 study of corporate philanthropy in Hungary, almost two-thirds of the interviewees had given some kind of support to nonprofit organizations, with a further 20% indicating a willingness to do so. The main mission areas that corporate giving supported in 2004 were generally the same priorities shared by the majority of individual donors: children, health and education. Although it is clear that the business and corporate community in Hungary is thinking in increasingly ethical ways, one cannot yet say that corporate social responsibility is widespread or that it has become an entrenched part of Hungarian business culture.

A functional legal framework exists in Hungary for NGOs to conduct income-earning activities, however it does not appear to be properly implemented by NGOs and there is still some confusion on their part as to which activities are legitimate and which are not. Membership dues are rarely collected by membership organizations, partly due to the general assumption that one cannot ask for money from one's members (especially in organizations of the disadvantaged), and partly due to a lack of proper member databases and a general lack of communication between the organizations and their members.

### ADVOCACY: 3.3

The 2003 government pledge to expand consultation with the NGO sector has unfortunately not materialized beyond the establishment of the NCF. Indeed, any consultation generally followed past patterns, where NGOs might be consulted on the areas of their particular expertise, but not in more sensitive areas such as budgeting or funding decision-making. Any consultation that did occur was done on terms decided by the government, often leaving NGOs powerless to shape the discourse in any way other than responding when given the opportunity to do so. Often government agencies seemed to be reluctant to ask for consultation, and often made the process awkward, such as by giving very little time to review lengthy documents, thereby limiting the amount of input that NGOs can provide. At the same time, however, the lack of regular consultation is also because many NGOs don't exercise their rights or potential to influence the lawmaking process. In some cases they are deterred because of a lack of know-how and experience in lobbying and affecting decision-making processes, or their inability to research and acquire adequate public interest data. Despite this, there is a possibility that Hungary's accession to the EU will encourage closer consultative contact between governmental bodies and NGOs, due to EU-level policies, as well as funding requirements.



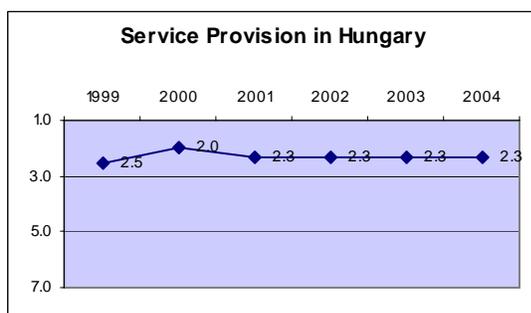
Over the past year, there were a few successful advocacy initiatives, most of which were launched by environmental activists. An encouraging example of a success came in the form of a large campaign against NATO and the Hungarian Army to prevent the installation of a radar locator in the mountainous region outside the city of Pécs. The campaign sparked a huge media debate over the relative importance of national defense over environmental conservation and vice versa. If anything, this experience demonstrated that the Hungarian media and the public are capable of holding and sustaining advocacy-related debates of this sort on a national level. In general, though, the majority of advocacy campaigns in Hungary are normally initiatives of individual organizations or associations with limited capabilities for outreach, an indication that issue-based coalitions are still rather untypical and rare in Hungary.

### SERVICE PROVISION: 2.3

The 1% Law scheme and the requirements for EU Structural Funds were strong motivators for nonprofit organizations to improve the services that they provide and to be more responsive to the priorities of those sectors of the public that they serve.

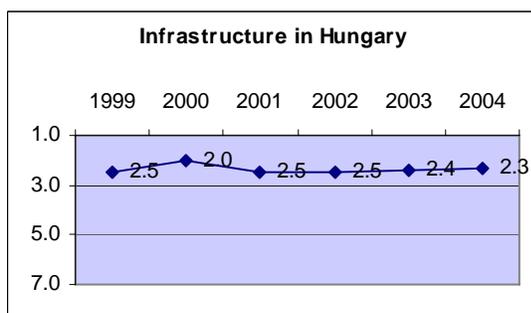
This was mostly the case with organizations that work in children's health, disability and employment issues. It does appear that the NGO sector as a whole is becoming increasingly conscious of the need to improve the quality of its services, but this

has not actually translated into concrete improvements across the whole sector as of yet. The services that Hungarian NGOs are providing are almost invariably directed beyond their membership, but that is largely because the concept of membership is still not very well understood by the sector. Indeed, the main time when serious efforts are made to communicate to members is in the spring, when they are encouraged to support their NGOs via the 1% Law (see also “Organizational Capacity” above).



Cost recovery for services provided is seriously affected by the fact that many NGOs lack adequate financial systems that can calculate costs accurately. Again, the application procedure to NCF funding exposed the infrastructural weaknesses that are apparently typical of the majority of smaller NGOs in Hungary. Despite these apparent weaknesses, one should not forget that the creation of the NCF did essentially demonstrate that the government values the presence of NGOs as service providers, enough so that it is willing to provide a considerable amount of basic institutional funding to support them. In addition, a separate budget and grant program is available from the NCF for quality development.

### INFRASTRUCTURE: 2.3



National Civil Houses act as ISOs to the Hungarian nonprofit sector and continue to receive support from the state to provide local infrastructural support to the sector, but it is hard to tell whether their work has been effective or not. The success of their work is partly dependant on their own capacity, but also on whether or not the NGO sector makes serious use of their support and assistance. ISOs themselves are not grant-making bodies, and therefore

are of less interest to many NGOs than institutions that can provide funds, all of which exist at only the national or international levels, with practically none functioning locally.

Through the National Civil Fund, the Hungarian government has made itself a leader in the region for the amount of funding it is providing in support of nonprofit research in a wide array of topics. This year, the NCF provided 514,000 USD in funds to 36 research projects.

Similar to the problem of a relative lack of issue-based campaign coalitions, there is also little in the way of NGO coalition-building in Hungary. Communications technology allows for a significant amount of information sharing between NGOs, but actual collaborative efforts on shared

projects is rare. In rural areas, there appears to be more cooperation, both within the sector and outside of it, as NGOs work with each other and with farmers on local development projects. Some progress is being made to develop NGO networks within the sector as a number of organizations have realized that their 'in-house' and informal networks are limited in their usefulness and that there is a need for more formal network-building efforts.

Training opportunities within the sector have increased since the previous year,

largely because of the significant investment made by the Trust for Civil Society in advanced training-of-trainer programs. This is particularly the case in rural areas where there is evidence of increased competition among training providers, when a few years ago this was not the case. In addition to externally funded programs, the NCF provided 693,000 USD for 76 applications from NGOs for training this year, although these will largely be delivered next year so their impact will not be felt imminently.

### **PUBLIC IMAGE: 3.0**

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The big media story for 2004, of course, was the institutionalization of the NCF, which generated more media interest than the nonprofit sector has normally enjoyed in the past. This interest tapered off by the beginning of the summer, however, and for

the rest of the year there was very little coverage of the nonprofit sector. Any coverage that did make it into print usually focused on scandals and negative issues, rather than on communicating NGO visions and achievements. Although it is evident from the increasing rate of response to the 1% Law that the public is becoming increasingly aware of the NGO sector, one must wonder how the media is shaping that impression given how selective it has been with the stories it published. Recent research has indicated that attitudes regarding the NGO sector within the business community are generally negative. Although rates of business giving are slowly increasing, the business sector is rather critical of the nonprofit sector, particularly for its lack of professionalism. The formation of the NCF was a clear indication of the Hungarian government's

interest in supporting the nonprofit sector, yet its uncritical funding policy is also indicative that it has only a superficial understanding of the players within the sector. At the same time, there is a similar lack of knowledge about the nonprofit sector within the sector itself. Although leading NGOs publish and disseminate annual reports regularly, this is not necessarily the case for the majority of the smaller, less developed organizations, and few opportunities are explored to share experiences and learn from one another. Furthermore, on the rare occasions when NGOs do come together to collaborate, it is to join forces to lobby the government, and not to improve their transparency or self-regulate.

