# HUNGARY

In 1997, the U.S. Trade deficit with Hungary equaled $592 million, an increase of $246 million from 1996. U.S. merchandise exports to Hungary in 1997 were $486 million, an increase of $155 million (46.8 percent) from 1996. Hungary was the United States' sixty-seventh largest export market in 1997. U.S. Imports from Hungary were $1.1 billion in 1997, an increase of $401 million (59.3 percent) from 1996.

U.S. foreign direct investment (FDI) in Hungary since 1989 totaled almost $6 billion at the end of 1997, of total FDI in Hungary of about $17 billion. Hungary is the leading recipient of U.S. investment in the region. Hungary was among the first Central and Eastern European command economies to implement some market-based reforms prior to the democratic transition in 1989-90. The current government continues to promote economic restructuring and market institutions.

Privatization and direct foreign investment are having positive multiplier effects throughout the economy. Continued foreign investment is a reflection of the government's ability to maintain economic stability, reduce inflation, and successfully complete its goal of privatizing at least 80 percent of gross domestic product (GDP) by the end of 1998.

## IMPORT POLICIES

Import policies have been progressively liberalized in an effort to encourage competition and to allow imports necessary for restructuring. Over 95 percent (by value) of products can be imported without an import license. An import license is required for precious metals, military goods, and certain pharmaceutical products. The state monopoly on foreign trade was eliminated in 1989.

In January 1995, Hungary raised many agricultural tariffs to Uruguay Round binding ceilings and introduced numerous tariff-rate import quotas that are assigned to most-favored nation (MFN) or preferential suppliers. There are also high tariffs imposed on wines and spirits which is compounded by excise taxes which favor locally produced products over imports. In addition, imported, but not domestic spirits are required to carry tax stamps.

Under an agreement with the World Trade Organization (WTO), Hungary will eliminate quotas on textiles, clothing, and other industrial products by 2004. As of January 1, 1998, import quota licenses are no longer required from WTO member states for imports of new vehicles with engine capacity greater than 1500 cc, apparel, medicine, used clothes, string and thread, carpets, and those types of radio receivers not produced in Hungary. Import quotas totaling $408 million in 1998 will apply to apparel from non-WTO states, carpets, jewelry, and a handful of industrial products. However, on average, quotas are only 60 percent utilized and no quota was fully utilized in 1997, so they do not appear to limit trade in practice.

The government of Hungary will grant import licenses for up to 68,000 new and 63,000 used cars in 1998, below the 200,000 total cars imported in 1991, but well above recent import levels. Weak local purchasing power still inhibits auto imports, but is improving. The customs duty law of 1995 forbids the importation of used cars over six years old. Specialized older vehicles may still be imported after passing a technical test.

These regulations, combined with standards for used cars which tend to exclude older U.S. models, effectively curb most used car imports from the U.S.

Hungary's average most-favored nation (MFN) import duties have been cut from 13.6 percent in 1991 to eight percent in 1997. An eight percent import duty surcharge introduced in March 1995 was eliminated on July 1, 1997. Under Hungary's 1991 EU Association Agreement and subsequent accords, tariffs for industrial imports from the EU and CEFTA are being substantially eliminated by the end of 2001. Under the Pan-European cumulation system and Pan-European free trade zone, effective in Hungary since July 1, 1997, customs duty on the imported content of goods subsequently exported under preferential trade agreements is no longer refunded. However, content from any member state can accumulate to qualify for preferential treatment. The Hungarian government introduced a new EU harmonized tariff schedule for 1997 with lower tariffs for imports from EU and CEFTA members. In the past year, several U.S. exporters (e.g., of autos, electrical generating equipment, wine and commercial laundry equipment) have expressed concern over the tariff preferences provided to the EU by Hungary. A review is planned in 1998 to study the effects of such preferences on U.S. competitiveness.

On January 1, 1997, the government eliminated for WTO members a two percent statistical fee and one percent customs clearance fee. Fees totaling five percent, however, are still required of goods coming from non-WTO states. Duties and fees on re-exported content are no longer refunded as of July 1, 1997 for non-EU importers, which has adversely affected certain U.S. industries (e.g., lumber and veneer producers). Firms exporting from Hungary with inputs from non-WTO members (such as Russia) were faced with greater costs and additional customs fees. An American aluminum producer, for which unrefunded fees would have totaled over $5 million per year, secured an 18-month waiver of these fees under the modified customs law which went into force August 1, 1997.

Standards, testing, labeling, and certification importers must file a customs document with a product declaration and, upon importation, present Hungarian certified documentation from the commercial quality control institute to clear customs. This permit may be replaced by other national certification and testing agency documents, such as those of the National Institute for Drugs. Some standards are reciprocal with those of recognized U.S. standard enforcement agencies. Hungary participates in the international electro-technical commission.

## STANDARDS, TESTING, LABELING AND CERTIFICATION

### Animal and Plant Health Regulations

Hungarian import regulations limit or delay imports of breeding animals, semen, planting seeds, and new plant varieties. The process of registration and testing of new plant varieties imported is time-consuming and costly. Relevant authorities (Institute for Agricultural Qualification and Ministry of Agriculture) set minimum breeding values for imported bovine semen and require repeated tests before distribution of the import shipment. In recent years, restrictive testing practices and industry association fees for imported bovine semen have made imports more costly, time-consuming, and uncertain. In late 1997, the US government received assurances that these fees and practices would be modified, but some discrimination likely remains, which affects a potential market on the order of $1 million per year for U.S. firms.

## GOVERNMENT PROCUREMENT

Foreign access to government-funded construction and service or supply contracts is regulated by the act on public procurement, effective November 1995, which increased transparency in public procurement. Tenders must be invited for the purchase of goods worth over 10 million forints (currently 200 forints equal one dollar). However, bids with more than 50 percent Hungarian content are considered equal to majority-foreign bids that are up to 10 percent lower in price. Purchases deemed to be related to state security, as well as purchases of gas, oil, and electricity, remain exempt from these regulations. The U.S. pharmaceutical industry reports a lack of transparency in the selection process of government tenders.

## EXPORT SUBSIDIES

Hungary maintained agricultural export subsidies in excess of its WTO commitments from 1995 to 1997, claiming that its base-period calculations had underestimated the true value and product coverage of subsidies during the Uruguay Round. Hungary proposed a revised schedule which would have substantially surpassed its original commitments in the number of items covered and monetary level. In October 1997, after formal complaints by the U.S. and other WTO members, Hungary committed to phase out excess export subsidies over a several-year period and agreed not to use subsidies to penetrate new export markets.

## LACK OF INTELLECTUAL PROPERTY PROTECTION

One of the greatest intellectual property rights (IPR) problems in Hungary is the lack of effective prosecutorial enforcement. The level of piracy for motion pictures and computer programs has decreased significantly but much improvement is still necessary. The copyright legislation also needs to provide for retroactive protection of U.S. works and civil ex parte search provisions, and the pipeline protection law for patents needs some refinements.

### Patent Protection

Protection of patent rights in Hungary was strengthened following the conclusion of a comprehensive U.S.-Hungary bilateral agreement on IPR protection in 1993. Under this agreement, Hungary agreed to provide patent protection for pharmaceutical products; under prior law, patents were limited to processes for producing pharmaceuticals. The bilateral IPR agreement also provides transitional pipeline protection for U.S. pharmaceutical products otherwise ineligible for new product patents in Hungary; provides that patents are available and that patent rights apply regardless of whether products are imported or locally produced; and provides limitations on the use of compulsory licenses. Implementing legislation entered into force on July 1, 1994.

There are, however, some limitations of Hungary's pipeline protection law that make pipeline protection inadequate under certain circumstances. For example, no pipeline protection can be obtained for those products where a corresponding foreign counterpart patent issues after the effective date of Hungary's pipeline law (*i.e.*, after July 1, 1994). The pipeline protection law also entails the uncertainty that a Hungarian company, once an invention is published, may have started work to develop a corresponding product before the innovator gets to file his or her pipeline application. Under such circumstances, it appears that a patent holder could then not enforce the pipeline patent. In addition, there is also a problem with Article 20 of the new law and the apparent incorrect application of the "modification of priority" concept.

There are also persistent problems in the Hungarian judicial system which makes prevention of patent infringement difficult. U.S. interests have not been able to obtain injunctive relief prohibiting the marketing of products the courts have determined to be infringing. In 1997, the Hungarian government strengthened access to legal injunctions and acted to reduce the backlog of court cases, but this did not affect ongoing IPR disputes, including a long-standing patent infringement suit by a large U.S. pharmaceutical firm. In addition, there is lack of technical expertise in patents by the courts, which can result in patent infringement cases taking three or more years to reach conclusion. Penalties awarded in such cases are also considered too low to act as effective deterrents.

**Copyright Protection**

Hungary's copyright laws largely conform to international standards, but certain legislative steps still need to be taken before Hungary meets its bilateral IPR and TRIPS commitments. The 1993 bilateral IPR agreement recognizes an exclusive right to authorize the public communication of work, including to perform, project, exhibit, broadcast, transmit, retransmit or display; it also requires that protected rights be freely and separately exploitable and conferrable (contract rights), and recognizes an exclusive right to authorize the first public distribution including importation for protected works. Nonetheless, to meet its TRIPS obligations, Hungary still needs to provide full retroactivity for sound recordings and civil ex parte search provisions.

In May 1993, Hungary added stiff penalties for copyright infringement to its criminal code. Despite the law, limited enforcement resources allow piracy to continue in the gray economy and the fines actually imposed are generally too low to be effective.

The U.S. motion picture industry reports video and cable television piracy to be a continuing problem in Hungary, as well as some satellite piracy. This industry estimates annual losses due to audiovisual piracy in Hungary were approximately $18.0 million in 1997 and that 40 percent of all motion pictures are pirated.

A U.S. software industry group estimates losses due to piracy of business software were $19.6 million in 1997 and that 58 percent of business software is illegal. Under current law, employers are prevented from exercising all economic rights with respect to software created by employees, which deters foreign and local investment in software development and publishing. Protection for encryption signals also needs to be provided under Hungarian law by prohibiting unauthorized retransmission of signals and prohibiting the manufacture, distribution, possession, sale, rental and use of unauthorized descrambling devices.

The U.S. sound recording industry estimates losses due to the piracy of sound recordings and music compositions were $7.0 million in 1997 and that the audio piracy level is 20 percent. Increased border protection is necessary since pirated recordings are entering Hungary from neighboring countries (*e.g.*, Bulgaria, Romania and the Czech Republic). Finally, there are also reports of book piracy amounting to an estimated $4.5 million in losses in 1997.

**SERVICES BARRIERS**

The Hungarian forint is fully convertible for current account transactions. The Hungarian government has gradually eliminated nearly all restrictions on long-term capital account transactions. In particular, as of January 1, 1998, restrictions were eliminated on (a) non-resident purchase of collective investment securities to open-ended investment funds, (b) resident firms acceptance of foreign credits or loans in excess of $50 million, (c) resident firms' loan payments abroad, (d) resident persons borrowing abroad, and (e) residents' investments in instruments of OECD-based issuers of less than investment grade. Restrictions remain on non-resident investments in instruments with less than one-year maturity. In keeping with Hungary's commitments at the time of its OECD accession in May 1996, foreign financial institutions may operate branches and conduct cross-border financial services in Hungary as of January 1, 1998.

Public television is required to fill 70 percent of its air time with European production, 51 percent of which must be Hungarian, excluding advertising, news, sports, game and quiz shows. Hungarian film quotas in the 15 to 20 percent range apply to public television. These quotas are not seen as cutting actual U.S. market share. For private broadcasters, the 1995 media law reserves for Hungarian programs 10 percent of program time excluding films (increasing to 15 percent after January 1, 1999), which does not in practice limit U.S. programs. In selling licenses for two private national television frequencies in 1997, the national radio and television board (ORTT) mandated a European quota of 50 percent of total annual program time, excluding ads, news, sports, games (lesser Hungarian content quotas apply as well). It is not yet clear whether these quotas will cost U.S. market share, since U.S. feature films and television productions retain a very strong presence, especially in prime time.

The Hungarian Parliament recently passed legislation which restricts the practice of foreign lawyers or law firms. The law would require that such foreign legal practitioners establish an association agreement with a Hungarian firm or lawyer before providing legal services. Many U.S. firms operating in Hungary believe the new requirements could lead to significant restriction on their practice of law and limit future investment in Hungary.

## INVESTMENT BARRIERS

After a sharp increase in privatization efforts in 1995, privatization continued strongly in 1996 and 1997. The Hungarian government passed a new privatization law in May 1995 that reduces to 25 percent from 50 percent the average amount of permanent ownership the government would retain in nearly all of the 163 companies identified as requiring permanent state participation. In 1997, the Hungarian government decided to reduce its 25 percent stock in a number of companies to a single golden share. This opened a significant number of companies to foreign investment. Small portions of other firms are being reserved for Hungarian citizens, for employee stock ownership programs and/or management buyouts.

Government delays in introducing energy price in 1995 and 1996 caused U.S. firms and foreign firms to fall short of the cost-plus-eight percent returns stipulated in energy privatizations. The introduction of regular quarterly energy price increases has improved profitability, but foreign firms still seek an eight percent return. Hungary terminated its blanket tax incentives for foreign investors as of January 1, 1994 and replaced them with incentives open to all large investors, based on export promotion, reinvestment of profits, and job creation in areas of high unemployment. Other recent tax incentives target investment to depressed eastern areas of the country. A customs law, passed in late 1995, eliminated duty-free importation of capital goods by foreign-owned companies. The law was intended to place domestic investors on an equal footing with non-Hungarian investors, but it eliminated a prior incentive to invest in Hungary.