VJT & PARTNERS

DOING BUSINESS

IN HUNGARY

2024

Preface

Doing Business in Hungary 2024 is a practical handbook for companies and individuals thinking about Hungary from a business point of view. The approach running through the guide makes it an essential resource for those considering establishing and those already operating a business entity in Hungary.

This three-part guide highlights the most important laws to be aware of during the establishment and operation of a business in Hungary, as well as numerous other issues which may arise during the "life" of a business, such as intellectual property and competition law issues.

You may wonder what makes this guide unique and different to other guides. Well, in addition to having a very business-focused approach, although written by lawyers, it is not full of legal jargon. This guide is, we hope, easy to understand, informative and filled with frequently asked questions which arise when setting up and running a business in Hungary.

We hope that our handbook provides you with many valuable tips and all the information you need on how to do business in Hungary.

Doing Business in Hungary 2024

Editor: Rebeka Németh

Publisher: János Tamás Varga, VJT & Partners Law Firm

1126 Budapest

Kernstok Károly tér 8.

Hungary

T: +36 1 501 9900

F: +36 1 501 9901

E: office@vjt-partners.com

This handbook has been prepared for the use of clients, partners and staff of VJT & Partners.

It is designed to provide general information for those considering doing business in Hungary and is not intended to be a comprehensive document. Therefore, we recommend consulting with us before taking any further action.

Table of Contents

Why Choose Hungary?

"It is not enough to be Hungarian; you must have talent as well."

—Alexander Korda

- Hungary is a welcoming country with rich natural beauty and cultural traditions
- Budapest is one of the most beautiful capital cities in Europe
- Located in the heart of Europe
- Business-friendly environment
- Membership in the European Union and in NATO
- Long-term political stability
- EU-conform investment incentives
- Highly developed logistical, transport and communications infrastructure
- Well-trained, creative and flexible human capital
- High productivity/wage ratio
- English language is widely used in business

Hungary has been traditionally one of the go-to investment destinations in Central & Eastern Europe (CEE) for US, Japanese and European companies for various reasons. It joined the EU in 2004 bringing with it a number of advantages in terms of a free trade system, movement of goods, services, capital and people. Ideally located, centrally in CEE, Hungary has a highly-qualified, multi-lingual work-force, well-developed infrastructure plus competitive corporate tax rates and incentives for companies.

In recent years, Hungary has focused on rebalancing the state budget and re-shaping labour and employment legislation to create a more flexible labour market. The Government's primary goals have been to reduce the level of state indebtedness and boost employment in Hungary.

New taxes have been introduced in certain service sectors, including energy, financial services, telecoms and retail. Concurrently, the level of certain social benefits, particularly pensions, has been reduced. Since January 1, 2017, the corporate income tax rate has been cut to 9%, currently the lowest rate in the EU.

The Government's defined goal is to attract international production companies and manufacturers to establish operations in Hungary. The success of this is illustrated by the opening of Mercedes-Benz's car assembly plant in Kecskemét in 2012 and Audi's significant expansion of its car plant in Győr.

The Government has also significantly opened up to China, India and Arabic countries to encourage inward investment into Hungary.

The Government is determined to attract foreign investors in all sectors, especially in the production and manufacturing sectors, with a variety of commercial incentives. This effort has proven to be fairly successful, as international companies are increasingly setting up in Hungary and realising numerous benefits that perhaps a number of Hungary's neighbours do not necessarily offer.

Although the imposition of new taxes in certain service sectors has led to a sharp decline in the volume of investments, this has been partially compensated for by the increasing investment activity in the production and manufacturing sectors in Hungary, particularly in the automotive sector.

Introduction

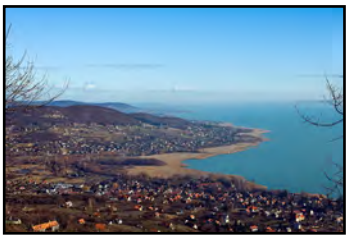
"Whatever man does he must do first in his mind."

—Albert Szent-Györgyi

An Overview of Hungary

Location	Central Europe
Area	93,030 km^2 (35,919 mi^2)
Population	9,599,744 (2023)
Life expectancy	75 years
Official language	Hungarian
Religion	Catholicism: 39%, Protestantism: 14.7%, Other: 1.1%, No religion: 18.2%
Literacy	98.7%
Capital	Budapest (1.75 million inhabitants)
Government	Republic
President of the Republic	Tamás Sulyok
Prime Minister	Viktor Orbán
Currency	Hungarian forint; abbreviations: Ft, HUF
Time zone	GMT + 1 (GMT + 2 from the last Sunday in March to the last Sunday in October)
Public holidays	January 1, Good Friday, Easter Monday, March 15, May 1, Whit Monday, August 20, October 23, November 1, December 25, 26
Climate	Continental with Mediterranean and Atlantic influences





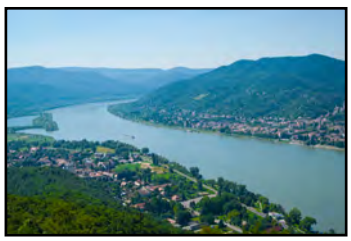
Geography

geographical features

Hungary is located in Central Europe surrounded by seven neighbouring countries and within easy reach of Western Europe. The majority of the landscape consists of plains and low mountains. The two largest rivers, the Danube and the Tisza, serve as navigable waterways. The largest lake in Central Europe, Lake Balaton, is located in Hungary. Lake Balaton is a popular holiday destination for both Hungarian residents and foreign tourists.

The capital of the country is Budapest, which is also the biggest city in Hungary. Budapest is divided into two parts by the river Danube. The Buda side is older and hillier, while the Pest side is the commercial centre of the city dotted with beautiful art nouveau buildings.

Hungary is located on the border of three climate zones. As a result, the country has a continental climate influenced by oceanic climate from the west, subarctic climate from the north and mediterranean climate from the south. Summers are typically sunny and warm and the general temperature is between 25–30 °C. For a few weeks, daytime temperatures may even reach around 35–38 °C. Winters are cold and the general temperature is between -10–0 °C. Springs and autumns are often really short and usually wet.



History

the highlights of more than 1000 years

To describe the history of a nation in a few sentence is impossible. However, by looking at the highlights of more than 1000 years of history we can deepen our understanding of Hungarians and Hungary.

After several hundred years of wandering, ancient Hungarians found a land of "flowing milk and honey" in the heart of Europe, in the Carpathian Basin. Under the leadership of the legendary chieftain Árpád, the seven tribes settled by the river Danube in 896. István, descendant of Árpád, was crowned the first Hungarian king with the Holy Crown, received from Pope Sylvester II. István centralised the royal authority and converted the country to Christianity and aiming it in a Western orientation. The Hungarian state was consolidated in the next century by the kings of the Árpád dynasty. The most famous written constitution was the "Golden Bull", which, similarly to the Magna Charta, declared the rights of noblemen and their relation to the king.

In the 13th century Genghis Khan's army, with hundreds of thousands of mounted soldiers, invaded the Carpathian Basin. Although the Tatars completely sacked the land, their continued invasion towards the west was halted. The restoration of the country was followed by two centuries of wealth and development. The borders of Hungary even extended to the Baltic Sea, Black Sea and Adriatic Sea. The Hungarian army resisted the forces of the Ottoman Empire and stopped the Turkish invasion. The court of king Mátyás was a centre of renaissance culture in Europe. He also established modern managerial practices to control the Hungarian economy.

36 years after the death of Mátyás, the Ottoman Empire conquered Buda, and 150 years of Turkish occupation began. Similar to the Tatars, the Turks were also halted in Hungary, which prevented them from invading Western Europe. In the 17th century the Habsburgs expelled the Turkish troops from Hungary and occupied the country.

The fight for freedom from the Ottoman Empire was replaced with the struggle for independence against the Habsburg Empire. As a climax of this struggle, a revolution broke out against the Austrian supremacy in 1848. The longest European revolution could only be suppressed one and half year later by the Habsburgs, with the intervention of the Russian army, followed by years of cruel and bloody revenge. Eighteen years later, a compromise between Hungary and Austria was signed, which led to the double-centred Austro-Hungarian monarchy. A new era of prosperity began: Budapest became a European metropolis, the first underground railway on the continent was built there and a spectacular industrial surge began.

World War I marked the end of the dual monarchy and the flourishing years of development. The treaty of Trianon in 1920 reduced the territory of Hungary by two thirds and the population by one third. Millions of Hungarians became minorities in the surrounding countries. This loss was and has remained one of Hungary's deepest national traumas.

In 1944, Hitler's troops occupied Hungary, and a year later the Soviet army "liberated" and occupied the country. In 1946, the monarchy was abolished and Hungary was declared a "democratic republic" governed by a communist regime under the power of the Soviet soldiers and guns.

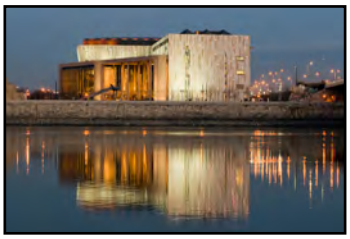
hundreds of Hungarians were executed and thousands more fled the country

The fight for freedom continued and led to the revolution of 1956 against the Soviet and communist oppression. The Soviet army crushed the revolution and reinstated the communist power. János Kádár became the puppet leader of Hungary with the Soviet Union behind the curtain. Hundreds of Hungarians were executed and thousands more fled the country.

The communist regime collapsed in 1989, and the last of the soviet troops left the country in 1991. A new era has begun in Hungary.







Economy

General Economic Information

Similar to other European countries, the structure of the Hungarian economy consists of three economic sectors: the agricultural sector, the industrial sector and the service sector.

Hungary's agricultural sector has a particularly favourable climate and geographic conditions. The agricultural sector accounts for approximately 3.8% of the country's GDP. Nearly 80% of the country's territory is suitable for agricultural production. Both the average number of sunny days and the quality of the soil are extremely high. Due to these favourable conditions, the quality and content of the Hungarian agricultural products are recognised worldwide for their superiority.

The agricultural, the industrial and the service sector.

The industrial sector represents about 22.6% of the country's GDP. According to the latest figures, the export-focused fields of the industrial sector have significantly expanded in the last few years. In line with these developments, the automotive, telecommunications and computer technology industries have seen significant growth, while food and other light industries, as well as the construction industry, have fallen back.

The service sector represents around 73.6% of GDP. Within this sector, private services (e.g. trade, tourism, finance and other economic services) are highly developed. Because of Hungary's ideal geographic location (see "**Geography**") the transportation sector is considered to be a core sector with important international transit traffic routes crossing the country.

In general, it is worth mentioning that the actual performance of the Hungarian economy is highly dependent on the EU's economy, especially on Germany's, since the majority of Hungarian exports (25%) are directed towards the German markets.

Current Economic Situation

Despite the Russian-Ukrainian war and the aftermath of the COVID-19 crisis slowing the dynamic growth of the Hungarian economy, numerous favourable developments have taken place over the past few years. See Table 1 below for a brief summary of the most important economic indicators for 2023 and the estimated indicators for 2024 and 2025.

recent economic trends in Hungary

In recent years, exports have become the engine of the economy. The automotive sector is now a Hungarian core industry, accounting for nearly 20% of exports. Indeed, Hungary is one of the most attractive countries for automotive investment in Europe. Four large automotive Original Equipment Manufacturers ("OEMs") have production activity in the country: Suzuki, Audi, GM and Daimler AG. In 2012, Audi AG - the most important automotive OEM in Hungary - began a huge investment project to increase production at its Győr plant. Audi also established an R&D centre in 2013 in addition to its car assembly plant. GM and Suzuki are also expanding their manufacturing capabilities. In 2012, Daimler AG began building class A and B Mercedes cars in its Kecskemét plant and by early 2016, more than 500,000 Mercedes cars had been produced. In 2016, Daimler AG announced two investment projects with a total value of EUR 1 billion - Daimler AG's investment is to be the largest-ever automotive invest- ment in Hungary, creating an additional 2,500 jobs. Daimler AG is building a new pressing plant at the Kecskemét site worth more than EUR 100 million. The con- struction of the 23,000m² new unit started operating in 2022. Daimler AG has invested EUR 141 million at its plant in Kecskemét to add fully electronic vehicles to the production range, and the first electric Mercedes-Benz vehicle was produced in October 2021.

In 2018, it was announced that another renowned automotive company will start production in Hungary. BMW launched its investment project in Debrecen with a total value of more than EUR 1 billion, creating 1,000 jobs. Whereas large multinational companies have invested and started production activities in Hungary, many equipment manufacturers and other suppliers have also settled in Hungary. Following in the tracks of the automotive industry, R&D and innovation are also playing a growing role. Currently, the two most important patterns of development in Hungary are the development of electromobility and autonomous cars.

The pharmaceutical business is a core part of Hungary's highly developed industrial base with a solid international reputation. The major players in this area include Richter Gedeon, Servier, TEVA, Sanofi and Bayer AG.

The performance of Hungarian tourism has set records every year between 2010 and 2019. Hungary's popularity as a tourist destination was on the rise both among domestic and international travellers. The well-known Hungarian hospitality, the country's special natural assets, its unique medicinal spas and lower prices have contributed to this growth trend. The number of guest nights spent in commercial accommodation has risen by 1.9% in 2023 compared to the previous year.

The Hungarian Investment Promotion Agency ("HIPA") consistently tries to attract direct foreign investments. HIPA continues to offer dozens of projects in various

industries including agriculture, manufacturing, real estate, green industry and innovation. Budapest has continued to rank amongst the top 10 most important European cities and for the first time, a smaller town, Debrecen has also reached the top 10 (in the category of smaller European cities of the future). Additionally, Central Hungary has also been recognised as an attractive investment location.

Prognosis for 2024

The Hungarian government is committed to fulfilling the government debt criteria as set out in the Maastricht Treaty. However, this has become a challenging task due to the aftermath of the COVID-19 pandemic, the effects of the Russian-Ukrainian war and the high rate of inflation.

According to the European Commission's Winter Forecast, in 2024, GDP growth is forecast to 2.4%.

As expected, the slowdown of economic growth already began in 2022 and Hungary's economy remained in recession in the first half of 2023. As the gradual economic recovery began in the second half of 2023, the central bank introduced a gradual reduction in the base policy rate from 13% to 10.75% alongside 2023. The inflation rate has decreased to 7.9%, as of November 2023.

The rate of unemployment increased by 0.4% compared to 2022 and stood at 4.1% by October 2023. In 2024, it is expected that unemployment will increase due to the approaching economic crisis.

Table 1. Hungarian Economic Forecast (percentage change on preceding year)

Description	2023	2024	2025
GDP, volume	-0.6	2.4	2.7
Private consumption expenditure (by volume)	-3.3	3.0	2.6
Exports of goods and services (by volume)	0.7	3.1	4.4
Imports of goods and services (by volume)	-4.4	2.3	5.1
Index of consumer prices	17.5	4.6	3.3
Unemployment rate	4.1	4.2	3.9

Data source: OECD Economic Forecast (November 2023)


Political Environment

General political environment

Enacted in 1949 and substantially amended in 1989 because of the democratic transition, the Constitution created the basis of the rule of law in Hungary. Consequently, parliamentary democracy was established in Hungary in 1990 and since then, the country has been politically stable. On 1 January 2012, a new Constitution ("Fundamental Law") entered into force that reflects both European and general international principles. Until the Fundamental Law entered into force, the official name of the country was the Republic of Hungary. On 1 January 2012, the official name of the country changed to Hungary; however, the form of government remained the same, i.e. a republic.

The highest body of popular representation is the unicameral Parliament made up of 199 Members of Parliament ("MP"). MPs are directly elected by the citizens every four years. The political structure is a multi-party system.

The Parliament elects the Prime Minister upon the recommendation of the President of the Republic. After his/her election, the Prime Minister forms the government. Government members are appointed by the President of the Republic upon the Prime Minister's proposal.

The President of the Republic is elected by the Parliament for a period of 5 years. The President is the guardian of democracy, who expresses the unity of the Hungarian nation. The role of the President is mostly representative, primarily with diplomatic duties, constitutional sanity checks on legislation passed and among other duties, the President also announces the date of the elections.

Due to the Russian-Ukrainian war, Hungary has been in a state of emergency since May 2022 (after ceasing the state of emergency period due to COVID-19 pandemic). In a state of emergency, the Fundamental Law authorises the Government to regulate Hungarian relations using governmental decrees. The Fundamental Law even gives the Government the power to amend and suspend Parliamentary acts. This has created a rapidly changing legal environment since the outbreak of the COVID-19 pandemic. The state of emergency is expected to be extended until 19 November 2024.

The Hungarian Judicial System

As in most countries, courts are authorised to settle civil, administrative, labour and criminal cases. Hungary has a four-level judicial system with the Curia (in Hungarian: Kúria, the Supreme Court) as the most authoritative.

District courts ("Járásbíróságok")

District courts constitute the courts of first instance in specific cases, e.g. disputes regarding intellectual property litigation. There are 113 district courts in Hungary (including the 23 districts of Budapest) that mostly settle minor civil and criminal cases. Litigating parties may appeal against the judgments of any court, from the district to the regional court.

Regional courts ("Törvényszékek")

Regional courts are part of the second level of the judicial system and play a double role. On one hand, regional courts are courts of second instance for appeals against the judgments of district courts. On the other hand, regional courts also constitute the general courts of first instance of the judicial system. In the former situation, the judgment of the regional court, as the court of second instance, is final and binding with no possibility to appeal, while in the latter case, litigating parties may appeal against the decision to the regional courts of appeal. There are 20 regional courts in Hungary - one in each of the 19 counties and the Metropolitan Court serving Budapest.

Regional courts have another important role - courts of registration operate at all of them. Their role is to register and supervise the operation of legal entities, e.g. companies, foundations, societies, etc. Companies are registered and deregistered (concluded) by these courts along with any changes to a company's corporate data.

Courts of Appeal ("Ítélőtáblák")

The 5 regional courts of appeal (founded in 2003 to reduce the workload of the Supreme Court) constitute the third level of the judicial system and act exclusively as the court of second instance in civil and criminal matters for decisions handed down in a regional court acting as the court of first instance. The decisions of the regional courts of appeal are always final and binding and not subject to an ordinary appeal.

Curia, the Supreme Court ("Kúria")

The Curia sits atop the Hungarian judicial system. It has a double role. On one hand, it is the competent court if an extraordinary challenge is lodged against the final decision of a court of second instance (a regional court or a regional court of appeal) in civil cases. In criminal cases, the Curia has a third instance role. In these cases, the

Curia may overrule a lower court's decision and may also command the lower court to restart proceedings. There is no appeal against the rulings of the Curia.

On the other hand, the Curia is responsible for the coherence of Hungarian court practice. It monitors the work of the lower courts and may issue binding decisions on certain legal questions that frequently come up in legal matters before the courts.

Court of Justice of the European Union ("Európai Unió Bírósága")

Although the Court of Justice of the European Union ("CJEU") is not part of the Hungarian judicial system, it plays an important role in and has an impact on the practice of the Hungarian courts. As a consequence of Hungary's EU membership, Hungarian law is subordinated to EU legislation in many aspects. If an EU legal principle is to be interpreted in a case before a Hungarian court, the court may (and the Curia must) turn to the CJEU for an authentic and binding interpretation, often called a "preliminary ruling". However, the CJEU will only give an interpretation of the specific legal principle as it has no authority to rule upon specific court cases.

This mechanism ensures the coherence of court practice both at national (Hungarian) and European levels.

Specialised courts ("Különös hatáskörű bíróságok") were abolished on 31 March 2020

Previously, the Administrative and Labour Courts were courts that specialised in public administration and labour law matters in the first instance. As of 1 April 2020, these specialised courts were abolished and the regional courts are now competent in the above matters in the first instance. The Budapest Metropolitan Court has exclusive jurisdiction in matters that previously belonged to the Administrative and Labour Courts in Budapest, e.g. visa matters. Appeals against the administrative decisions of the regional courts may be submitted to the Curia and appeals against labour law decisions to the regional courts of appeal.

Other entities in the Hungarian Justice System

Apart from the ordinary courts, notaries and arbitration courts may also proceed in civil cases.

Instead of filing a lawsuit, an order for a payment procedure may be requested at any notary public for civil claims up to HUF 3 million. Parties may agree on turning to arbitration courts.

The Hungarian Chamber of Commerce and Industry operates a permanent arbitration court whose jurisdiction is often set out in commercial contracts.

In both cases, decisions can be challenged before ordinary courts, although the arbitration award can be challenged only on a very narrow basis.

FAQ

1. Which court is the court of first instance for my case?

For minor cases, the district courts are competent in the first instance, whereas in major cases, it is the regional courts. In special labour law cases, the regional courts are also competent in the first instance. As a basic rule, territorial competence is decided upon the residence or seat of the defendant or upon the place of work in labour law cases.

2. Do I need the legal support of an attorney-at-law before the courts?

The general rule is that the presence of an attorney-at-law as a legal representative is mandatory only in procedures before the regional and higher courts (the regional courts of appeal and the Curia). However, clients are strongly advised to have legal support provided by an attorney-at-law in each court proceedings.

3. At which court do I need to register my company?

To register a company, the incorporation process must be started before the Court of Registration that operates within the organisation of the regional courts. It is important to note that it is mandatory to be represented by an attorney-at-law when establishing a company.



EU Membership and the Schengen Agreement

participation in the European integration

The relationship between Hungary and the European Union dates back to 1988, when Hungary was the first Central Eastern European country to establish diplomatic relations with the European Community. The Accession Treaty was concluded in 2003 in Athens and Hungary joined the EU on 1 May 2004. In January 2011, Hungary took over the EU presidency for half a year for the first time since the country joined the EU in 2004. The next time Hungary takes over the EU presidency will be for half a year in 2024.

In 1985, the dismantling of internal border controls started with the conclusion of the Schengen Agreement across the EU. As an EU member state, Hungary joined the Schengen Agreement on 21 December 2007, taking full responsibility for controlling EU borders. The Schengen Area now encompasses 27 countries as Croatia was admitted in December 2022.

The significance of joining the Schengen Agreement is that, on one hand, Schengen countries do not carry out border checks along their internal borders; on the other hand, they have established controls with clearly defined criteria along their external borders. Furthermore, Schengen countries have set up a common visa policy for short stays (for stays of up to three months) that is applied through "Schengen visas". Citizens of some non-EU countries are required to hold a visa to travel to the Schengen Area. A short-stay visa issued by one Schengen country entitles a holder to travel throughout the whole Schengen Area for up to three months within a six-month period. However, visas for visits exceeding this three-month period remain subject to national procedures.

It is expected that from mid-2025, citizens of other non-EU, visa-exempt countries (e.g. the UK, the USA, Canada and Australia) will be required to fill out the ETIAS online application form before travelling to the Schengen area. They will be able to enter the Schengen area when they have been notified about the ETIAS approval via e-mail. The success rate of the ETIAS application is expected to be more than 95%. More information about ETIAS can be found here: https://www.etias.info/application/.

The effects of Brexit

The United Kingdom left the EU on 31 January 2020 after 47 years of EU membership. The transition period between the EU and the UK ended on 31 December 2020. Since 1 January 2021, several changes have been executed regarding the relationship between EU counties and the UK. From that date, EU citizens may not travel freely to the UK. The British government's visa system has been introduced for EU citizens arriving in the UK, including for Hungarian citizens, except for visa-free entry for up to six months (e.g. tourism).

Note • Schengen cooperation enhances the free movement of persons by enabling citizens to cross internal borders of the Schengen Area without being subjected to border checks.

Useful Information about Hungary

Based on the rules of Hungarian orthography, the date structure is as follows: year/month/day, e.g. 2020/12/31. As far as written numbers are concerned, Hungarians use a comma as the decimal separator, e.g. 3,14 and a full stop (period) as the thousand separator, e.g. 1.234.567.

In Hungary, quantity, volume or size must be expressed using the metric system, e.g. kilograms, litres, m^2, m^3, etc.

In the Hungarian language, family names are followed by first names, e.g. Taylor John. Usually, business cards are presented in this manner unless they are prepared in English.

Hungary is situated in the Central European Time Zone (CET). Hungary uses the practice of daylight savings time, changing clocks by one hour on the last weekends of March and October.

Hungary's favourable location makes it a popular destination for foreign investors. Distances between Budapest and some major European cities:

- London, United Kingdom: 1450 km
- Paris, France: 1250 km
- Brussels, Belgium: 1130 km
- Vienna, Austria: 210 km
- Berlin, Germany: 690 km
- Prague, Czech Republic: 440 km

Useful Information about Business Practices

business practice and business etiquette tips

After the democratic transition, individualism moved more and more into the foreground. Hungarian business people have quickly adopted Western business styles and practices and they have become even more motivated by success. Young business people are expected to be well-educated, hardworking and able to work individually.

Respect and formality are key values in Hungarian business culture. In business relations, Hungarians do not call their partners by their first names until they are invited to do so by their partners. Status and hierarchy are important factors for Hungarians.

Relationships are very important in business life all over the world. Additionally, having an extensive network and valuable relationships are essential to being successful in the Hungarian business environment. Hungarians prefer to negotiate and conduct business personally. Since business is quite relationship-oriented, it is advisable to spend some time with Hungarian counterparts and earn their trust before commencing negotiations.

Hungarians are quite cautious in business negotiations. They prefer to pay attention to and review all the details and aspects of the deal; therefore, the negotiation procedure may be time-consuming. Meeting deadlines is a crucial requirement in Hungarian business culture. Hungarians are expected to work overtime to keep deadlines and they expect the same attitude from their counterparts. During negotiations, Hungarians are not reluctant to interrupt or argue if they feel it is necessary to arrive at the best solution. Such behaviour is normal in Hungarian business life and should not be taken personally. When drafting contracts, Hungarians prefer precise and clear wording.

Business Etiquette

business practice and business etiquette tips

- Punctuality in terms of meetings and appointments is one of the most important requirements in Hungarian business culture. Hungarians are usually on time or even arrive early for meetings and they expect the same punctuality from their business partners as well. If you are late, always make sure to inform your Hungarian counterpart about your delay in time. Never cancel a meeting at the last minute because it is considered to be a sign of disrespect in Hungarian culture.
- Avoid organising meetings during July and August as these are the main holiday months.
- The business dress code is conservative in Hungary. At meetings, men usually wear a dark suit with a tie, while women wear a women's suit or a dress. When doing business with a Hungarian counterpart, it is advisable to dress up formally and conservatively.
- Businessmen greet each other with a handshake. It is useful to take plenty of business cards for the first meeting and present them to all the participants of the meeting.
- Long business lunches and dinners and other social programmes are important parts of the negotiation process. Do accept these dinner and cultural invitations and take the opportunity to get to know your Hungarian business partners personally and establish a relationship as close as possible.
- It is not expected, but Hungarians do appreciate it if a foreign counterpart is familiar with Hungarian history and culture. You may impress your Hungarian partner by initiating a short conversation about Hungarian wines, composers (e.g. Liszt, Bartók) or scientists (e.g. Albert Szent-Györgyi).

- Avoid making a toast with beer glasses. After the suppression of the Hungarian revolution and the war of independence in 1848-49, the Habsburgs celebrated their victory by toasting with beer glasses. However, despite the historical ban on clinking beer glasses ending 150 years after the end of the Hungarian revolution and war of independence in 1999, the Hungarian cultural rule of toasting with beer glasses remains controversial.

Useful Links

some useful Hungarian websites in English

For your ease of reference, please find below some English websites providing further useful information about Hungary.

The Hungarian government

http://abouthungary.hu/

Consular Services

http://www.konzuliszolgalat.kormany.hu/en

The Hungarian Central Statistical Office

http://www.ksh.hu/?lang=en

The Central Bank of Hungary

https://www.mnb.hu/en/

The National Tax and Customs Administration

https://nav.gov.hu/en

The Budapest Business Journal

http://www.bbj.hu/

The Hungarian Investment Promotion Agency

http://hipa.hu/main

The National Directorate-General for Aliens Policing

http://www.bmbah.hu/index.php?lang=en



Establishing a Business Entity

"It is the future for which we must always work, not immediate pocketable momentary success."

—Zsigmond Móricz

(writer)

*This part depicts the aspects you should consider when deciding on the actual form and process of investing in Hungary (**How to Invest?**), and also presents the main forms of companies which can be established in Hungary (**Companies**). You can find in this part some practical information regarding the start of your business activity (**Setting up an Office**) and about the investments classified into different categories (**Branch Office and Commercial Representative Office, Mergers and Acquisitions, Real Estate**). In addition, this part shares some useful thoughts in the area of financial security in Hungary (**Financial Stability**) and also gives you an overview of special rules of investing in strictly regulated sectors like energy or telecommunication (**Strictly Regulated Sectors**).*

How to Invest?

In this chapter, we present the most important factors to consider when deciding on the form of your investment. The table on page 32 summarises some of the advantages and disadvantages of the relevant company types to help you decide which company type best suits your needs.

Setting up a business

Guidelines to Decide on the Form of the Investment

There are many aspects to consider when determining the actual form of the investment through which you aim to reach your business goals. It is also of utmost importance for an investor to always think a step ahead and choose the appropriate type of company that will best fit future business plans. Below, we provide you the most important aspects of this decision that need to be considered when choosing the form of an investment. You will find more specific descriptions (and, also, ways that VJT & Partners can assist you) in the chapters throughout this publication.

aspects to be considered when deciding on the form of investment

- **Owner's (shareholder's) liability**
  For an investor, an important question is the issue of the owner's (shareholder) liability for the debts of its company. In general, if the owner is subject to limited liability, it will not be liable for the company's unsettled obligations. However, if the owner's liability is unlimited, it will be liable for the unfulfilled obligations of the company (for more information, see "**Branch Office and Commercial Representative Office**" and "**Companies**").

- **Executive officer's (CEO's) liability**
  In principle, the company is liable for its CEO's acts towards third parties and the CEO is liable towards the company for the damage suffered by the company unless causing the damage was beyond the CEO's control, it was not foreseeable and the CEO could not have been expected to avoid the respective circumstance or prevent the damage. If the CEO intentionally caused the damage, the company or the CEO or both can be sued for compensation (the creditor can choose who to turn to for its claims) (for specific liability rules, see "**Financing Matters**").

- **Capital requirements**
  The amount of capital you wish to invest is a decisive factor regarding the type of company you choose. There are statutory minimum amounts or restrictions regarding the amount and type (i.e., cash or non-cash) of capital of companies to bear in mind when forming a company (for more information on this topic, see "**Branch Office and Commercial Representative Office**" and "**Companies**").

- **Foundation and operation costs, taxes**
  There are administrative fees regarding the foundation of certain types of companies (e.g. a company limited by shares, in Hungarian: zrt.), while the foundation of other types of companies (e.g., a limited liability company, in Hungarian: kft.) is free of charge in terms of administrative fees. The operation of the company also depends on a wide range of expenditures. Taxation generally does not depend on the actual type of the company; however, there are some cases, in which the type of the company matters, e.g., replacement tax schemes (for more information, see "**Branch Office and Commercial Representative Office**", "**Companies**"; "**Setting up an Office**", "**Strictly Regulated Sectors**" and "**Taxation**").

- **Foundation timelines**
  There are no big differences between the types of company regarding the time needed for establishment as far as registration processes are concerned. Of course, preparatory works for more complex structures may take more time. An administrative time-saving option (i.e., simplified registration) is available for most company types, at the expense of using standardised documentation and content (for more information, see "**Branch Office and Commercial Representative Office**" and "**Companies**").

- **Administrative duties (accounting and bookkeeping)**
  The burden of accounting, bookkeeping, payroll and similar duties depend more on the turnover and the number of employees in the business than on the type of the company. In general, administrative burdens increase as the structure becomes more complex (for more information, see "**Taxation**", "**Accounting**" and "**Auditing**").

Below, you will see a few advantages and disadvantages of the Hungarian company forms:

Form / type	Advantages	Disadvantages
Limited liability company (in Hungarian: kft.)	limited liability simplified registration available one owner suffices	the sale of ownership interest to a third person is restricted, unless the owners agree otherwise the equity must not fall to (or below) 50% of the registered capital or below the minimum registered capital
Private company limited by shares (in Hungarian: zrt.)	limited liability simplified registration available one owner suffices	costs and administrative burdens to issue and deal with shares the equity may not fall to (or below) 2/3 of the registered capital or below the minimum registered capital more strict rules for corporate governance

Form / type	Advantages	Disadvantages
Public company limited by shares (in Hungarian: nyrt.)	limited liability raising capital from the public	may only be transformed from a zrt. more administrative burdens relatively high registered capital requirement strict rules for trading with shares
General partnership (in Hungarian: kkt.)	simplified registration no minimum capital requirement	owners' unlimited liability for unsettled obligations at least two owners required
Limited partnership (in Hungarian: bt.)	simplified registration no minimum capital requirement	at least two owners required and at least one must bear unlimited liability for unpaid obligations
Branch office	may build confidence among creditors as it is an organisational unit of the parent company (rather than a separate entity) no need for minimum capital	the parent company has joint, several and unlimited liability for the branch office's obligations no simplified registration available
Representative office	may build confidence among creditors as it is an organisational unit of the parent company (rather than a separate entity) no need for minimum capital	unlimited direct liability for the representative office's obligations no simplified registration available
Sole proprietorship	not a statutory requirement to engage a lawyer to establish no need for minimum capital	unlimited liability for unpaid obligations

Investing in an operating business

Naturally, investing in an operating, already-existing business entity is also a feasible option which might better suit your needs or meet your expectations. For more information on various types of investment opportunities involving an already existing entity, please see "**Mergers & Acquisitions**".

Companies

*This chapter deals with the most common forms of Hungarian companies. Although there is no legal requirement to have a Hungarian owner or co-owner in a company, you should take into consideration that, currently, having a direct or indirect foreign stakeholder may have implications if your Hungarian company is involved in certain transactions (see "**Foreign Direct Investments**" for more details). For administrative and commercially practical reasons, our clients often choose to - and we generally advise them to establish a limited liability company ("kft.") or a private company limited by shares ("zrt."). For further details, please see our summary below.*

most important types of company in Hungary

Limited Liability Company (Hungarian abbreviation: "kft.")

Requirements

- Ownership requirements: a kft. may be set up by one or several members (quotaholders). There is no need for a Hungarian stakeholder.
- Capital: the statutory minimum amount of the registered capital is HUF 3 million (to be provided by a cash or non-cash contribution).
- •Liability: As a general rule, the exposure of the members for the unfulfilled obligations of a kft. is limited to their investment (capital contribution). This means that, in general, the members will not be liable for the unsettled debts of the company (i.e. in other words, forced to make additional payments on top of what they have already made). In exceptional cases, the corporate veil may be lifted- if the kft. is liquidated, a member may be held fully liable for all of the outstanding creditor's claims if the member (intentionally or grossly negligently) abused its limited liability.

Operation

Members' rights are represented by a "business quota" (in Hungarian: "üzletrész"). Unlike shares, business quotas do not materialize but they exist virtually, each member may have more than one business quota and a business quota may be owned by more than one member. Unless otherwise agreed by the members, if a member intends to sell its business quota to a third party (i.e. someone outside the kft.), each member, the company and a person appointed by the company - in this sequence - has a right of first refusal and may match the purchase offer and buy the business quota instead of the third party buyer. In general, members have liberty in including special rules in the company's Articles of Association, also in overruling most default statu-

tory provisions. It is important to emphasize that such liberty may only be exercised within the limits laid down by law; therefore, utmost attention should be paid when implementing derogations from the general rules.

The main decision-making body of a kft. is the members' meeting. Management is done by one or more managing director(s) (who do not act as a board) elected by the members' meeting. The members may also decide to establish other corporate bodies (e.g. an investors' board); however, the existence and operation of such other corporate bodies may not affect the competence and operation of the default, statutorily-determined decision-making bodies.

The kft. must apply double-entry bookkeeping requiring a qualified bookkeeper. A kft. must prepare its annual financial report in Hungarian.

The engagement of an auditor is not obligatory unless the average annual turnover of the last two business years exceeds HUF 300 million or the average annual number of employees employed by the kft. in the last two business years exceeds 50. The Accounting Act also lists certain circumstances where engaging an auditor is obligatory.

Court of Registration Procedure

fees and deadlines of registering the kft.

The application to register a kft. must be submitted by an attorney-at-law to the competent Court of Registration within 30 days of signing the Articles of Association. Some business activities (mainly in the financial sector) require a regulatory licence issued by the competent supervisory authority for the company foundation itself, in which case the registration must be applied for within 15 days of receiving the final and binding licence. In exceptional cases, the establishment must also be licenced by the FDI supervisory authority.

In an ordinary registration procedure (normally used when the members intend to use non-standard terms or bilingual corporate documentation), the court must register the kft. within 15 working days. The court also manages the issuance of the kft.'s tax number by forwarding the registration request to the tax authorities. If the owners or management are from outside Hungary, it takes the tax authorities several days to issue the tax number. Registration is free of charge.

A kft. may be registered through an expedited procedure where the owners give up their liberty in defining the terms of the Articles of Association by applying a standard form of Articles of Association determined by law. In turn, the court will register the kft. within 1 working day after issuing the kft.'s tax number. This form of registration is also free.

Private Company Limited by Shares (Hungarian abbreviation: "zrt.")

Requirements

establishment and other administrative criteria of a zrt.

- Ownership requirements: A zrt. is established through private offering of shares to a single or several shareholders.
- Capital: The statutory minimum registered capital is HUF 5 million.
- Liability: The shareholders' exposure for the unfulfilled obligations of a zrt. is limited to their investment. It means that, in general, the shareholders will not be liable for the unsettled debts of the company (i.e., in other words, they will not be forced to make additional payments for the zrt. on top of what they have already made). As with a kft., in exceptional cases, the corporate veil may be lifted if the zrt. is liquidated.

Operation

Shareholders rights correspond to the aggregate face value of the shares they hold. Preference shares securing extra rights for their owners (e.g,. voting or dividend preference shares) may also be issued.

The main decision-making body of a zrt. is the general meeting (of its shareholders). The zrt.'s management generally consists of a board of directors made up of a minimum of three members, but the shareholders may confer these powers to a single CEO instead of a board.

The zrt. must apply double-entry bookkeeping requiring a qualified bookkeeper. A zrt. must prepare its annual financial report in Hungarian.

The engagement of an auditor is not obligatory unless the average annual turnover of the last two business years exceeds HUF 300 million or the average annual number of employees employed by the zrt. in the last two business years exceeds 50. The Accounting Act also lists certain circumstances where engaging an auditor is obligatory.

Compared to a kft., a zrt.'s operation is stricter and provides less liberty to its shareholders and its officers in terms of corporate governance (i.e. rights attached to different types of shares are more strictly regulated).

Registration Procedure

fees and deadlines of registering a zrt.

The registration of a zrt. may be filed for when the shareholders have paid at least 25% of the issuance value of the shares. Any remaining cash contributions must be paid within 1 year from the zrt.'s registration.

The application to register a zrt. must be submitted by an attorney-at-law to a competent Court of Registration within 30 days of the signing of the Articles of Associa-

tion. Some business activities require a regulatory licence for the company foundation itself, in which case the registration must be applied for within 15 days of receiving the final and binding licence.

In an ordinary registration procedure (normally used when the shareholders intend to use non-standard terms), the court must register the zrt. within 15 working days. The court also manages the issuance of the zrt.'s tax number by forwarding the registration request to the tax authorities. If the owners or management are from outside Hungary, it takes the tax authorities several days to issue the tax number. The registration fee is HUF 100,000. In addition to the company registration procedure by the competent Court of Registration, a stock formation procedure must also be conducted with the involvement of the central security depository (currently, KELER Zrt.) and such procedure requires the shareholders to have a securities account.

A zrt. may also be registered through an expedited process where the owners give up their liberty in defining the terms of the Articles of Association. In turn, the court will register the zrt. within 1 working day after issuing the zrt.'s tax number. The registration fee for this form of registration is HUF 50,000.

Public Company Limited by Shares (Hungarian abbreviation: "nyrt.")

Requirements

establishment and other administrative criteria of a nyrt.

- Ownership requirements: A nyrt. must be first established as a zrt. and then transformed into its final nyrt. form through a public offering.
- Capital: The statutory minimum registered capital is HUF 20 million.
- Liability: The shareholders' exposure for the unfulfilled obligations of the nyrt. is limited to their investment. This means that the shareholders will not be forced to make additional payments for the nyrt. on top of what they have already made.

Operation

A nyrt.'s shares are traded publicly on the stock exchange.

Shareholders' rights correspond to the aggregate face value of the shares they hold. Preference shares securing extra rights for their owners (e.g. voting or dividend preference shares) may also be issued.

The main decision-making body of a nyrt. is the general meeting (of its shareholders). The management of a nyrt. is through a board of directors made up of at least 3 members. For a nyrt, there is no opportunity to appoint a CEO instead of a board.

A nyrt. must apply double-entry bookkeeping requiring a qualified bookkeeper. Engagement of an auditor is obligatory. A nyrt. must prepare its annual financial report in Hungarian. For further information regarding any tax-related issues, see "**Taxation**".

Registration procedure

establishment and other administrative criteria of a nyrt.

The registration of a nyrt. commences with filing for registration as a zrt. following the payment of at least 25% of the issuance value of the shares. Any remaining cash contributions must be paid within 1 year of the zrt.'s registration. Following registration as a zrt., the shareholders need to decide on whether to float on the stock exchange and if so, the zrt. may apply to register as a nyrt.

The application to register a nyrt. must be submitted by an attorney-at-law to the competent Court of Registration within 30 days from signing the Articles of Association. Some business activities require a regulatory license for the company foundation itself, in which case the registration must be applied for within 15 days of receiving the final and binding licence.

The transformation of a zrt. into a nyrt. may be registered within the course of a standard registration procedure only (no expedited process is available). The competent Court of Registration must register the nyrt. within 15 working days. The registration fee is HUF 500,000.

How can VJT & Partners help?

VJT & Partners, with its commercially focused approach, can help clients to find the company form that best suits their business plans. We can help in drafting and filing all of the company's corporate documents to the competent Court of Registration. Where necessary, VJT & Partners can also help you to apply for regulatory licences.

Company forms	Minimum number of owners	Minimum registered capital	Liability of owners	Auditor requirements	Registration
Limited Liability Company ("kft.")	1	HUF 3 million	Limited liability	2 years' average annual turnover > HUF 300 million OR 2 years' average annual employee no. > 50	None
Private Company Limited by Shares ("zrt.")	1	HUF 5 million	Limited liability	2 years' average annual turnover > HUF 300 million OR 2 years' average annual employee no. > 50	Standard: HUF 100,000 (+ HUF 5,000 publication fee) Expedited: HUF 50,000
Public Company Limited by Shares ("nyrt.")	several	HUF 20 million	Limited liability	Mandatory	HUF 500,000 (through transformation from an existing zrt.)

FAQ

1. What do articles of association (deeds of foundation) contain as a minimum?

As a minimum, the articles of association contain:

- the company name,
- the company's seat,
- the company's owners,
- the company's main and other business activities (corresponding to statistical codes),
- the registered capital and each owner's share together with payment terms,
- the representation/signing rules,
- the initial managing directors/board members, the auditor (if any) and supervisory board members (if any), and
- additional minimum content that specific company forms may require.

The Articles of Association with several owners typically also include matters reserved for the members / general meeting, special signing rights in key matters, and restrictions concerning the transfer of shareholdings.

2. Can a company commence any business activity before registration?

Once the application for registration is submitted, the company may commence business (except where such business activity is subject to regulatory licencing). Owners and managing directors / board members have enhanced liability for the company's obligations if registration is unsuccessful but business has been already done.

3. How long does registration take?

The length of time required for the registration of a company is not only influenced by court procedure deadlines, but is also very heavily influenced by foreign preparatory works. For example, signing and legalisation of foundation documents abroad and translation of certificates of incorporation of foreign owners can be time-consuming. Generally, setting up and registering a simple company with foreign owners or managing directors can take between 2-4 weeks if managed remotely.

Setting up an Office

Registering an official seat and opening a bank account for your company are unavoidable obligations for every new business entity. In this chapter, we will provide you with certain basic information about these processes.

Registered Office – Property required

A company wishing to be registered must have a physical address to use as its registered office. For registration, it is sufficient if the company declares its registered office to the competent Court of Registration. However, in this respect, the attorney at law (whose involvement is mandatory during the registration) must check the land registry (if an owned property is intended to be used for this purpose) or check the landlord's permission (if the office is to be leased).

Basic Requirements for a Registered Office

The address of the company's registered office also serves as the company's official mailing address. Business and official documents are to be received and kept there. A company signboard must also be put on public display near the entrance of the property. The registered office and the place of central administration may be at different locations. However, in this case, the place of central administration must also be listed in the company register.

The place of central administration may also be located outside Hungary. However, this could pose double taxation issues that may be managed by a double taxation relief mechanism (see "**Taxation**" for more detail).

Virtual Office

a virtual office can reduce operating costs

There are many options for reducing the initial operating costs of a business. One of them is to contract for virtual office services with a virtual office services provider. This option makes it possible that the company does not actually occupy unnecessary office space at high costs before expanding its business. A virtual office services provider (typically, accountants or accounting firms performing the company's bookkeeping) simply allows the use of its address as the company's registered office, and also handles the company's mailing and offer ad hoc access to meeting rooms. Law firms are not allowed to provide such services.

Rules of Purchase for Hungarian and EEA-resident Companies

Hungarian and EEA-resident companies may purchase or lease non-arable real property (e.g., an office or apartment) in Hungary without any restrictions (except the permission below).

Rules of Purchase for Foreign (Non-EEA-resident) Companies

purchase of real estate by foreigners

The purchase of non-arable, Hungarian real property by foreign (non-EEA resident) entities needs the permission of governmental authorities. The government office may deny permission, if the purchase is against either the public interest or the interest of the municipality. Typical denial cases could be, e.g., a compulsory strike-off or liquidation of the company, outstanding tax obligations, or other company tax number deletion cases. However, cases of denial based on these grounds are quite rare.

How can VJT & Partners help?

We provide our clients with all the information and legal assistance needed to use or acquire an office for company registration purposes. This might include support in the decision-making process in choosing the best available solutions, drafting and negotiating the necessary purchase or lease contracts, or assisting in obtaining other rights to use a real property as a registered office.

Opening a Bank Account for the Company

A company may open an operative bank account only after its tax number is generated and must open a bank account within 8 days from registration into the company registry. (See "**Branch Office and Commercial Representative Office**" and "**Companies**" for more information on how to register a company.)

Opening a bank account for companies with foreign owners/managing directors can be an administrative burden. According to the banks' business practice, the physical presence of the signatory is required and ultimate beneficial owners (basically, individuals with more than a 25% indirect ownership at the end of the ownership chain) will need to be identified usually by showing legalised copies of their passports.

How can VJT & Partners help?

VJT & Partners offers support in collecting the necessary documentation, as well as preparing everything to open a bank account with the preferred bank.

FAQ

1. Can I operate a business in Hungary without setting up a Hungarian company?

Under certain, strict conditions, you may do business in Hungary without establishing a domestic legal entity.

Furthermore, if your company is domiciled in an EU member state, with certain exceptions, you may provide cross-border services without establishing an entity in Hungary.

2. In which forms of undertaking may a foreign person do business in Hungary?

As a general rule, a foreign person may do business in Hungary in one of the following registered company forms:

- as an individual entrepreneur (if acting as an individual),
- by having a branch office or a commercial representative office registered with the Hungarian Court of Registration, or
- by holding shares (or business quotas) in a company domiciled in Hungary.

3. Can a foreign company also establish a business presence in Hungary via joint venture?

Foreign investors may establish a joint venture with Hungarian natural or legal en- tities by setting up any of the possible business entities. In a corporate joint venture, members may enter into a shareholders' (or 'quotaholders') agreement to regulate their corporate governance rights and obligations.

4. Can a foreign company also establish a business presence in Hungary by contracting with a Hungarian agent or distributor?

Foreign investors may enter into distribution or franchise agreements with Hungarian entities.

Under a distribution agreement, the distributor purchases the foreign investor's products and sells them on its own behalf. Under a franchise agreement, the foreign investor grants the franchisee certain rights of use and exploitation of assets protected by copyright or industrial property rights. Under such framework, the franchisee undertakes to produce and supply goods, services, or both through the use and exploitation of these assets. The franchisee acts on its own behalf.

A foreign investor may also appoint an agent to facilitate the conclusion of contracts with third parties.

5. Can companies relocate their registered office from another EU member state to Hungary while retaining their legal personality?

A foreign company may relocate its registered office from another EU member state to Hungary without losing its legal personality. This means that a foreign company, while retaining its legal personality, may transform into a domestic company without going into liquidation or winding up.

Branch Office and Commercial Representative Office

This chapter briefly introduces two additional forms of undertaking reserved only for foreign investors who wish to establish and pursue business activities in Hungary without setting up a local entity that is formally independent of their parent companies.

Branch Office

A branch office is not a separate entity but an organisational unit of a foreign company, through which the foreign company pursues a business activity in Hungary. The branch office operates under its own name but on behalf of the foreign parent company. Unlike the general concepts of limited or unlimited liability of the stakeholder(s) for a company's obligations, the parent company is jointly and severally liable with the branch office for the branch office's obligations (the creditor can choose who to turn to for its claims). The parent company has a general obligation to continuously ensure that the branch office has the funds necessary to manage and pay its debts.

As the branch office is only an organisational unit of a foreign parent company, it cannot transform into, demerge from or merge with another company. If businesses need to be merged, this must be done through an asset deal (i.e., transfer of the business (i.e. each and every asset) from the branch office to another company).

Establishment

No registered capital is required but the parent company must provide the capital necessary for the operation of the branch office.

requirements of establishing a branch office

The application to register a branch office must be submitted by an attorney-at-law to the competent Court of Registration within 30 days of the deed being executed. If an official licence is necessary to establish the respective branch office, the license by the competent authority must be attached to the application. In this case, the registration application must be submitted to the court within 15 days of the branch office receiving its licence. Based on the application filed, the court will obtain a tax number from the tax authorities. The court must register the branch office within 15 working days after obtaining the tax number. The registration fee is HUF 50,000.

Operation

The branch office must be registered with the competent Court of Registration before commencing its business activities. The branch office may pursue all types of business activity except for representing its parent company, i.e. the branch office may

business activities may be pursued by a branch office

not act as an agent. In certain regulated industries, foreign companies registered and licensed in the European Economic Area ("EEA") are allowed to do business in Hungary through their branch office without possessing a separate license for the Hungarian market. Branch offices have limited possibilities in terms of receiving state aid and can only apply if expressly allowed by law.

Engaging an auditor is mandatory, except if the parent company is registered within the EEA. The foreign parent company is subject to Hungarian taxes regarding its branch office's business activities in Hungary. The branch office is subject to Hungarian accounting laws and the foreign parent company must publish its annual financial statements in Hungary.

Commercial Representative Office

A commercial representative office is also an organisational unit of its foreign parent company that only performs commercial representation and marketing activity for its parent company. The parent company is directly liable for all the obligations of the commercial representative office.

Similar to the branch office, the commercial representative office itself cannot demerge, transform into or merge with another company.

Establishment

requirements of establishing a commercial representative office

No registered capital is required but the foreign parent company must provide the capital necessary for the operation of the commercial representative office.

The application to register a commercial representative office must be submitted by a lawyer to the competent Court of Registration within 30 days of the execution of the deed of foundation. If an official licence is necessary to establish the respective commercial representative office, the licence must be attached to the application. In this case, the registration application must be submitted to the court within 15 days of the receipt of the licence by the commercial representative office.

Based on the application, the court will obtain a tax number from the tax authorities. The court must register the commercial representative office within 15 working days of obtaining the tax number. The registration fee is HUF 50,000.

Operation

operation and activities of a commercial representative office

The commercial representative office may only start its business activities after its registration with the competent Court of Registration. As its name suggests, the commercial representative office undertakes commercial representation for its foreign parent company. Commercial representation includes arranging agreements between its parent company and business partners, as well as providing marketing and advertising services for its parent company.

The commercial representative office has no obligation to engage an auditor. The foreign parent company is subject to Hungarian taxes regarding its commercial representative office's business activities in Hungary. Unlike the branch office, the foreign parent company's annual financial statements do not need to be published in Hungary.

The Difference Between the Branch Office and the Commercial Representative Office

main distinguishing features between the branch office and the commercial representative office

The main difference between the branch office and the commercial representative office is that while the branch office pursues business activities under its own name but on behalf of its foreign parent company, the commercial representative office cannot pursue any business activity under its own name. Further, while the branch office and its foreign parent company bear joint, several and unlimited liability for the branch office's obligations, the foreign parent company of the commercial representative office is directly responsible for all the liabilities of the commercial representative office.

How can VJT & Partners help clients?

VJT & Partners can draft and file all corporate documents necessary to register a branch office or commercial representative office with the competent Court of Registration and can provide support in obtaining any licences that may be necessary for establishment.

Form	Minimum registered capital	Liability of owners	Auditor	Registration fees	Business activity restrictions
Branch Office	none	joint, several and unlimited liability of the parent company and the branch office	mandatory (except if the parent company's registered office is in the EEA)	HUF 50,000 (+ HUF 5,000 publication fee)	No representation / agency activity on behalf of the parent company
Commercial Representative Office	none	direct, unlimited liability of the parent company	N/A	HUF 50,000 (+ HUF 5,000 publication fee)	Only commercial representation / marketing activity for the parent company

FAQ

1. How can I transform a branch office / commercial representative office into another form of undertaking?

Direct transformation is not possible. If the parent company aims to change the form of its undertaking in Hungary, it needs to set up the desired company form, transfer the business (assets, contracts, etc.) from the branch office / commercial representative office to the newly established company and then terminate the branch office / commercial representative office.

2. Can a branch office / commercial representative office be an owner of a Hungarian company?

No.

Mergers & Acquisitions

This chapter highlights the key points of a merger and acquisition ("M&A") transaction from a Hungarian perspective. This includes the general principles for M&A transactions and a description of the usual processes and parties' obligations.

Benefits and Forms of M&A Transactions

Mergers and acquisitions are both actions through which companies seek economies of scale, efficiency and enhanced market visibility. M&As include all manners of company stake or asset-related transactions, e.g.:

- national and cross-border transactions,
- asset and share deals,
- leveraged buyouts,
- equity investments, and
- public and private deals.

In practice, company acquisitions are much more likely to be share deals than asset deals. In a share deal, the investor acquires part or all of the target company (the shareholding in it) itself with all the contracts and licences as well as all the (tax and other) liabilities. In an asset deal, the investor acquires only selected assets or business lines of the company without the company's liabilities in general.

General Process of an M&A Transaction

An M&A transaction frequently starts by signing a letter of intent or a term sheet, each setting out the key commercial terms, target dates and principles, along which the parties will continue their negotiations. It may or may not grant exclusivity for negotiations to the potential buyer for a certain period.

This is usually followed by a legal/financial/environmental/technical, etc. due diligence performed by the buyer to identify the risks that may negatively affect or in extreme cases, hinder the transaction or the target's future business prospects. The end product of the due diligence, the due diligence report, also serves as a basis to negotiate and draft the transaction documents (the sale and purchase agreement in the first place) highlighting the issues to be covered from a legal perspective.

The signing of the transaction agreement(s), payment of the purchase price and acquisition of the ownership may take place on the same day. But this is often not the case, the buyer might set pre-conditions ("conditions precedent") for the seller to fulfil before actually buying the target. In these cases, the signing and payment of the purchase price/acquisition ("closing") take place on different days.

It may also occur that, due to the non-fulfilment of certain conditions precedent critical to the buyer, although the transaction agreement is signed, closing never takes place and the parties withdraw from the transaction. It is not uncommon that the purchase price is not paid in a single instalment - the buyer may withhold a percentage to cover certain risks within a certain period or the parties may agree that a purchase price adjustment is payable based on the target's performance after the change in ownership.

Typical Mandatory Obligations for a Buyer in an M&A Transaction

Notification of Acquiring a Supermajority

If, as a result of the transaction, the buyer directly or indirectly acquires at least 75% of the votes (a supermajority influence) in the target company, the buyer needs to report such acquisition of influence to the Court of Registration within 15 days from the acquisition.

Within 60 days from the publication of this supermajority, any minority member/shareholder may request the buyer to purchase its quota/shares at market value but for not less than the amount of the target company's own equity corresponding to such minority quota/shares.

Public Takeover Bid

If the bidder intends to acquire more than 33% of the shares in a public company limited by shares (in Hungarian, the abbreviated form of this type of company is "nyrt.") (or more than 25% if there is no shareholder in the target company with more than 10% of the votes other than the bidder) a public takeover bid must be made first.

This bid must be pre-approved by the Central Bank of Hungary.

If the bidder becomes a holder of at least 90% of the votes within 3 months following the acquisition and proves to have the funds to acquire all remaining shares, then the bidder may purchase all remaining shares in the target company even against the remaining shareholders' will (if this intention was indicated when making the takeover bid).

However, the same option is available to the minority shareholders - if 90% or more of the votes were acquired, the remaining shareholders may request the majority shareholder to purchase their shares.

Other Obligations

If a business is sold as a going concern, the whole company or part of the company's business (i.e. assets instead of shares), the seller (or if so agreed, the buyer) must inform the employee's representatives of the sale, its target date and any potential changes that concern the employees (see "**Transfer of an Undertaking**").

The Hungarian Competition Authority's pre-approval might also be required for an M&A transaction, depending on its magnitude based on the combined turnover data (see "**Competition Law**" for the detailed rules of merger control).

For a foreign investment, an M&A transaction may also be subject to national security screening relating to certain sectors of national security interest (see "**National security screening of foreign investments**").

How can VJT & Partners support an M&A transaction?

Due to the complexity of an M&A transaction and the frequently changing regulations that may affect it, it is necessary to consult a top-end law firm. VJT & Partners can help clients at all stages of an M&A deal, e.g. running and coordinating the due diligence, negotiating and drafting the letter of intent and the transaction agreements, supporting the signing and fulfilment of conditions precedent and holding the retained purchase price in escrow or managing post-closing matters. As we deal with M&A matters on a daily basis, we have considerable experience in international and domestic M&A transactions. We also dedicate our resources to understanding both our clients' intentions and concerns and to proposing suitable solutions.

FAQ

1. What is the difference between a "share deal" and an "asset deal"?

A share deal means that the buyer purchases shares in the target company holding the desired assets or business from the target company's owner(s). In practical terms, the buyer becomes the owner of the company with all its assets, contracts and liabilities without cherry-picking.

In an asset deal, the buyer directly purchases the desired assets, contracts or business from the company that enables the buyer to select the assets (real property, machines, intellectual property, etc.) and liabilities it needs only and avoid those it is not interested in taking over. Tax and regulatory (licensing) considerations, the magnitude of the target's liabilities and ownership relations may all have an influence on which path to choose.

2. What is a letter of intent?

A letter of intent is often used in M&A transactions to acknowledge the fact that the deal is being seriously considered. It is a document that outlines a common understanding between two or more parties of the key business terms and transaction principles before engaging in the more time-consuming part of the transaction preparation. Although it is usually not binding on the parties, i.e. the parties will not be forced to enter into the transaction, it frequently contains some provisions that bind the parties, e.g. conducting exclusive negotiations within a certain timeframe or confidentiality undertakings regarding the information shared to prepare for the transaction.

3. What is a disclosure letter?

One of the buyer's main goals in an M&A transaction is to minimise/cover the unforeseen negative impacts on the purchased business. On the other hand, the seller's intention is to sleep well after the purchase price is paid and the business is sold. The disclosure letter is to protect the seller from claims (typically warranty claims) brought against the seller from problems arising after the deal is closed, insofar that no claims will be successful that are based on the information disclosed in the disclosure letter.

4. What are warranties?

In the M&A context, warranties are contractual promises made by the seller in the sale and purchase (transaction) agreement confirming that certain assumptions (on which the purchase price offer was based) regarding the target business are correct (e.g. the target is not in breach of its contracts). If these statements turn out to be untrue (e.g. the target company is in breach of contract and its partner has a claim against the target company) this can materially influence the value of the business the buyer has purchased. The corresponding warranty provision may create legal grounds for the buyer to seek compensation for the negative financial effects.

5. What is due diligence?

Due diligence is an audit process through which a potential buyer collects information about the target company it intends to acquire and serves to identify the risks associated with the target company and to enable the buyer to give an informed purchase price offer. The process can include, among others, a review of the financial, legal, tax, technical or environmental records of the target company and generally, anything material that may influence the buyer's willingness to buy or pay the purchase price.

Real Estate

This chapter highlights the main points of Hungarian real estate regulation and some insights from an investor's perspective.

Real property information / formalities

The land registry system deals with all relevant legal information about real property located in the territory of Hungary (e.g. the name of the current and for- mer owners, encumbrances, execution rights, usage rights and easements). The infor- mation regarding the status of the real property found on the registry system is public, up-to-date and online to ensure easy access.

Any agreements concerning the registered rights (creation, modification or termination of ownership, usufruct, right of use, easement, right of purchase, right of sale, mortgage, building right) concerning a real property in the Land Registry must be made in writing, countersigned by a Hungarian attorney at law, notary or legal counsel registered by the Bar Association, and filed with the Land Registry authority to update the registry system.

A new land registry law will be enacted

On 1 October 2024, a new land registry law will come into force which will fundamentally change the procedure within the land registry system. From that day, the land registry procedure will be fully electronic instead of the present paper-based system. All documents and applications can be filed to the Land Registry Office via an online form. The new legislation will also allow attorneys to draw up real estate-related agreements as an electronic document with digital signatures and online authentication.

Ownership of real property / restrictions

Transferring the ownership of a real property requires the new owner to register with the Land Registry.

The acquisition of agricultural land in Hungary is restricted. Third-country nationals (non-Hungarian and non-EU/EEA citizens) and legal entities whether within or outside the EU (with very few exceptions) may not acquire ownership of agricultural lands.

EU/EEA citizens and legal entities domiciled within the EU/EEA may otherwise ac- quire non-agricultural real property without restriction. The acquisition of real

property by third-country nationals and third-country legal entities is subject to the prior permission of the competent government office (kormányhivatal).

In general, the land and the buildings located on the land belong, by default, to the owner of the land. Parties may agree differently and provide that the building and the land beneath are owned by separate owners.

The acquisition (and lease) of state or municipality-owned real estate is generally subject to tender. Various statutory pre-emption rights might also need to be observed when purchasing real property.

Lease of business premises

Lease agreements require fewer formalities than sale and purchase agreements (e.g. only apartment lease agreements must be in writing); also, filing with the Land Registry is not required. There is one type of business lease in Hungary. Apart from the cost per square meter, the most heavily-negotiated terms of business lease agreements are the term (typically a defined term), break and extension options, indexation, fit-out, maintenance and repair obligations (i.e. what is included in the rent or maintenance fee) and guarantees. A change of the real property's owner, unless otherwise agreed upon by the parties, has no impact on the lease agreement.

Construction Law Regulations

Zoning law / classifications

The zoning plan both:

(i) describes the permitted use of the land within the boundaries of the municipality, and

(ii) provides for the key specifications of developments and buildings, etc.

The zoning plan is made by the local municipalities and is resolved by its general assembly. No construction or development against the zoning plan may be carried out. Therefore, developments in these "zones" might require modifications to the zoning plan; this is subject to the decision of the municipality's general assembly.

Developments on agricultural land also require the reclassification of the specific real property by the Land Registry office and must be supported by a binding building permit.

These decisions may be challenged before the competent court by various persons concerned by the decision (e.g. neighbours).

Construction authority procedures

The building permit process is now electronic and the authority is now more supportive than before. A developer may officially ask the building authority's support staff to run a pre-check on documentation waiting to be filed to identify who might be the persons concerned by the process (this is of relevance from the appeal perspective), and generally, to find out information about the permit procedure.

Building permit

To start construction works, the developer must apply for a building permit. The construction works may be started based on a final and binding building permit issued by the competent government office. Several persons might have a legal interest in the building permit (e.g. neighbours) and may challenge the decision before the competent court.

Occupancy permit

After completing construction works, an occupancy permit is needed to use the building. The authority issues the occupancy permit if the building is suitable for use and the construction was completed in accordance with the building permit.

Other construction matters

Depending on the real estate's location, the construction must also comply with the townscape requirements of the municipality, where applicable.

The development of retail real properties in excess of 400m² is subject to special procedures and requires special approval from the appropriate governmental office (which also includes the judgment of the relevant ministries).

Archaeological or environmental works (including the clearing of unexploded munitions) might be necessary to prepare the site, possibly causing significant costs and delays in the construction process. Additional roads might need to be constructed as part of the development; this is subject to a separate road-building permit process. Securing a certain number of parking spaces might also be mandatory.

If the value of the construction crosses a certain threshold (approx. EUR 5.5 million), a project fund manager must be engaged in the construction process, managing the funds of the construction costs to secure due payment of subcontractors.

Operating Regulations

Licencing / reporting commercial activity

Certain special commercial activities require an operating permit (e.g. the sale of weapons, ammunition, explosives and explosive devices, gas sprays, pyrotechnic products); otherwise, starting commercial activity is subject to notification to the appropriate commercial authority.

Site permit

Certain commercial activities, e.g. metal fabrication or engine production, require a site permit unless the activities are subject to environmental licencing or operation permits (see above).

How can VJT & Partners help?

VJT & Partners can support you across a wide variety of real estate transactions, including the acquisition and leasing of retail, office, industrial space as well as property owned by individuals.

FAQ

1. Can foreigners own real estate in Hungary?

The acquisition of agricultural land in Hungary is restricted. Third-country nationals (non-Hungarian and non-EU/EEA citizens) and legal entities from either inside or outside the EU (with very few exceptions) may not acquire ownership of agricultural lands.

EU/EEA citizens and legal entities domiciled with the EU/EEA may otherwise acquire non-agricultural real property without restriction. The acquisition of real property by third-country nationals and third-country legal entities is subject to the prior permission of the appropriate government office (kormányhivatal).

2. Do I need a lawyer to buy a property?

Any agreements relating to the registered rights of a real property in the Land Registry (e.g. the transfer of ownership or an encumbrance) must be in writing, countersigned by a Hungarian attorney at law and be filed with the Land Registry authority to update the registry system.

3. What other costs are associated with buying real estate?

In general, the buyer must pay the statutory duty and registration fees at the Land Registry and the costs of acquiring the certificate of title; the seller must pay taxes and the costs of the energy certificate. Additional expenses may arise with the establishment or termination of credit, mortgage or other encumbrances and insurances.

Financial Stability

This chapter aims to provide you with a brief overview of certain foreign exchange and financial regulatory characteristics due to Hungary not yet being a member of the Eurozone.

Exchange Control in Hungary

no foreign exchange restrictions

Despite Hungary currently being outside the Eurozone, it needs to be stressed that investors face no greater risk in Hungary than in any other EU Member State. No foreign exchange restrictions exist and capital flows freely. Transactions in foreign currencies can be made freely and the Hungarian Forint (HUF) is fully convertible.

The Central Bank of Hungary

the role of the CBH/MNB

The Central Bank of Hungary (in Hungarian: Magyar Nemzeti Bank; "CBH/MNB") is responsible for supervising the financial intermediary system, setting the base interest rate, setting and publishing official exchange rates, preserving the stability of the financial system and ensuring the external stability of the Hungarian economy. The Government agrees decisions about the exchange rate system with the MNB. The MNB must be independent of the Government and the institutions of the European Union, except the European Central Bank (for more information about the MNB see "**Financial Industry**").

Supervision of Financial Institutions

The MNB is responsible for the supervision of financial institutions, e.g. banks, insurance companies, etc. and generally has a wide scope of competence regarding the financial stability of Hungary via its Financial Stability Council.

FAQ

1. Do I face any special risks arising from the fact that Hungary is not a member of the Eurozone?

No. Although Hungary is not a member of the Eurozone, the CBH/MNB ensures the financial stability of Hungary and the external stability of the

Hungarian economy. Therefore, you do not face bigger risks when investing in Hungary when compared to any other EU Member State.

2. Can I face any restrictive exchange control measures?

No. The HUF is fully convertible and the government has no power to restrict or suspend this convertibility.

Strictly Regulated Sectors

Every form of company in Hungary needs to be registered. However, in certain cases, the founding of a company is also subject to special sector-based foundation licences. This means that certain companies may only apply for registration with the Court of Registration if a foundation licence has already been obtained. In other cases, already existing and registered companies may only pursue business activities subject to a special sector-based business licence. These rules apply to industries with detailed sector-specific rules where specific regulatory authorities are entitled to control, authorise and even regulate the given industry. Apart from licencing, companies in these industries need to comply with sector-specific statutory rules or report certain fields of their activities to the competent Hungarian authority. In addition, in these industries certain transactions need to be acknowledged or approved by the given regulator.

In this section, we give a brief practical insight into some of the main strictly-regulated sectors (i.e. the financial, energy, telecommunication and pharmaceutical sectors), particularly in terms of the key compliance regulations, competent regulatory authorities and licences.

The Financial Industry

sector-based regulations apply to almost all types of participants in the financial industry

The regulatory regime of the Hungarian financial system is diverse; meaning that in line with several EU directives, a special sector-specific regime applies to nearly all types of market participants. Generally speaking, all financial market participants must comply with the sector-specific regulations, apply for licences and report on certain fields of their activity to the Central Bank of Hungary ("CBH/MNB"). Moreover, it is common for all market participants that they may only be founded in the corporate form that is set out by the relevant sector-specific regime. In this context, it is to be noted that the sector-specific regulations prescribe special minimum capital requirements for these corporate forms.

The CBH/MNB is the main regulator of the financial industry. It primarily supervises the financial markets, grants licences and imposes sanctions for non-compliance with sectoral rules. The main fields of the financial sector are the banking, insurance and capital markets.

Our FAQ contains more information about both the detailed rules of corporate forms, the minimum capital requirements and CBH/MNB licencing/authorisation proceedings.

Banking Market

The main regulator of the banking market is the CBH/MNB. It is primarily responsible for the licencing / authorisation and supervision of compliance with prudential rules (e.g. capital adequacy and risk management) and fair market behaviour of banking market participants.

The primary governing law is Act CCXXXVII of 2013 on Credit Institutions and Financial Enterprises ("CIFE Act") that provides rules for the licencing, reporting, ownership and corporate structure, corporate governance, management requirements, prudential rules, customer protection, registry, audit, accounting and supervision of the banking market. Under the CIFE Act, a financial institution may operate in the form of:

- a credit institution, i.e. a bank, a specialised credit institution or a cooperative credit institution (in the form of savings or credit cooperatives), or
- a financial enterprise, i.e. a financial institution authorised to perform one or more financial service set out by the CIFE Act, a financial holding company or payment clearing houses.

In general, both types of financial institutions may pursue all types of banking services set out in the CIFE Act; however, only a credit institution is authorised to collect deposits and provide currency exchange services.

Further, financial institutions may not pursue money transmission services or the issuance of electronic money.

Licences / authorisations issued by the CBH/MNB

Credit institutions are subject to two-tier licencing. Both a foundation licence and a business licence must be obtained - we go into more detail about two-tier licencing in our FAQ. For financial enterprises, only a foundation licence is required.

the two-tier authorisation of credit institutions

For credit institutions, apart from the foundation licence and business licence, the CBH/MNB's authorisation is also required for:

- transformation, merger and demerger,
- amendment of the deed of foundation,
- acquisition of a qualified interest in a credit institution,
- election or appointment of executive officers,
- commencement of operation,
- amendment of the scope of business activities,
- carrying on financial services business through the use of a prime intermediary or multiple prime intermediaries,
- establishment of a commercial representative office, branch office, subsidiary (credit institution, financial enterprise or other enterprise) in a third country,
- acquisition of a qualified interest in a non-resident company,
- transferring deposits and contracts for the repayment of funds,
- termination of operation, and
- collateral valuation policy.

For financial enterprises, apart from a foundation licence, the CBH/MNB's authorisation is also required for:

- merger, demerger and transformation,
- amendment of the scope of business activities,
- appointment of executive officers, acquisition of a qualified interest in a financial enterprise,
- carrying on its financial services business through the use of a prime intermediary or multiple prime intermediaries, and
- termination of its operation.

For financial enterprises, apart from the foundation licence, the CBH/MNB's authorisation is also required regarding:

- merger, demerger and transformation,
- amending its scope of activities,
- appointing its executive officers,
- acquiring a qualified interest in a financial enterprise,
- carrying on its financial services business through the use of a prime intermediary or multiple prime intermediaries, and
- terminating its operation.

The Insurance Market

The insurance market is supervised by the CBH/MNB. The key legislation is Act LXXXVIII of 2014 on Insurance Business ("Insurance Act"), providing rules for the licencing, reporting, corporate structure, management, investment, insurance products, operation, registry, audit and accounting, customer protection and super- vision of the insurance and reinsurance market. The Insurance Act is the implementation of the Solvency Directive into the Hungarian legal system.

Licences / authorisations issued by the CBH/MNB

two-tier authorisation of insurance companies

Insurance and reinsurance activities are subject to two-tier licencing, i.e. both a foundation and a business licence must be obtained.

Further key matters, for which CBH/MNB's authorisation is required, are the following:

- commencement of business activities involved in or closely related to insurance or reinsurance,
- termination of insurance or reinsurance activities,
- any change in insurance or reinsurance activities,
- transfer of an insurance or reinsurance portfolio,
- transformation, merger and demerger,
- acquisition of a qualified interest in an insurance or reinsurance company (either as a company limited by shares or as a cooperative),

- foundation or acquisition of shares in a third-country (non-EU resident) insurance or reinsurance company and establishment of a branch in a third country,
- employment, assignment, appointment or election of a manager or other senior manager and
- employment or engagement of a managing agent.

The Capital Market

The Hungarian capital markets are also supervised by the CBH/MNB. The primary legislation governing this activity is Act CXX of 2001 on the Capital Market that provides rules for the production, issuance and conversion of, as well as trading with, securi- ties, acquisition of influence in public limited companies, prohibition of insider trad- ing and market manipulation, protection of investors, regulation of the stock exchange, clearing and central depository operations, authorisation and supervision. Certain capital market participants, e.g. investment service providers, commodity exchange service providers, managers of investment funds and depositaries are regulated by separate acts.

The Budapest Stock Exchange

The Budapest Stock Exchange ("BSE/BÉT") is where trading of publicly-issued securities takes place. It is a self-governed organisation that provides conditions of trading, rights and obligations of traders and issuers and conditions of membership. The BSE/BÉT also has certain supervisory powers. Namely, officers designated in the BSE/BÉT's by-laws may suspend the trading of certain financial instruments.

trading of publicly issued securities

Investment services

The provision of investment services is subject to one-tier licencing of the CBH/MNB as only a business licence needs to be obtained.

Hungarian law allows for investment service providers to provide a full range of investment services including placement and underwriting, trading, agency activities, portfolio management and custodian services for all types of financial instruments. Here, it is to be noted that the traditional separation of the banking and capital markets is not completely clear, given that credit institutions may also provide a full range of investment services under their licences. We go into more detail about the universal banking licence in our FAQ. However, this does not apply vice versa as investment firms cannot pursue banking services. To comply with the Markets and Financial Instruments Directive, Hungarian law places special emphasis on the protection of investors; thus, investment service providers are subject to strict rules of authorisation and disclosure.

Investment Fund Management

Investment fund management as a complex market scheme typically has at least three participants: investment funds, investment fund management companies (fund

managers) and depositaries.

Investment funds are legal entities established and operated under the principles of risk diversification by fund managers who must invest the capital received from investors on behalf of and for the benefit of investors. Investment funds may be categorised based on:

- the operation of the fund – public offering of investment units (public funds) or private placement of investment units (private funds),
- the type of the fund – open-ended (meaning that investors may withdraw their money by selling back their investment units at any time) or close-ended (meaning that investment units cannot be sold back during the term of the fund),
- the duration of the fund – established for an indefinite or definite period of time,
- the investors – professional or retail investors,
- the type of primary assets – security fund, property fund, venture capital fund or
- private equity fund, or
- EU harmonisation – UCITS and AIFs.

Investment funds are established by registering with the CBH/MNB – please see our FAQ for more details. We note that special rules apply to certain public and open-ended funds established in line with the UCITS directive ("UCITS investments funds") that may be managed (and the investment units may be marketed) on a cross-border basis – explained further in our FAQ.

Investment funds are managed by fund managers acting as legal representatives. Fund management activity includes a wide range of tasks, e.g. preparation of investment strategies, prospectuses, financial reports, targets (which type of investment fund to establish) and determination of the management rules of the fund, entering into a contract with a depositary to provide custodian services, entering into a contract with an investment service provider to market investment units and investing the equity of the fund. To protect investors, fund managers must comply with special investment restrictions (e.g., threshold rules on investing in the financial instruments of one single issuer). Fund management activity is subject to one-tier licencing by the CBH/MNB, meaning that only a business licence needs to be obtained.

Depositaries are mostly credit institutions or investment firms authorised by the CBH/MNB to provide a special type of investment service, i.e. custodian services. The main task of the depositary is to keep the financial instruments of the fund in its custody. In addition, the depositary manages the funds' accounts, monitors cash flows and dealing in investment units during the subscription procedure. The depositaries are also responsible for monitoring compliance with applicable laws and management rules. It is to be highlighted that the depositary must act solely in favour of the investors and independently of the fund manager. The depositary also has significant supervisory powers; namely, the depositary must refuse to carry out the fund manager's instructions which break the law or breach the management rules of the fund. If the fund manager fails to take the necessary measures to restore compliance with the relevant laws or the management rules of the fund, the depositary must immediately notify the CBH/MNB.

How can VJT & Partners help?

We have solid experience in regulatory matters falling under the CBH/MNB's authority. We have particular expertise in licencing / authorisation proceedings with the CBH/MNB. Thus, VJT & Partners is ready to assist its clients in obtaining sector-specific licences or giving legal advice in any kind of financial regulatory matter.

Energy Sector

the energy sector consists of the electricity, gas and district heating markets

The energy sector consists mainly of the electricity, gas and district heating markets. The main regulator is the Hungarian Energy and Public Utility Regulatory Authority ("HEA/MEKH"). HEA/MEKH is primarily responsible for the licensing (including certain acquisition supervision competences) and supervision of compliance with the relevant legal regulations and for establishing administrative pricing. For more information about HEA/MEKH proceedings, please see our FAQ. It also has some competence in consumer protection and supervision of competition. Of course, in this sector, the Hungarian Competition Authority ("HCA") and the consumer protection authorities are also important regulators.

Electricity

Market structure

highlights of the electricity sector

As a general rule, the electricity sector follows a competitive market model where customers may purchase, traders may purchase and sell, and generators may produce and sell electricity under free-market conditions. In this model, competition could be restricted to prevent abuse of market power or to protect universal service customers (defined below).

The key players of the electricity market are the following:

- the transmission system operator (the TSO, a single company called MAVIR, indirectly owned and controlled by the Hungarian state, charged with operating, maintaining and improving the entire Hungarian transmission network),
- distribution system operators (DSOs, each technically distributing electricity in a particular territory),
- generators (i.e., electricity producers),
- traders (each purchasing and selling electricity to the customers),
- the regulated electricity market (HUPX, the Hungarian Power Exchange) and
- customers.

Regarding the regulated electricity market (HUPX, the Hungarian Power Exchange, http://www.hupx.hu), electricity and guarantees of origin can be traded.

Apart from operating on the free market, electricity traders can opt to obtain a uni-

versal service licence that grants the right and obligation to provide services in a particular area for universal service customers. Universal service customers are household customers who opt for universal services instead of buying electricity on the free market, and also customers receiving low voltage electricity of not higher than a total of 3x63A. Universal service providers are obliged to contract with and supply universal service customers under the conditions and officially controlled prices set by law.

We go into more details about the fields of official price regulation and the nature of the universal service in our FAQ.

Licences issued by the HEA/MEKH

In the electricity sector, an HEA/MEKH licence is required to:

- establish a small power plant with a nominal generating capacity of at least 0.5 MW, but less than 50 MW, to generate electricity and terminate its electricity generation,
- establish a power plant with a nominal generating capacity of 50 MW or more, generate electricity and expand, increase or decrease its nominal generation capacity to the extent set out in specific legislation and suspend or terminate its electricity generation,
- control transmission systems,
- distribute electricity,
- trade electricity,
- provide universal services, and
- operate on the regulated electricity market.

It is to be noted that the construction, operation, occupation, renewal and decommissioning of electrical installations, production lines, private lines and direct lines (for special building structures) also requires a licence from the building authority, i.e., the government office.

Natural Gas

Market structure

highlights of the gas sector

Similar to the electricity sector, the natural gas sector also follows a competitive market model. The key players of the natural gas market are the following:

- the transmission system operator (the TSO, a single company called FGSZ Zrt., owned and controlled by MOL Nyrt., the key player on, among others, the Hungarian fuel market, charged with operating and coordinating the entire Hungarian natural gas transmission network),
- gas supply operators (charged with cross-border gas supply and maintenance, and the operation of cross-border transportation grids),
- gas producers (generating gas in Hungary),
- distribution system operators,

- gas storage companies (for commercial or security storage),
- gas traders,
- the regulated gas market (the Hungarian Gas Exchange), and
- customers.

Similar to the electricity sector, the natural gas sector also has a universal service segment and MVM Next Energiakereskedelmi Zrt ("MVM") is the sole universal service provider in the gas sector. MVM has contracting and supply obligations towards universal service customers under the conditions and official prices set by law. Universal service customers are household gas users who opt for universal supply services instead of buying gas on the free market, customers with a gas demand of not more than 20m3/hour and also the local municipalities for supplying the tenants of residential properties owned by local government.

Licences issued by the HEA/MEKH

In the natural gas sector, an HEA/MEKH licence is required to:

- operate a transfer system,
- distribute natural gas,
- store natural gas,
- trade natural gas,
- provide universal services, and
- operate on the regulated natural gas market.

District Heating

Market structure

highlights of the district heating sector

Unlike the gas and electricity sectors, the district heating sector follows the public utility service model. In this model, the government regulates prices and supply areas (the area of a municipality or a part of the municipality) are mostly serviced by one district heating company. The market follows a simple pattern as the main players in the market are:

- District heating producers

  District heating producers generate thermal energy and sell it to the district heating traders or district service providers.
- District heating traders

  District heating traders may be producers who sell thermal energy to service providers or traders who buy the energy from producers and sell it to providers.
- District heating service providers

  District heating service providers have contracting and supply obligations towards household consumers also at the official prices set by law.
- Customers.

District heating producers/traders may sell thermal energy to district heating service providers only at the official prices set out by law.

Licences issued by the HEA

In the district heating sector, an HEA licence is required to:

- install district heating facilities for the nominal capacity limit of 5MW thermal output or above,
- extend, convert, increase or decrease district heating facilities for the nominal capacity limit of 5MW thermal output or above,
- change the fuel of the district heating facilities for the nominal capacity limit of 5MW thermal output or above; and
- produce or supply district heating, irrespective of the capacity production.

In addition, certain permissions are required from the building authorities to install and use the district heating facility, pipeline network or its equipment or heating center on a third party's property.

Authorisation of Certain Corporate Actions

With certain exceptions, in all three sectors, certain corporate actions of the market participants are subject to HEA authorisation:

- the merger and demerger of a licenced company, its transformation or its termination without succession,
- the decrease of the registered capital by at least 25%, and
- the acquisition (directly or indirectly) of at least 5%, 20%, 25%, 33%, 50%, 75%, 90% or 100% of the votes and the exercise of the related rights concerning such influence.

Consumer Protection

guaranteed service level model

The HEA does not handle all individual consumer complaints (e.g. HCPA handles complaints about billing and payments). Still, consumer protection remains an important task of the HEA.

In all three energy sectors, special emphasis is placed on consumer protection rules, e.g. rules on customer contracts, information obligations towards customers, etc. In addition, in the gas and electricity sectors, two special models are adopted – the guaranteed service model and the supply of last resort.

The guaranteed service model means that certain licensees, e.g. universal service providers, must pay a penalty to the customer if the expected services are not met.

The supply of last resort is a special concept in the electricity and gas market that aims to guarantee a permanent service to customers. In the electricity market, if a universal service provider:

- becomes insolvent,
- is unable to supply the energy product,
- has had its licence withdrawn by the HEA and consequently the supply of the energy product is in danger for the universal service customers,

the HEA must appoint a supplier of last resort to provide services for universal service customers. Similar rules apply in the natural gas market.

Supervision of the Competition (Competition Law Authorities)

The competitiveness of the natural gas and electricity markets is supervised jointly by the HEA and the HCA. In cases of abuse of a dominant market position, the difference between the two systems of supervision is that while the HCA carries out ex-post tasks, e.g. investigating and sanctioning the abuse of a dominant market position, the HEA carries out ex-ante intervention to prevent the abuse of a dominant market position.

Therefore, the HEA conducts market analysis in the gas and electricity sectors. If the competition is not considered to be sufficiently effective on any relevant market based on the findings of the market analysis, the HEA identifies the player that has significant market power and imposes certain additional obligations on this player, e.g. a transparent sale, the abolition of discriminative market practices, price restrictions, cost-plus pricing or the obligation to make an offer.

The Pharmaceutical Sector

General Overview

Hungary has a strong tradition of pharmaceutical manufacturing and has always maintained a high level of pharmaceutical consumption. In recent years, multinational biotechnology companies have also begun to capitalise on Hungarian opportunities. The registration and sale of pharmaceutical products are strictly controlled proceedings in Hungary; therefore, all pharmaceutical market participants need to comply with sector-based regulations. The National Center for Public Health and Pharmacy / Nemzeti Népegészségügyi és Gyógyszerészeti Központ ("NCPHP/NNGYK") is responsible for granting licences for activities carried out in connection with medicinal products being introduced into the Hungarian market. The key regulated fields of the Hungarian pharmaceutical sector are:

- manufacturing,
- marketing,
- wholesale distribution, and
- supply of medicinal products.

Pharmaceutical Manufacturers' Licences

manufacturing medicinal products

The manufacture of medicinal products means the authorised production of medicinal products in a controlled industrial environment. Based on Act XCV of 2005 on Medicines, a medicinal product means any substance or combination of substances presented for treating or preventing diseases in human beings or any substance or combination of substances that may be used in or directly applied to the human body, either with a view to:

- restoring, correcting or modifying physiological functions by exerting a pharmacological, immunological or metabolic action, or
- making a medicinal diagnosis.

Any manufacturing activity of medicinal products in Hungary can only be pursued if in possession of a valid manufacturing licence issued by the NCPHP/NNGYK for medicinal products. To ensure that the quality of the medicinal products manufactured conforms with the requirements laid down in the marketing authorisation, the NCPHP/NNGYK only authorises the production of a medicinal product if the applicant satisfies the staff- and infrastructure-related requirements set out in special regulations.

Process of Marketing Authorisation

As a general rule, a medicinal product may be introduced to the market in any EU/EEA member state only if licenced by a member state's competent government body (national licencing) or by the European Commission under EC Regulations (community licencing). Before a medicinal product is introduced into the market, it is recommended that patent protection is obtained for the relevant medicinal product. For more information on patent protection, see "**Intellectual Property**" or "**Industrial Property**".

marketing authorisation of medicinal products

In the Hungarian market context, the licencing procedures can be divided into three categories based on the territorial scope:

- If the applicant intends to obtain a marketing authorisation only for the territory of Hungary, the rules of national procedure apply.

  During the national procedure, the NCPHP/NNGYK is authorised to evaluate the submitted documentation of the medicinal product. The licencing procedure starts with an application and the NCPHP/NNGYK examines whether the submitted documentation meets the formal requirements. In the process of granting marketing authorisation, the quality, safety and efficacy of the new medicinal product are also evaluated. Regarding the suitability of the product, it will be declared a medicine by a public administration decision. This licence is valid only in Hungary.
- If the applicant intends to obtain marketing authorisation in the territory of Hungary and simultaneously in several EEA member states, it can either choose the mutual recognition procedure ("MRP") or the decentralised procedure ("DCP").

The MRP may be conducted if the relevant medicinal product has been authorised in at least one EEA member state (known as a Reference Member State: "RMS"). In such case, the applicant who already holds the licence issued by an RMS may ap- ply for a licence in other member states (individually known as Concerned Mem- ber State or "CMS"). The CMSs are asked to mutually recognise the licence of the RMS. If the application is successful, each CMS will issue a licence permitting the marketing of the medicinal product in their countries.

The DCP may be conducted when the application for the medicinal product's marketing authorisation is pending in several member states simultaneously and has not been authorised in any member state previously. One of the member states (again an RMS) will coordinate the whole process. The RMS will issue the preliminary assessment report and send it to the other CMSs concerned. The CMSs may agree with the report or may raise objections or further questions. If the application is successful, each member state will issue the licence permitting the marketing of the medicinal product in their countries.

- In certain cases, the applicant must (or sometimes is entitled to) obtain an EU-wide central licence that is also considered to be a valid marketing authorisation in Hungary. During the centralised procedure, the application must be submitted directly to the European Medicines Agency. The Agency's Committee assesses the applicability of the medicinal product. Based on the Committee's opinion, the licence is issued by the European Commission and is binding for all EEA member states.

The centralised licencing procedure is compulsory for:

- medicinal products derived from certain processes of biotechnology,
- advanced therapy medicinal products,
- orphan medicinal products, and
- medicinal products containing an entirely new active substance for which therapeutic indication is the treatment of acquired immune deficiency syndrome, cancer, neurodegenerative disorder or diabetes, auto-immune diseases or other immune dysfunctions and viral diseases.

The centralised licencing procedure is optional for:

- other medicinal products containing a new active substance, and
- medicinal products that constitute a therapeutic, scientific or technical innovation or are of interest to patients at the Union level.

The name of the medicinal product is indicated in the marketing authorisation. This may be either an invented name that cannot be confused with a common name, or a common or scientific name together with a trademark or the name of the marketing authorisation holder. Thus, it is highly recommended to obtain trademark protection for the medicinal product's name. For further discussion about trademarks, see "**Intellectual Property**" - "**Industrial Property**").

The marketing authorisations is valid for a maximum of five years (irrespective of whether the authorisation is issued by the NCPHP/NNGYK or the Commission). The licence may be renewed upon request that must be submitted at least nine months before its expiry and is subject to the reassessment of the balance between the risk and benefits involved. Once renewed, the marketing authorisation of a medicinal product will remain valid for an unlimited period of time, except where the competent authority grants only an additional five-year renewal on justified grounds relating to pharmacovigilance and patient exposure.

Parallel Import Licence

Parallel import refers to the import of medicinal products to Hungary from other member states by an importer who is independent of the manufacturer or its authorised distributor. In other words, the import is made outside of the manufacturer's distribution channel.

The parallel import licence is issued by the NCPHP/NNGYK.

Parallel import covers the following activities:

- procuring the medicinal product in the state of origin,
- importing the medicinal product for marketing in Hungary,
- re-packaging the medicinal product,
- performing quality assurance and assessment,
- releasing the medicinal product,
- storing and inventorying the medicinal product,
- transferring the medicinal product to the procurer,
- performing activities related to ending the marketing of the medicinal product,
- maintaining records, and
- supplying product data.

If a parallel importer repackages the product, the packaging and labelling must be compliant with Hungarian regulations and the NCPHP/NNGYK is entitled to investigate the medicinal product concerned.

If the NCPHP/NNGYK issues a parallel import licence, it is valid for a period of five years.

Pharmaceutical Wholesalers' Licences

Wholesale distribution of medicinal products comprises all activities relating to:

- supplying medicinal products to retailers, including the storing and transporting of medicinal products,
- exporting to and importing from EEA member states, and

- exporting to states outside the EEA,

as a result of which medicinal products are transferred from the manufacturer or producer to those authorised to supply medicinal products to the public.

wholesaling authorisation issued by the NIP

All wholesale trade activities of medicinal products for human use in Hungary are only to be carried out by those possessing a valid wholesaling licence issued by the NCPHP/NNGYK . Wholesale distribution licences will remain valid until revoked.

Clinical Trials

Clinical trials are special medicinal investigations carried out on humans that aim to study the effects of one or more medicinal products. Clinical trials are commonly classified into four phases. Each phase has a different purpose and helps scientists answer a different question.

medical investigations carried out on humans

Clinical trials are strictly regulated and may only be conducted with the NCPHP/NNGYK's permission. Furthermore, clinical trials may only be conducted under the terms in the authorising decision of NCPHP/NNGYK and to the specifications of the authorised protocol. It is to be noted that each clinical trial must be planned, conducted and reported in line with the principles of good clinical practices ("GCP") and in accordance with the Helsinki Declaration on the ethical principles of medicinal research. The GCP is published by the NCPHP/NNGYK. In addition, the planning and conducting of clinical trials must, at all times, take place in line with the applicable professional standards, in particular, the detailed guides published by the European Commission on clinical trials.

The Supply of Medicinal Products

The supply of medicinal products includes all activities by which medicinal products are made directly available to users. Medicinal products may be procured on behalf of pharmacies that dispense them to patients. Pharmacies may procure medicinal products only from business entities authorised to engage in activities related to the wholesale distribution of medicinal products. Special regulations related to implementing and operating pharmacies (i.e. how to acquire the implementation and operating permit) are laid down in Act XCVIII of 2006 on the safe and economical supply of medicinal products and the general rules of medicine distribution and in related ministerial decrees.

It is to be noted that certain special rules and procedures apply for special medicinal products, e.g. narcotics or psychotropic substances, veterinary medicinal products, herbal medicines, homeopathic medicinal products.

How can VJT & Partners assist you in pharmaceutical cases?

Due to the complexity of the pharmaceutical regulations, we strongly suggest that you seek professional Hungarian legal advice. VJT & Partners has advised numerous buyers on international M&A transactions in the pharmaceutical wholesale sector. We also have expertise in licencing matters, e.g. marketing licencing of medicinal aids in Hungary. Moreover, our law firm has advised on data protection issues related to clinical trials and pharmacovigilance.

Telecommunications Sector

General Overview

Telecommunications is one of the most heavily regulated industry sectors in Hungary. Act C of 2003 on electronic communications ("ECA") lays down the fundamental rules regulating the provision of electronic communications services and electronic communications networks. However, the ECA does not regulate the content delivered over electronic communications networks. The ECA aims to develop the electronic communications infrastructure, promote competition and protect consumers' interests.

The National Media and Infocommunications Authority ("NMIA/NMHH")

the NMIA supervises the telecommunications sector

The NMIA/NMHH is the main supervisory authority of the telecommunications sector. Its supervisory activity covers all aspects of electronic communications, in particular, the NMIA/NMHH:

- conducts market supervision including the supervision of market practices and general terms and conditions of subscriber services,
- analyses relevant electronic communications markets,
- identifies service providers having significant market power and imposes obligations on them, and
- grants individual rights of use, e.g. frequency assignments and radio licences.

Notification and Licensing Requirements

Please note that the provision of electronic communications services is not subject to licensing. However, the service provider must submit a notification to the NMIA/NMHH before starting to provide services. The ECA defines the mandatory content of the notification which includes:

- the service provider's company name, company form and address (registered office and its branch(es), if any),

- the service provider's business registration number or other official registration or identification number,
- the name (business name) and contact details (postal address, telephone number, e-mail address) of the person designated to liaise with the NMIA/NMHH,
- the designation and a brief description of the electronic communication service or, if the service provider operates an electronic communications network, the designation and a brief description of the electronic communications network and the EU Member States involved in the provision of the services,
- the planned date of commencing the service, and
- the service provider's website address that is related to the operation of the electronic communications networks or the provision of electronic communications services.

The NMIA/NMHH must also be notified of the actual date of commencing the service, terminating the provision of services and any modification of the data notified.

However, the granting of an individual right of use by the NMIA/NMHH is required in the following cases: the installation of a radio station, radio equipment, radio-communications network and radio system. All require obtaining a frequency assignment and radio licence for their operation. As a general rule, the construction of electronic communications infrastructure is subject to the licence issued by the NMIA/NMHH.

Market Analysis and Obligations Imposed on SMP-Service Providers

special rules apply to service providers having significant market power

One of the main goals of the telecommunications regulations is to ensure and promote effective competition in the market. The NMIA/NMHH analyses market segments identified as relevant markets to see if effective competition has already been realised. If the NMIA/NMHH finds that effective competition has not yet been realised, it identifies the service providers with significant market power. The NMIA/NMHH may impose certain obligations on service providers with significant market power in the context of transparency, non-discrimination, accounting separation, access and interconnection, price control or functional separation.

Provision of Universal Service

The NMIA/NMHH may designate universal service provider(s) to ensure that broadband internet access and voice services are available to all users at an affordable price.

Universal service providers have the obligation to provide universal services to users. More specifically, universal service providers have a contracting obligation to provide one access point to universal services for each user who has a residence, registered office or business premises in the particular authorised areas of the relevant universal service provider.

FAQ

Financial Sector

1. What is the solvency capital requirement ("SCR") in a nutshell?

The Solvency II directive introduced the concept of the SCR to cover potential risks. It must be set at a level so that insurance and reinsurance companies can meet their obligations with a confidence level of 99.5%.

While a breach of minimum capital requirement may result in the revocation of licence, a breach of the SCR usually results in the CBH/MNB's intervention to achieve an appropriate action to restore the SCR.

2. In what corporate forms must the most important financial market participants be founded?

- Banks and specialised credit institutions may be founded in the form of companies limited by shares or as branch offices of a foreign entity.
- Cooperative credit institutions may be founded as cooperatives.
- Financial enterprises may be founded in the form of companies limited by shares, cooperatives, foundations or the branch offices of foreign entities.
- Insurance companies may be founded in the form of companies limited by shares, European companies, cooperatives, associations or as the branch offices of foreign entities.
- Investment firms may be founded in the form of companies limited by shares or the branch offices of foreign entities.
- Investment fund managers, in general, may be founded only in the form of companies limited by shares.

3. What are the minimum registered capital requirements for the foundation of the main financial market participants?

In the banking market, the following minimum capital requirements are applicable:

- for banks and financial holding companies: HUF 4 billion,
- for cooperative credit institutions: HUF 300 million,
- for financial enterprises (except for financial enterprises providing credits or loans, financial holding companies and payment clearing houses): HUF 100 million,
- branch offices of third-country companies: HUF 4 billion endowment capital, and
- financial enterprises providing credits or loans: HUF 150 million.

In the capital market, the following minimum capital requirements are applicable:

- for securities funds established publicly: HUF 200 million,
- for real estate funds established publicly: HUF 1 billion,
- for securities funds established by private placement: HUF 100 million,

- for real estate funds established by private placement: HUF 500 million,
- for private equity and venture capital funds: HUF 250 million,
- for fund managers managing securities funds: EUR 125,000,
- for fund managers managing real estate funds: EUR 300,000 (with special rules that apply if the portfolio handled by the fund manager exceeds EUR 250 million),
- for investment firms: EUR 150,000, and
- for investment firms pursuing certain investment services: EUR 750,000.

On the insurance market, the minimum capital requirement must not be less than 25% of the solvency capital requirement. Regardless of this general 25% threshold, special minimum amounts apply as a minimum capital requirement for insurance companies engaged in specific insurance sectors (e.g. EUR 4 million for companies engaged in life insurance).

4. When must the minimum capital be paid?

For one-tier licencing procedures, the full amount of minimum capital must be paid at the time of application for the foundation licence.

However, for two-tier licencing procedures, the applicant may pay only part of the minimum capital when applying for the foundation licence; the rest may be paid after application, but before application for the business licence.

5. Can the applicant pursue any financial activities after obtaining the foundation licence, but before obtaining the business licence? Are there any deadlines for application for the business licence after the foundation licence has been granted?

The applicant may not pursue business activities based on the foundation licence alone. With the foundation licence, the applicant may only begin to make preparations for its business activity and apply to the Court of Registration for company registration.

Pursuing actual business activities is only possible after obtaining the business licence. Upon receipt of the foundation licence, the deadline to apply for the business licence is 90 days for insurance / reinsurance companies and 6 months for credit institutions.

6. Is the official translation of foreign documents compulsory?

When applying for the foundation or business licence and in the case of an acquisition of a qualified interest, the official translation (provided by the National Office for Translation and Attestation) of foreign documents is compulsory. In other cases, the CBH/MNB has the discretionary power to decide whether to request only a short Hungarian summary or the full official translation of the document.

7. What is the usual decision-making process of the CBH/MNB? What is the usual time frame?

During the authorisation / licencing, the CBH/MNB carefully reviews the documents and information regarding the application. If required, it conducts site inspections and

evaluates whether granting authorisation will violate any legal provisions. Irrespective of the CBH/MNB's actions, the applicant must submit a statement that it has provided the CBH/MNB with all the data and information required for the authorisation.

The general administrative deadline to issue the authorisation is 3 months. But, in certain cases, the decision regarding authorisation may be extended once for a further 3 months, e.g. in cases of the authorisation regarding foundation, merger, demerger, pursuance of activity or transfer of portfolio.

The decisions of the CBH/MNB can be challenged before the Budapest-Capital Regional Court.

8. Does Hungarian Law recognise the concept of the universal banking licence?

Hungary recognises the concept that banks may pursue both banking and investment services (universal banking). However, there is no single licence for both traditional banking and investment service activities.

Apart from traditional banking activities, if a credit institution wishes to provide in- vestment services, it must obtain an additional business licence authorising the credit institution to provide investment services.

Therefore, a credit institution altogether needs three licences to pursue universal banking: a foundation licence of a credit institution, a business licence of a credit institution and a business licence to provide investment services.

9. Is there any relief from regulatory burdens with regard to EU/EEA domiciled companies looking to enter the Hungarian financial market?

The most important relief from regulations applies to companies registered in another EU/EEA member state, e.g.:

- insurance companies,
- credit institutions,
- financial enterprises (under certain specific conditions),
- investment fund managers managing Hungarian UCITS funds, and
- investment firms registered in another EU/EEA Member State.

These companies may carry out their activities in Hungary through their Hungarian branch office or via cross-border services, without any authorisation or licence requirements of the CBH/MNB ("Single European Passport"). In addition, for UCITS investment funds registered in another EU/EEA member state, the compliance requirements are simplified. In all these cases, the main financial supervisory authority will remain in the EU/EEA country where the company is registered.

10. Is there any relief from regulatory burdens with regard to third-country companies looking to enter the Hungarian financial market?

As a general rule, companies registered in a third (non-EU/EAA) country must obtain a licence from the CBH/MNB. Still, in some specific cases, there is important relief from regulations:

- financial institutions operating in the form of a Hungarian branch office may avoid certain compliance requirements, e.g. certain corporate governance or prudential rules do not apply, and
- a financial institution registered in a country that is a member of the Organisation for Economic Co-operation and Development (OECD) may pursue certain financial activities on a cross-border basis, e.g. granting loans and credits, financial leasing activities.

11. What is the usual procedure to establish an investment fund?

In both cases (for establishing public and private funds), prior to the establishment, the fund manager must prepare the management rules, enter into a contract with the depositary, organise the subscription procedure to collect the required minimum capital. Once the minimum capital has been collected, the fund manager will submit the registration application to the CBH/MNB. However, there are some notable differences between the establishment procedure of private and public funds:

- While the management rules of a private fund must only be notified to the CBH/MNB, the management rules of a public fund must be approved by the CBH/MNB,
- In contrast to private funds, fund managers of public funds must also prepare a prospectus, key investor information and public announcement, documents of which are subject to the CBH/MNB's prior approval, and
- Whilst in the case of private funds, the only precondition of beginning the subscription procedure is to make the management rules available to potential investors 7 days before the commencement date of the subscription; in the case of public funds, the subscription procedure may commence only after the approval of the prospectus, key investor information and public announcement, investment data, the management rules (the approval deadline is 20 working days) and the necessary publications.

The Energy Sector

1. What is the difference between the former public utility service and the universal service?

The main difference between the two is that while the former public utility service means buying and selling the energy product at the official price, the universal service means that the energy product is purchased at the market price and sold at the official price.

2. Apart from the universal services, are there any other areas where the prices are officially regulated in the gas and electricity sectors?

Yes. The network usage fees in the electricity sector, e.g. the transmission system operator's fee or the electricity distribution fee, and in the gas sector, e.g. gas supply fee, the gas distribution fee and the gas storage fee, are officially regulated fees.

3. Does Hungarian law have unbundling rules?

In accordance with EU directives, Hungarian law recognises the concept of accounting and functional unbundling. The main aim of unbundling rules is to ensure that:

- a vertically integrated electricity company pursuing transmission system control or distribution separates these activities in terms of legal personality, organisational structure and decision-making from the other activities of the vertically integrated electricity company,
- a horizontally and vertically integrated electricity company and a company pursuing several electricity activities keeps separate accounts for each of their activities,
- an integrated gas company pursuing gas supply and the operation of the Hungarian gas network, gas distribution and gas storage, separates the gas supply, the gas distribution and gas storage activity in terms of legal personality, organisational structure and decision-making from the other activities of the vertically integrated gas company,
- an integrated gas company and a company pursuing several gas activities keeps separate accounts for each of their activities, and
- a licensee pursuing more activities regarding district heating must keep separate accounts for each activity, e.g. electricity production, district heating production, district heating service and other activities.

4. What is the usual time frame for approval by the HEA?

The HEA's general administrative deadline (also applicable to licensing procedures) is 75 days unless otherwise provided by other sectoral rules.

5. What does the HEA examine during the licensing procedure?

In all three energy sectors, the HEA examines compliance with statutory provisions, long-term facility conditions, e.g., technical, financial and business criteria, and the ab- sence of some negative conditions, e.g., whether the applicant has been or is engaged in a bankruptcy or liquidation proceedings or whether any of the applicant's operating licences have been revoked within a ten-year period prior to applying for a reason attributable to the applicant.

6. Can the HEA's decision be challenged?

Individual administrative decisions may be challenged in front of the competent court. The applicant may ask for the HEA's decision to be suspended unless otherwise provided by statutory sectoral rules. The competent court has the power to amend the HEA's decision (with some exceptions).

The Pharmaceutical Sector

1. Does a licence for the manufacture of medicinal products also constitute the right to trade self-manufactured products on the wholesale market?

Yes, but only if the manufacturer complies with the personnel and infrastructure-related requirements set out in the related legislation for the wholesale distribution of medicinal products.

2. What does the marketing authorisation issued by the NCPHP/NNGYK contain?

The marketing authorisation, in addition to the medicinal product's identification data, contains:

- the number of the marketing authorisation, the name of the marketing authorisation holder and the manufacturer's registered office,
- the summary of product characteristics,
- the label information,
- the package leaflet,
- the classification of the medicinal product, and
- the expected shelf life of the medicinal product and storage instructions.

3. What is the timeframe of the main administrative procedures conducted by the NCPHP/NNGYK?

The administrative time limit for marketing authorisation procedures is 210 days from the day after applying to the NCPHP/NNGYK. Furthermore, the authority must bring a decision concerning applications for wholesale distribution within 90 days of the date of receiving the application.

4. What are the main requirements concerning the operation of a pharmacy?

A pharmacy may start to operate:

- when it possesses an establishment permit issued by the government body in charge of the healthcare system,
- if it has a pharmacist vested with an independent right in the case of a public pharmacy,
- when it possesses an operating permit issued by the government body in charge of the healthcare system,
- for public pharmacies, if the operator has sufficient liability insurance coverage for damage that the pharmacy may cause, and
- if the pharmacy meets the conditions decreed by the competent minister regarding architectural requirements, equipment and furniture and personnel requirements.

Telecommunications Sector

1. Is the Hungarian regulation on electronic communications harmonised with the EU regulatory framework?

Yes, the regulatory framework of the European Union adopted in 2018 has been transposed into the ECA.

2. What are the primary preconditions of providing electronic communications services in general?

In general, the provision of electronic communications services is not subject to licensing; however, the service provider must notify the NMIA/NMHH before starting such services.

3. What electronic communications activities are subject to licence?

Certain activities, e.g. the operation of a radio station, radio equipment, radio communications network or radio system and the construction of electronic communications infrastructure are subject to licence.

4. What are the main obligations that can be imposed on electronic communications service providers having significant market power?

The NMIA/NMHH may impose certain obligations on service providers having significant market power in the context of transparency, non-discrimination, accounting separation, access and interconnection, price control or functional separation.

5. What are the main tasks of the NMIA/NMHH?

Among others, the NMIA/NMHH:

- conducts market supervision including the supervision of market practices and the general terms and conditions of subscriber services,
- analyses relevant electronic communications markets,
- identifies service providers having significant market power and imposes obligations on them, and
- grants individual rights of use, e.g. frequency assignments and radio licences.

6. Does the Hungarian telecommunication regime apply to Voice Over Internet Protocol (VoIP) services as well?

Yes, the Hungarian telecommunication regime also applies to VoIP services as it is considered to be a form of electronic communications service.

Operating a Business Entity

"With a little skill we could build steps from the rocks that roll across our paths."

—István Széchenyi

*This part briefly outlines the most important administrative burdens (**Taxation**, **Accounting** and **Auditing**) of an existing Hungarian business entity. In addition, this part highlights the most important rules regarding the establishment, maintenance and termination of an employment relationship (**Working in Hungary**) and also gives an overview of some financial issues, such as crediting, state subsidies, insolvency (**Financing Matters**).*

Taxation

In this chapter, we introduce the Hungarian tax authorities and their competencies, followed by an overview of the main building blocks of Hungarian state revenue, i.e. corporate tax, personal income tax and value-added tax ("VAT"). We also explain the anti-avoidance rules that influence tax optimisation and provide an insight into double tax treaty schemes with a view towards the growing importance of cross-border transactions.

General Overview

no unified tax code applies in Hungary

One of the Hungarian government's main priorities is to raise taxes on consumption and lower taxes on employment and profit. As a result, Hungary has the highest VAT rate and one of the lowest personal income and corporate income tax rates in Europe. The Hungarian taxation system tends to tax income, sales and other specific transactions, rather than capital.

The Hungarian taxation system is based on different substantive tax laws in which no unified tax code applies. The same applies to the tax administration which is also regulated in separate tax acts.

Generally speaking, the Hungarian taxation system works on a self-assessment basis (with some rare exceptions). This means that the taxpayer must assess their income and calculate their tax. While only limited information must be disclosed, taxpayers must take their obligation seriously given that the tax authority may audit and impose penalties and interest for late payments or submitting incorrect data.

Tax Authorities

National Tax and Customs Administration

Hungary's central tax authority is the National Tax and Customs Administration ("NAV/NTCA") which combines the state tax authority and the customs authority. Locally, the notaries of municipal governments act as tax authorities regarding local taxes. In general, the tax authorities supervise companies over their entire "life circle" (from foundation to dissolution). Companies are subject to tax registration by the NAV/NTCA and only companies with a tax number can pursue business activities (for more information, see the FAQ section). The tax authorities can inspect registered companies at any time until 31 December of the 5th calendar year following the calendar year in which taxes should have been declared or paid.

Avoiding tax obligations may result in fines, the deletion of the tax number (i.e. the dissolution of a company) and, in serious cases, criminal sanctions.

Personal Income Tax

Taxpayer

For personal income tax purposes, an individual qualifies as a resident taxpayer if they:

- have Hungarian citizenship (except dual citizens with no permanent or habitual residence in Hungary),
- have stateless status,
- have settled status in the case of non-EEA nationals,
- stay for more than 183 days in a calendar year in Hungary in the case of EEA nationals,
- have a permanent address in Hungary,
- have their centre of vital interest in Hungary (even if their permanent residence is not in Hungary or not only in Hungary), or
- have habitual residence in Hungary (if none of the above conditions have been met).

The tax treaties prevail over the residence test conditions found in domestic rules.

Taxable Income

Both resident and non-resident taxpayers have a tax liability but the scope of their liability may vary. Non-resident taxpayers are only subject to tax on their income generated in Hungary. Such Hungarian-earned income includes:

key elements of tax administration

- income received domestically,
- income received abroad for activities performed in Hungary, or
- income originating from a Hungarian asset.

Resident taxpayers are subject to tax on their whole worldwide income, but they may ask for relief from double taxation based on specific tax treaties.

From a taxation point of view, there are two different types of income:

(i) consolidated income tax, i.e. on salaries, income from independent activities and other similar income, and

(ii) unconsolidated, or independent income tax, i.e. on interest, capital gains, dividends, etc.

Tax Rates

The tax rate for consolidated income is levied at a flat rate of 15%.

The tax rates for independently-taxed incomes are also generally 15%. The base of the independently-taxed income is the gross income subject to exceptions.

Tax Administration

key elements of tax administration

Tax returns must be submitted annually and an advance tax payment is compulsory. The taxpayer may perform their obligations by:

(i) using the tax return prepared by the tax authority, or

(ii) completing a self-assessment.

The tax return prepared by the tax authority –The tax authority prepares drafts of the personal income tax return for taxpayers registered for electronic tax filing or for those other taxpayers who request a draft return from the tax authority by 15 March. In these cases, the tax authority will prepare the draft return and the taxpayer will have the possibility to challenge this draft (or prepare their own return without accepting the draft) by 20 May.

Self-assessment – In other cases, e.g. for a sole proprietorship, the taxpayer assesses their income and calculates the tax. The tax return must be filed and the assessed tax must be paid by 20 May.

Advanced tax payment – Employers must deduct tax from salaries on a monthly basis (due on the 12th of the month following the actual month the work was performed). For other types of income, e.g. income generated from renting a property, as a general rule, the advanced tax payments must be carried out by the personal income tax resident itself on a quarterly basis (due on the 12th of the month following the actual quarter the work was performed).

Termination of the Hungary-USA Double Tax Treaty

As of 1 January 2024, the double taxation treaty between Hungary and the US terminated. In the absence of a tax treaty, from 2024 the right of the United States of America to deduct withholding taxes (up to 30%) on payments under its domestic rules will not be limited. While 90% of the withholding tax deducted abroad may be offset against domestic tax liability, 5% of separately taxable income (for example: dividend) will still be subject to tax in Hungary. If a US resident receives income from Hungary, the payer will also deduct the 15% personal income tax, which can be offset against US tax liability under US rules.

Corporate Income Tax

Taxpayer

Corporate resident taxpayers are treated as residents if they are incorporated under Hungarian law or have their place of management in Hungary. They are subject to corporate taxation on their worldwide income with the right of relief from double taxation. If a double taxation treaty applies, the treaty determines the residence. Corporate non-resident taxpayers are only taxed if they are foreign companies carrying out business activities in Hungary through a permanent establishment (through a fixed location for engaging in a business activity, e.g. a branch or representative office or through an employee or other personnel providing services for more than 183 days within 12 months) or if they earn income by selling shares held in a company owning real estate in Hungary. They are subject to corporate tax on the income earned in Hungary.

Corporate taxpayers may be taxed at a group level if all the criteria for this are met (please see more about corporate group taxation in our FAQ).

Taxable Income

taxable income of corporates

The corporate income tax base is the pre-tax accounting profit that is adjusted by certain modifying (deductible and non-deductible) items allowed by law. In general, all expenses incurred in generating taxable corporate income are deductible. In addition, apart from deductible items, the corporate tax base can be further decreased through depreciation and rules concerning losses.

Depreciation rules aim to write off purchase or production costs. In general, machinery and equipment are subject to an annual rate of 14.5% for depreciation. Computers are subject to an annual 33% depreciation rate. Certain new tangible assets and intellectual properties acquired or purchased in or after 2003 may be depreciated at an accelerated annual rate of 50%. Taxpayers may apply a lower depreciation rate than the rate provided by tax law; however, not lower than the depreciation rate for accounting purposes.

The rules on loss provide that taxpayers may use their loss from previous years to decrease the tax base if it does not constitute an abuse of law. Tax losses may be car- ried forward up to five years with a 50% limit of the amount that can be offset against the annual tax base. Permission from the tax authority is not required to carry a tax loss forward.

Finally, the rule on minimum tax applies to companies with a loss or trivial profit. Companies must pay the minimum tax if their pre-tax profit or tax base does not reach the minimum tax base, i.e. 2% of the total revenue adjusted by certain qualified items. The minimum tax is calculated by applying the general corporate income tax

rates to the minimum tax base. Optionally, these taxpayers may pay tax based on their actual tax base if they file a declaration that the low tax base has legitimate grounds. However, in this case, it is more likely that the company will be audited by the tax authority.

To mitigate the economic consequences of the pandemic and enhance investments, the rules on tax base deduction regarding the development reserve have been extended. A development reserve may be established of up to 100% of the profit before tax, and the previous annual cap of HUF 10 billion has also been abolished.

Tax Rates

Corporate income is levied at a flat rate of 9%. This is currently the lowest corporate income tax rate in the EU. A number of tax and tax base reliefs are available, for example for new investments, energy efficiency investments or support for sport, so the 9% tax rate can be reduced even to 1.8%.

Capital Gains, Interests, Royalties and Dividends

the most important cases of deductible items

The corporate tax base is subject to numerous deductions. However, we will mention only a few of the most important tax exemptions.

Capital gains are treated as being a part of business income and accordingly are included in the corporate income tax base. However, capital gains from certain transactions are tax-exempted, e.g. incentives for holding and licensing companies. The sale of capital participation is exempt if the taxpayer holds participation for at least a year and reports the acquisition to the tax authority within 75 days of the acquisition. The amendment provides a one-off possibility to report such capital participation after the general deadline. The tax exemption can apply if such capital participations are going to be reported within the deadline of the year of 2023's corporate tax return (beside the corporate tax has to be paid on the 20% of the difference between the current market price and acquisition price of capital participation). A similar exemption rule applies to the sale of reported intellectual property if reported within 60 days of the acquisition.

Hungarian-sourced dividends that are paid to other companies (irrespective of whether the companies are Hungarian or foreign) are also tax-exempt. Foreign-sourced dividends received by Hungarian companies are also tax-exempt unless the dividends are received from a controlled foreign company ("CFC" - the definition of a CFC is shown below, under the anti-avoidance rules). However, due to recent changes in the law, the part of the dividends received from a CFC derived from genuine transactions may also be tax-exempt.

Interests and royalties paid to foreign companies are not subject to withholding tax. In addition, inbound royalties are subject to a 50% deduction rate — a preferential tax rate of 4.5%.

Deductible items	Sale of registered capital participation	Dividends	Outbound royalties and interest	Inbound royalties	Inbound interest
Deduction rates	100%	100%	100%	50%	0% (non-deductible)

Limitation on interest deduction

From 2019, new rules have applied to the limitations of interest deduction. Instead of testing the former debt-to-equity ratio (the ratio limit was 3 to 1), the new tax rules state that interest deductibility is connected to the profit before tax.

Under the new rules, a taxpayer's net borrowing costs (i.e. as a general rule, these are the interest expenditures incurring in the interest of the business activity that exceeds the taxable interest revenue or equivalent revenue) may be deducted by up to 30% of the taxpayer's tax base calculated without adjustment for the interest deduction limitation decreased by the net interest expense tax depreciation and amortisation (Tax EBITDA) or up to HUF 939,810,000 per year (whichever amount is higher).

If the net cost of borrowing exceeds this cap, the taxpayer may still reduce its tax base up to the unused interest deduction capacity generated in the previous tax year(s). The limitation of interest deduction rules is subject to some group ratio rules.

Tax Administration

The corporate income tax system works on a self-assessment basis. Advance tax payments based on anticipated profit are due on a monthly (the 20th of each month) or quarterly (the 20th of every third month) basis depending on the threshold (if the tax paid in the previous year exceeded HUF 5,000,000). Corporate taxpayers must submit the tax report and pay the difference between the tax advances paid and the corporate tax assessed for the tax year or may request a refund of such by 31 May (assuming that the taxpayer's financial year is the same as the calendar year).

Value Added Tax (VAT)

overview of VAT

VAT is a consumption tax imposed on the supply of goods and services. As indicated by its name, only the added market value is taxed. At every stage of the market, the taxpayer shifts the burden of VAT payment by increasing the sale price of products and services with the added VAT input. Simultaneously, the taxpayer may reclaim the prior added VAT input that they paid in the previous market stage for the supply of goods and services.

Taxable Transaction

VAT taxpayers are all natural persons, legal persons or organisations with a legal entity that pursue a regular business activity regardless of the purpose, place and results of this activity. The object of VAT is the supply of goods and services (for consideration) performed in Hungary, the purchase of products within the European Community and the import of products. The tax base is the sales value of the goods and services modified by items specified in the legislation (e.g. discount, surcharge) or the value increased by the customs duty for imported products.

Tax Rates

The general tax rate is 27%. A reduced rate of 18% applies, e.g. to dairy and bakery products. Another example of a reduced rate is the rate of 5% that applies to medicines and certain medical-related goods, books and non-daily newspapers, and that also applies to certain new residential properties until 31 December 2024. As from 2024, a reduced rate of 0% applies to daily newspapers.

Group Taxation

The whole corporate group, upon request to and approval from the tax authority, is treated as a single taxpayer regarding its tax liability. The group prepares one consolidated tax return. Transactions between the members of the group are not within the scope of VAT.

VAT Exemptions

Hungarian VAT law has adopted the destination principle, meaning that only imported products are levied with VAT in cross-border transactions. Consequently, outbound transactions (exports and the great majority of intra-Community supplies) are not subject to Hungarian VAT and the prior VAT input can be deducted.

Certain transactions carried out in Hungary are also VAT-exempt; however, without the right to fully recover the prior VAT input. Important examples include the lease and rental of property as well as the sale of property (excluding sales before the completion of construction and sales where the permit has been issued less than two years before the sale). Nonetheless, the taxpayer in these cases may opt to pay VAT if they want to deduct prior VAT input (see the FAQ section for details). Some financial transactions, e.g. insurance, reinsurance and credit transactions, investment fund management and equity transfers, are also VAT-exempt.

A taxpayer who has settled in Hungary for business purposes or has a permanent or habitual residence in Hungary could opt to be exempted from VAT payment if the total value of the considered supply of goods and services realised does not exceed

HUF 12,000,000 in either the previous or the given calendar year.

Cases	VAT exemption	Right to deduct VAT input
Exports and intra-Community supplies	Yes	Yes
Lease and rental of property, sale of property (under certain conditions)	Yes	No However, the taxpayer may deduct VAT input if it opts for VAT payment
Financial transactions	Yes	No
Threshold exemption (HUF 12,000,000)	Yes	No

Tax Administration

Taxpayers need to register for VAT. Non-Hungarian entities, i.e. those taxpayers who have not settled for business purposes in Hungary or do not have a permanent or habitual residence in Hungary, are required to register for VAT if they perform a regular taxable business activity in Hungary. Non-EU entities, i.e. those taxpayers who reside for business purposes in a non-EU country or have a permanent or habitual residence in a non-EU country, need to appoint a fiscal representative. Taxpayers need to issue invoices (under certain conditions, issuing electronic invoices is also a possibility) and keep detailed bookkeeping of those invoices. As of 1 July 2020, an online data reporting obligation was introduced relating to all invoices issued by a taxpayer to another resident taxpayer for domestic transactions. As of 1 January 2021, almost all invoices to which Hungarian invoicing rules apply are subject to this reporting obligation.

VAT tax administration also works on a self-assessment basis. The taxpayer must report VAT:

- on a quarterly basis in general,
- on a monthly basis if the net VAT liability reported for the second year before the actual year exceeded HUF 1,000,000, or
- on an annual basis if:

(i) the net VAT liability reported for the second year before the actual year did not reach HUF 250,000, or

(ii) in the second year before the actual year, the taxpayer had revenue not exceeding HUF 50 million (excluding VAT) from supplying goods and services and they do not have an EU tax number.

Taxpayers must report and pay VAT and reclaim VAT input by the 20th of the month following the relevant month (for monthly returns) or relevant quarter (for quarterly returns), or by the 25th of the second month following the relevant year (for annual returns).

The tax authority prepares draft VAT returns for taxpayers that will become valid when the taxpayer accepts and submits their VAT return by the deadline for submitting the return.

Miscellaneous Taxes

Small Business Taxes

types of replacement taxes existing under Hungarian law

The small business tax (in Hungarian: "KIVA") is a replacement tax which is an option for certain small and medium enterprises, e.g. zrt., under certain conditions including those in which the given enterprise employed no more than 50 employees in the preceding tax year and the annual revenue was below HUF 3 billion in the preceding tax year. The tax base is the balance of certain deductible and non-deductible items set out by law increased by employment-related payments (which qualifies as the base for social security contributions according to the social security regulations). Deductible items include, e.g. the amount recognised as the growth of equity (in particular, the increase of the registered capital) or the amount of dividend received (less the amount of tax paid abroad). Non-deductible items include, e.g. the amount recognised as a decrease of equity (in particular, the decrease of registered capital), the amount of penalties or the costs not incurred in the interests of the business enterprise. KIVA replaces the effect of certain taxes, e.g. corporate income tax and social security tax. The tax rate is 10%.

Social Security Tax

With social security tax, the state ensures funding for the Hungarian social security system. However, it does not grant social rights of allowances or subsidies (these social rights are covered by individual social contributions.) It is the employer who must calculate and pay the social security tax. The tax base is identical to the tax base for personal income. The tax rate is 13%.

Local Tax

Local governments have the right to levy certain local taxes (tax on buildings, land tax, communal tax, tourism tax and local business tax) up to the mandatory limits set out in the Local Tax Act. The most significant local tax is the local business tax with an upper limit of 2% of net revenue decreased by certain deductible expenses.

Crisis Tax on the Financial Sector

A crisis tax on the financial sector was introduced in 2010 after the global financial crisis to improve the balance of the state budget. Certain financial sector players are subject to extra taxation, e.g. credit institutions, financial enterprises and managers of private equity funds. The tax rates vary according to the particular financial subsector.

Special Retail Tax

As of 2020, a special retail tax has been reintroduced in Hungary. The tax base is the net sales revenue of the taxpayer deriving from retail activities increased with certain adjustments. The tax rate is determined progressively with a view to the tax base. Practically, all kinds of retail activities are subject to this tax but only if the taxpayer's tax base exceeds HUF 500 million tax base.

Extra-profit Tax

As of June 2022, the Government has introduced various extra-profit taxes. Various taxpayer groups are affected by the extra-profit taxes, e.g. insurance companies, and pharmaceutical distributors. The tax rates, tax returns and payment deadlines vary according to particular taxpayer groups.

Excise Tax

As of June 2022, the Government has introduced various extra-profit taxes. Various taxpayer groups are affected by the extra-profit taxes, e.g. insurance companies, and pharmaceutical distributors. The tax rates, tax returns and payment deadlines vary according to particular taxpayer groups.

Transfer Tax

The transfer of Hungarian real estate is subject to a transfer duty of 4% up to the market value of HUF 1 billion and 2% for the excess with a cap limit of HUF 200 million per property. It is to be noted that property acquisitions by share deals may be also subject to transfer tax (more information about this can be found below in the FAQ section).

Anti-avoidance Rules

General Rule

the applicable anti-avoidance rules

The transaction must be based on real economic and commercial reasons to claim tax benefits. Moreover, the tax benefits are not available if the main goal (or one of the main goals) of the transaction is to secure a tax benefit contrary to the subject matter or purpose of the applicable tax legislation.

In addition to this general tax anti-avoidance rule, several special anti-avoidance rules exist, mainly in the field of corporate taxation.

Transfer Pricing Rules

To disallow price agreements for tax purposes, Hungary follows OECD guidelines that provide that transactions between related parties must be concluded at the same market price as is determined between unrelated parties ("arm's length price"). In general, the parties are treated as related parties if:

(i) one party holds more than 50% of the voting rights in the other party,

(ii) one party holds a direct/indirect management control over the other party, or

(iii) a third party holds more than 50% in both parties.

Since 1 January 2015, the parties have also been treated as related parties if a controlling influence on business and financial policy exists between them due to the identical composition of their management boards.

If the price determined between the related parties differs from the market price, the tax authority may adjust the tax base to the arm's length price (i.e. the tax authority may determine an additional tax, up to the market price level) and, as a general rule, impose a penalty of up to 50% of the additional tax plus a daily late interest calculated based on the applicable base rate of the Central Bank of Hungary (i.e. the applicable rate increased by 5% and divided by 365). Related parties are required to document inter-company transactions in "transfer pricing registers". Failing to comply with the documentation requirements may result in a penalty of up to HUF 5 million as a general rule, but for repeated violations, the penalty could even be up to four times the amount initially imposed. Companies are also obliged to provide data to the tax authority regarding the determination of the arm's length price within the framework of their corporate income tax report.

If the related parties are uncertain as to whether or how to determine the arm's length price and wish to avoid potentially costly disputes with the tax authority, they can opt for advance pricing arrangements ("APA"). Under the APA, the related parties agree with the Ministry of Finance upon the application of the arm's length price principle (as a general rule, from three to five years in the future).

Controlled Foreign Companies ("CFC") Rules

Controlled Foreign Companies ("CFC") rules have the ultimate goal of targeting Hungarian tax residents in offshore tax schemes. The relatively new Hungarian CFC rules (effective from 2019) are complex; thus, Hungarian persons/entities that have control over foreign companies/organisations are advised to review the applicability of CFC rules to their tax schemes.

In general, the basic concept is that, for the CFC rules, a foreign company qualifies as a CFC if:

- the taxpayer directly or indirectly holds more than 50% of the votes or more than a 50% share in the registered capital of a foreign company, or the taxpayer is entitled to more than 50% of the net (after-tax) profit of a foreign company, and
- the effective corporate tax paid by this foreign company is less than the tax difference arising from the amount it would have paid to Hungary and the amount of effective corporate tax paid (if the former amount exceeds the latter).

The foreign permanent establishment of a resident taxpayer also qualifies as a CFC if the effective corporate tax paid by this foreign permanent establishment is less than the tax difference arising from the amount it would have paid to Hungary and the amount of the effective corporate tax paid (if the former amount exceeds the latter).

The CFC rules also introduced the novel "significant personal function" concept. Ac- cording to this concept, a foreign company or foreign permanent establishment quali- fies as a CFC if the foreign tax scheme aims to achieve tax benefits and the Hungarian tax resident provides the essential personal functions that contribute to the income- generating activities of the foreign company or foreign permanent establishment to a large extent.

In the CFC qualification, the size of the foreign company may be also relevant. A foreign company will not qualify as a CFC if its pre-taxed profit does not exceed HUF 243,952,500 and the non-trading income does not exceed HUF 24,395,250 or its pre-tax profit does not exceed 10% of its operating costs for the given tax year. Tax law contains a list of non-trading incomes, i.a. incomes deriving from interests, financial instruments, copyrights, shares/equities and financial leasing.

A permanent establishment of a foreign company may not qualify as a CFC if it is exempt from or not subject to tax in the country of residence of that foreign company. However, exemptions related to a CFC cannot be applied if the foreign company or foreign permanent establishment has a tax residency in a "non-cooperative state".

The general effect of CFC rules is that Hungarian tax residents cannot avoid their tax obligation through a CFC transaction. The following highlights summarise some of the main CFC rules:

- consideration paid to a CFC is not treated as business expenses and accordingly, they are not deductible for corporate income tax purposes unless the taxpayer has proven to the contrary, and

- dividends, which are generally tax-exempt, are taxable if received from a CFC and not derived from genuine transactions.

Rules under ATAD II (The Anti-Tax Avoidance Directive)

In line with the implementation of the EU directive, ATAD II, several new anti- avoidance rules have been introduced in Hungary. ATAD II introduced rules on hybrid mismatches. These rules aim to avoid double non-taxation, double deduction, deduction without inclusion and non-taxation without inclusion in cross-border transactions based on the differences between tax systems, i.e. the different characterisation by two countries of entity, payment or business activities.

Based on this concept, if a Hungarian tax resident enters into an agreement with a related party or a party to a structured agreement (i.e. an agreement which prices the mismatch results into the agreement or which sets the mismatch results as the goal of the agreement), the costs as business expenses are not deductible. In line with ATAD II, the "exit tax" has been levied on tax companies who relocate their place of management, their assets or their business activity outside Hungary to prevent them from avoiding Hungarian tax for the unrealised capital gains at the time of exit from Hungary.

Tax Treaties

Hungary is a signatory to tax treaties with more than 80 countries. In line with OECD guidelines, the treaties grant relief from double taxation, a credit for foreign tax paid or an exemption from foreign income. Particularly favourable tax rates are granted to the source country resident in terms of dividends, interests and royalty payments in transactions carried out between parties of the signatory states. However, as far as corporate income tax is concerned, these favourable tax rates have relevance only regarding inbound royalties/interest given that the domestic Hungarian rules offer an even more favourable position, a tax exemption for dividends and outbound royalties/interests.

The list of nearly all of the countries that have concluded tax treaties with Hungary can be found here: https://en.nav.gov.hu/taxation/double_taxation_treaties.

As of January 2024, the Hungary-USA DTT terminates. In the absence of a bilateral treaty, a state's right to levy tax is unlimited, i.e. it can tax any income or property for which its domestic rules provide. The personal income tax consequences of the termination of the treaty are briefly discussed in the personal income tax section.

Recommendation

VJT & Partners encourages you to contact the firm if you deal with Hungarian taxation issues. Hungarian tax law certainly raises complex legal issues, e.g. preparing transfer pricing documentation or tax reports, or applying for an advance tax ruling, that require the expertise of professional tax consultants. VJT & Partners and its renowned Hungarian tax consultant partner with 25+ years' relevant experience will be happy to assist in solving any such issues.

FAQ

1. How does a company file for tax registration?

A company is subject to tax registration and can only pursue its business activity with a tax number. However, you do not need to apply for tax registration as the Court of Registration automatically transfers the relevant data to the tax authority under the framework of the company registration procedure, and the tax authority automatically generates your tax number.

2. Can a taxpayer obtain a binding advance tax ruling and what is its effect?

A company may ask the Ministry of Finance to issue binding advance tax rulings for future transactions or standard form contracts. The application for a binding advance tax ruling is subject to a fee of HUF 10 million in the case of a standard form contract, HUF 8 million in other cases in general and HUF 12 million for an accelerated procedure. You must be represented by an attorney, a tax adviser or an auditor. This ruling will bind the tax authority in future tax audits (until the end of the fifth tax year following the issuance of the ruling) if there have been no changes in facts, tax regulations or international legal obligations in the meantime.

3. When should a landlord opt for the VAT obligation regarding the letting of real estate properties? How can this choice be reported to the tax authority?

Although the letting of real estate properties is, as a general rule, a VAT-exempt activity, a landlord may still opt for a VAT payment taking into account the following reasons. First of all, a landlord cannot deduct input VAT if they carry out the letting as a VAT-exempt activity. Secondly, the shifted burden of the VAT payment would not financially affect most tenant companies given that a tenant will be able to recover the paid VAT through VAT input deduction.

However, if a tenant is not a VAT payer (e.g. banks, insurance companies), then the tenant cannot reclaim the paid VAT as a deduction of VAT input. In this case, a landlord needs to consider what the better option is:

(i) a VAT payment - meaning a landlord will have the right to deduct VAT input, or

(ii) avoiding the VAT payment - meaning that no VAT will be charged on the rent. If a landlord wants to opt for the VAT obligation, then the tax authority simply needs to be notified by the landlord that they wish to opt for VAT obligations. In this

case, the landlord will be mandatorily subject to VAT from the beginning of the following calendar year (after the end of the year in which the notification was submitted) for five years.

4. Is there a net wealth tax in Hungary?

In Hungary, there is not a net wealth tax (construed as a levy based on the aggregate value of all household holdings including housing, savings, deposits, etc.). Instead, there is a real estate property tax, but only at a local level. Namely, local municipalities can levy local taxes on buildings and lands up to certain statutory ceilings.

5. Is stamp duty (property transfer tax) levied only on direct property acquisitions or also on indirect property acquisitions by share deals?

Yes, under certain conditions indirect property acquisitions by share deals are subject to property transfer tax. Namely, the acquisition of at least 75% in a company owning Hungarian real estate is subject to transfer tax. In this case, general transfer tax rates are applicable (4% up to the market value of HUF 1 billion and 2% for the excess, with a cap limit of HUF 200 million per property).

6. Who may apply for corporate group taxation? What is its main benefit?

Corporate group status will be available to those Hungarian tax-resident companies between whom there is direct or indirect control of at least 75% of the voting rights or a third party has this share of voting rights in them. Moreover, these taxpayers must have the same balance sheet date and prepare the financial reports either according to Chapter III of the Hungarian Accounting Act or according to International Financial Reporting Standards (IFRS).

The main advantage of corporate group taxation is that group members may offset losses and tax incentives against the positive tax base of other group members under certain conditions, and the transfer pricing rules are also simpler among group members.

7. Did Hungary introduce the global minimum tax in line with the new international standards?

Yes, in line with the EU Directive no. 2022/2523 and the OECD Model Rules, Hungary introduced the global minimum to close cross-border tax loopholes in cases of group companies exceeding the revenue threshold of EUR 750 million in at least two of the last four consolidated financial statements of the group's ultimate parent entity. The essence of global minimum tax is if a multinational group's effective tax rate in a given country is below the minimum rate of 15%, it is liable to pay additional tax.

Accounting

This section aims to introduce the basic structure of the Hungarian accounting system. It summarises the general rules and concepts of bookkeeping and financial reporting as well as filing and publication obligations.

General Overview

Hungary's Accounting Act sets out the rules for accounting principles, bookkeeping, financial reporting, as well as disclosure and publication requirements. The Accounting Act is only a framework act and any loopholes that exist are filled in by accounting standards.

Bookkeeping

Bookkeeping is the: (i) keeping of an economic entity's records on a continuous basis of the events occurring during its activity that affect its financial and earnings position, and (ii) closing such records at the end of the business year. In general, companies must do double-entry bookkeeping. Below are some of the most important bookkeeping rules:

- records must be maintained in Hungarian,
- in general, the business year corresponds to the calendar year (see the FAQ section for more details),
- records must be kept in HUF; however, in certain cases, records can be kept in a foreign currency (see the FAQ section for more details), and
- transactions may be recorded only if there is documentation supporting the transaction (e.g. invoices, contracts, certificates or bank statements).

Financial Reporting

All companies must prepare a financial report in Hungarian based on bookkeeping records following the end of each business year. The main types of financial reports are:

- an annual report,
- a simplified annual report,
- a simplified report, and
- a consolidated annual report.

Annual Report

As a general rule, companies that keep double-entry books must prepare an annual report. The annual report must give a true and fair view of the company's actual financial position and earnings, as well as any changes in this position. It must contain:

- all assets, equity, reserves and liabilities (considering all deferred items as well),
- all revenues and expenditures during the relevant period,
- the balance sheet profit or loss figure,
- the data and explanations that are necessary to give a true and fair view of the company's actual financial situation,
- the data and explanations that are necessary to introduce the results of its operation

The annual report is composed of the balance sheet, the profit and loss account and supplementary notes. In addition, a business report must also be prepared simultaneously with the annual report.

In general, supplementary notes contain data and explanations requested by the Accounting Act and additional information (besides for the balance sheet and cash flow) to take a closer look at a true and fair view of the company's assets, liabilities, financial position and results of operations. More specifically, supplementary notes must include the applied accounting policies and the cash flow statement.

The business report is a written evaluation of the annual report's figures. It describes the company's financial position at the end of the business year and the possible prospects of the company's future position.

Simplified annual report

- Companies keeping double-entry books may prepare a simplified annual report if, on the balance sheet date for two consecutive business years, two of the following criteria are met:
- the balance sheet total does not exceed HUF 1,200 million,
- the annual net sales do not exceed HUF 2,400 million, or
- the average number of employees in the company's business year does not exceed 50.

As its name suggests, the simplified annual report differs from the annual report in its length:

- it only needs to contain certain headings of the balance sheet and the profit and loss account as set out in the Accounting Act,
- the data disclosure obligation regarding the supplementary notes are limited, and
- no business report is required.

Simplified report

Companies that are not subject to a compulsory audit (for the scope of the compulsory audit, please see "**Auditing**") may prepare a simplified report if, on the balance sheet date for two consecutive business years, two of the following criteria are met:

- the balance sheet total does not exceed HUF 150 million,
- the annual net sales do not exceed HUF 300 million, or
- the average number of employees in the company's business year does not exceed 10.

The simplified report is even simpler than the simplified annual report. The key principles regarding a simplified report are:

- it only needs to contain certain headings of the balance sheet and the profit and loss account as set out in a special governmental decree,
- no supplementary notes are required, and
- no business report is required.

Consolidated annual report

The general rule is that a parent company exercising a controlling influence over other companies directly or through its subsidiary must prepare a consolidated annual report. For accounting purposes, a controlling influence means:

- control over the majority of the votes (more than 50%) based on ownership,
- control over the majority of the votes (more than 50%) based on an agreement with other owners (shareholders),
- the right to elect or dismiss the majority of the executives or members of the supervisory board, or
- decisive control over the company's operations based on an agreement with the owners (shareholders) or the deed of foundation regardless of the above.

However, a parent company does not have to prepare a consolidated annual report if, on the balance sheet date for two consecutive business years preceding the actual business year, two of the following criteria have been met:

- the balance sheet total does not exceed HUF 6,000 million,
- the annual net sales do not exceed HUF 12,000 million, or
- the average number of employees of the company group in the company's business year does not exceed 250.

The consolidated annual report consists of the consolidated balance sheet, the consolidated profit and loss account and the consolidated supplementary notes. The financial and earning positions of the companies included in the consolidation must be described in the consolidated annual report in such a manner as if the companies

operated as a single company. In that context, any accumulation arising from the intra-company relationships in the consolidated annual report must be eliminated.

Filing and Publication

Companies keeping double-entry books must file and publish the following documents within five months from the balance sheet date of the given business year (in practical terms, by 31 May each year):

- the annual report or simplified annual report (approved by the company's owners),
- (for a compulsory audit) the auditor's report containing the seal of approval or rejection of approval, and
- the resolution on the use of after-tax profits (dividends declared).

The parent company must file and publish the following documents within six months from the balance sheet date of the consolidated annual report:

- the consolidated annual report, and
- the auditor's report containing the seal of approval or rejection of approval.

Both filing and publication requirements are fulfilled by sending the required information in an electronic form to the Company Information Office of the Ministry of Justice.

Recommendation

Each Hungarian company registered with the Hungarian Company Registry must keep accounts and regularly submit an annual report, even if the relevant company is not actively doing business. For this reason, it is important that Hungarian companies engage an accountant to deal with these obligations.

Auditing

This section gives an overview of Hungarian auditing requirements and introduces the basic rules related to engaging auditors.

General Overview

The general rule is that all companies obliged to keep double-entry books must be audited unless:

- the average annual net sales of the company do not exceed HUF 300 million in the last two business years preceding the business year under review, and
- the annual average number of employees in the company does not exceed 50 in the last two business years preceding the business year under review.

It is to be noted that the above exemptions do not apply to certain entities such as branches of foreign companies, companies included in the consolidated annual report, banks and insurance companies. These entities must be audited.

Compulsory audit	Companies keeping double-entry books
Exceptions	• The average annual net sales of the company do not exceed HUF 300 million in the last two business years preceding the business year under review, and • The annual average number of employees in the company does not exceed 50 in the last two business years preceding the business year under review.
Exceptions do not apply and an audit is compulsory	• E.g. branches of foreign companies, companies included in the consolidated annual report, banks and insurance companies.

Auditing Tasks

The main purpose of the audit is to verify if the annual report has been drawn up in accordance with the Accounting Act and provides a true and fair view of the company's financial position, earnings and operations. The audit must also investigate whether there is conformity between the annual report and the business report annexed to it.

Auditor

General practice is to appoint an auditor either when establishing the company or at a later date, but before approving the annual report. The auditor is an individual or a firm that is a member of the Hungarian Chamber of Auditors. If a firm has been appointed, the firm needs to appoint an individual auditor responsible to act on their behalf.

The minimum term for which the auditor is appointed is the period between the date the general meeting appoints an auditor and the date the general meeting adopts the annual report of the given business year.

The main task of an auditor is to prepare a written report about the audit of the annual report, the simplified annual report, or the consolidated annual report. The auditor may either give or refuse its approval.

Apart from this main task, an auditor has the following responsibilities:

- the auditor may review the company's documents (books, accounts, accounting system) and request the company to provide information during the audit,
- the auditor must immediately request the management to take action enabling the owners of the company to make the necessary decisions if: (i) the auditor noticed changes in the company's assets that are likely to jeopardise the company's ability to satisfy any claims against the company, or (ii) the auditor noticed any circumstance entailing the liability of the executive officers or members of the supervisory board,
- the auditor must inform the Court of Registration if the above request was ineffective,
- the auditor must be invited to the general meeting convened to adopt the annual report,
- the auditor may not provide any services for the company or collaborate with the management in a way that may jeopardise their independent status, and
- the auditor may attend the meetings of the supervisory board as an observer and must attend such meetings when requested to do so by the supervisory board.

Recommendation

Auditing has become compulsory for a wide range of businesses. Given the strict rules of auditing, VJT & Partners encourages every company to engage a Hungarian auditor to deal with auditing issues.

FAQ

1. Does the business year necessarily correspond to the calendar year? Is the balance sheet date always 31 December?

In general, the business year is the same as the calendar year and thus, the balance sheet date is usually 31 December. However, companies (except for some special categories, e.g. banks or insurance companies) may opt for a balance sheet date and business year different to the calendar year if this is justified by the nature of their business operations.

2. Can the records be kept in a foreign currency?

In general, the records must be kept in HUF. However, in certain cases, the records can be kept in a foreign currency:

- foreign companies (free zone companies and other companies defined as non-residents under foreign exchange law), European Economic Interest Groupings, European public limited liability companies and European cooperative societies may prepare their annual report and keep their records in the currency defined in their articles of association. Figures must be provided in foreign currency units consistent with the official exchange rates of the Central Bank of Hungary,
- a company may prepare the annual report and keep records in EUR or USD if it defined EUR or USD as the main currency in its articles of association and its accounting policy before the commencement of the given business year, or
- a company may prepare the annual report and keep records in a foreign currency, other than EUR or USD, if altogether more than 25% of revenues and expenditure and more than 25% of financial assets and financial liabilities were generated in the other foreign currency in the given business year and the business year before.

3. Who should prepare the company's annual report or business report?

As a general rule, companies keeping double-entry books are under an obligation to prepare and publish an annual report. To fulfil these obligations, the company must engage a qualified accountant/auditor to prepare the annual report for the company which then has to be signed by the representatives (directors) of the company and approved by the members/shareholders of the relevant company.

The company must also prepare the business report simultaneously with the annual report. However, the engagement of a qualified accountant/auditor is not required to prepare the business report. The company may prepare this on its own.

4. What is the earliest date to issue the final audit report?

The earliest date to issue the audit report is the date when the directors sign the proposed annual report. However, if the general meeting amends the annual report, the auditor needs to prepare a new report.

5. Do Hungarian accounting standards follow international accounting standards?

Yes, Hungarian accounting standards generally follow the standards of the International Federation of Accountants. However, there remain some differences.

Working in Hungary

This chapter provides employers with useful information on the main rules of working in Hungary. It explains under what conditions foreign citizens can be employed in Hungary, what are the main working conditions the employers must ensure for their employees, how employment relationships can be terminated and finally, which rules must be followed if there is a change of employer.

Employment of Foreigners

The rules regarding the employment of foreign citizens differ depending on whether they concern the employment of EEA or third-country citizens.

Rules Regarding EEA Citizens

the employment of EEA citizens is not subject to any permits

Since 1 January 2009, the employment of EEA citizens and their family members are not subject to any permits. However, the employer must notify the competent labour centre of the employment of EEA citizens. It is worth noting that fulfilling the notification obligation is not a prerequisite to establishing an employment relationship or commencing employment itself. Fulfilling this notification obligation is required for labour inspections.

Rules Regarding Non-EEA Citizens

non-EEA citizens can work in Hungary on the basis of a work permit

By comparison with the citizens of the EEA, non-EEA or third-country citizens (with some statutory exceptions) can only be employed in Hungary based on specific permits. The most common type of permits are:

- simple work residence permit,
- guest worker residence permit,
- group work residence permit,
- intra-company transfer residence permit, or
- EU blue card.

In all these cases, the residence permit and work permit are issued in a unified procedure within 70 days as from filing the application. In other words, these permits include both residence and work permits.

Some statutory exemptions exist where a work permit is not required, e.g. permanent residency status or work by a foreign national who is an executive officer or a member of the supervisory board in a foreign-owned Hungarian company. In other cases, a work permit is required but without conducting the labour market test, e.g. in

case of employment of certain key employees (not qualifying as executive officers) or when the total number of foreign employees does not exceed 20% of the total workforce of the foreign-owned Hungarian company.

Simple work residence permit

This the most common type of work permit for blue-collar workers. The permit is valid for 2 years + renewable for a further 1 year. After the first 3-year period, the permit may be renewed again for 2 years (+ a further 1 year upon the expiry of the 2-year period) or upgraded to EU permanent residence card after continuously living in Hungary for 5 years.

Guest worker residence permit

This is another type of permit for blue collar workers available in cases of certain privileged employers (e.g. national strategic investors or strategic partners of the Hungarian government or companies participating in the Exporter Partnership Program) or a qualified Hungarian temporary employment agency.

The permit is valid for 2 years + renewable for a further 1 year. After the first 3-year period, the permit may be renewed again for 2 years (+ a further 1 year upon the expiry of the 2-year period) or upgraded to EU permanent residence card after continuously living in Hungary for 5 years.

The benefit of this option is that the labour market test may be conducted in an expedited procedure within 7 days.

Group work residence permit

A group work permit is available when the employer is in partnership with the Minister for Foreign Economic Affairs to complete an investment project. Such an employer may submit a prior group employment authorisation request which makes the onboarding of larger groups of employees much simpler. This type of permit may be issued up to completing the investment, but maximum of 3 years.

Intra-company transfer permit

The intra-company transfer (ICT) permit is available for white collar workers if the third-country company and the Hungarian host company belong to the same company group.

In general, the ICT permit is valid for a maximum of 3 years (except in case of trainees when it is valid for a maximum 1 year). The ICT permit is renewable and may be upgraded into permanent residency after continuously living in Hungary for 3 years.

If the employee has an ICT permit issued by another EU member state:

- the employee may stay in Hungary for a maximum of 90 days, and

- the employee may work at the Hungarian host company without requiring specific
- permission to do so.

EU Blue Card

The EU Blue Card is used to employ third-country citizens with high qualifications. The EU Blue Card has a double function. The EU Blue Card is valid for a maximum of 4 years and can be renewed and upgraded into permanent residency after continuously living in Hungary for 3 years.

Work Conditions

Employment Contracts

Formal requirements

requirements of an employment contract

In Hungary, a written employment contract must be concluded to enter into an employment relationship. Simply put, if it comes to getting engaged in an employment relationship, at all times and under all circumstances, the employer and the employee must sign an employment contract.

It is the employer's responsibility to propose an employment contract in writing. Failing to do so may result in the employment contract being declared invalid upon the employee's request within 30 days from the start of their employment.

Mandatory content and guidelines

The parties to the employment contract must, by all means, agree both on the personal base wage and the job title of the employee. These terms are mandatory under Hungarian labour law.

If the parties fail to provide for a place of work, the place that is usual for the work position will be the place of work. If the parties do not provide for the duration of the employment contract, it is deemed to be for an indefinite period. Should the parties wish to establish an employment relationship for a definite period of time, this must be specifically set out in the employment contract. The term of a fixed-term employment relationship may not exceed 5 years (inclusive of any extension). If the employ-

Note • The EU Blue Card is an EU-wide work and residence permit used to employ highly educated third-country citizens. As a general rule after 18 months the applicant may move to a different EU country to work in highly skilled employment. .

ment contract contains no indication of the starting date of employment, this date is the day following the conclusion of the employment contract.

Besides the above mandatory elements, the parties may set any other provisions they wish to provide for in the employment contract, as long as the provisions are not in violation of statutory labour regulations.

It is worth noting that the labour authorities may inspect whether the mandatory formalities and content have been complied with.

Working Hours

Full-time / part-time

The whole duration of the work, from start to end, including any preparatory and concluding activity (e.g. the opening or closing of a store), qualifies as "working hours". However, the duration of breaks or the time spent commuting are typically not included. In general, full-time daily working hours are a total of 8 hours per day.

The employee and the employer are allowed to agree on part-time employment in the employment contract, setting shorter daily working hours than commonly applicable to the given position. Remuneration for part-time work is usually paid on a pro-rata basis.

Scheduling working hours

scheduling working hours

It is the employer who determines the schedule of working hours. In general, working hours are scheduled and allocated for weekdays, Monday to Friday.

The schedule of working hours may be unequal, meaning that working hours may be scheduled either for every weekday or just for some of them but in an unequal way. Employers have access to various tools under Hungarian labour law to put an unequal working hours' schedule into practice.

The primary tool is called a "working time framework", in which a longer time period serves as a basis for setting the working hours of the employee. In a working time framework, the employee does not perform the required daily working hours every working day, but in the average specified in the working time framework. If, for example, more work is anticipated on a certain day, the employee works longer hours; these then can be counterbalanced by a shorter working day when there is less work to be done.

In this system, the amount of work can be allocated according to the employer's actual needs and requirements. Applying a working time framework is also beneficial for the employer, since overtime work and its remuneration may be avoided.

The working time framework is of a static nature, its starting and ending date as well as its duration must be set by the employer. The duration is generally 4 months or 16 weeks that may be extended to 6 months or 26 weeks in certain cases. Objective technical or work organisational issues may justify setting a 36-month working time framework in the collective bargaining agreement.

The other notable tool for scheduling uneven working hours is the "settlement period". If no working time framework is applied, the employer may schedule the normal weekly working hours in such a way that the employee may perform the normal working hours of the given week allocated over a longer period. The duration of this period is regulated in the same way as for the working time framework. So, in general, it may be a maximum of 4 months or 16 weeks, or 6 months or 26 weeks in certain cases, and technical or work organisational issues may justify setting a 36-month settlement period in the collective bargaining agreement. In practice, each week, a new settlement period commences on a rolling basis in contrast to the static nature of the working time framework which has a defined end.

In general, under Hungarian labour law, the scheduled daily working hours need to be longer than 4 hours (except for part-time employment) but no longer than 12 hours. The maximum amount of weekly working hours is 48 hours.

An employee may be entitled to freely determine and develop their own flexible working schedule. This may be in writing either in the employment contract or in a written statement from the employer. It is crucial that the inherent nature of the employer's activity must allow the employee to schedule and organise their working hours. In this case, no overtime pay differential needs to be paid.

Employers with special operation schedules

Certain employers' businesses may require them to operate according to an unconventional schedule. This includes employers who also need to operate on Sundays, e.g. due to customary local requirements, as well as employers who cannot stop their operations, e.g. public utilities. These employers are subject to rules allowing a more flexible scheduling of working hours.

Working inconvenient and unsociable hours

To protect employees, certain limitations are imposed on employers when scheduling inconvenient working hours, e.g. at night, on Sundays or on official holidays. Employees in these situations are entitled to receive extra remuneration.

Performing work between 10 p.m. and 6 a.m. is deemed "night work" under Hungarian labour law. It is prohibited to schedule night work for an employee:

- from the date of her pregnancy being diagnosed until the child reaches the age of three,
- who is a single parent raising a child who is under three years of age, or
- who is under 18 years of age.

Main allowance types

Night work with a duration of more than an hour (between 10 p.m. and 6 a.m.) entitles the employee to a 15% night allowance on top of their base wage (except if the employee is entitled to shift allowance).

Employees working between 6 p.m. and 6 a.m. are entitled to a 30% shift allowance if the starting date of their scheduled daily working hours varies regularly.

Employers providing essential services to the public or, by nature, operating on Sunday may order employees to work on Sunday as normal working hours. In many cases, employees working on Sunday are entitled to a 50% extra allowance.

Employers must pay employees a 100% official holiday allowance for working on official holidays as normal working hours.

Working hours different than originally scheduled, as well as working more hours than established in the working time framework or the settlement period, are deemed overtime working hours under Hungarian labour law. To protect employees, the yearly statutory upper limit of overtime is 250 hours; this may be increased by a collective bargaining agreement to 300 hours. Apart from the general overtime limit, the employer and the employee may agree on a further 150-hour overtime limit (or, if the general overtime limit is increased to 300 hours by collective bargaining agreement, a further 100 hours). In certain categories of overtime work (working more hours than originally scheduled for a given day) employees are entitled to a 50% overtime allowance or time-off.

Employees working on stand-by duty at or outside their workplace are eligible for a 20% or 40% allowance.

Work-life balance

Employees are entitled to holiday leave. Holiday leave in Hungary is divided into basic and extra holiday due in each calendar year and is calculated based on the time the employee spends in work in the given year. The basic holiday leave is currently 20 working days in Hungary. Eligibility for extra vacation is subject to the employee's age and the number of their children under 16 years of age. Holiday leave (including extra holiday) must be used in the year for which it is due excluding parental and paternity leave. However, the parties may agree (only for a given calendar year) that extra holiday leave based on the employee's age can be used by the end of the year following the year in which the extra holiday leave was originally due.

Maternity leave is an uninterrupted 24-week period in Hungary, starting a maximum of 4 weeks prior to the expected due date unless both parties agree otherwise.

In the event of the birth of a child, the father is entitled to 10 working days' paternity leave by the end of the second month following the birth of the child at the latest.

Employees shall be entitled to 44 working days' parental leave up to the age of three. The employee may request a change of place of work and scheduling of working hours, teleworking or part-time work until their child reaches the age of 8, except during the first 6 months of the employment.

A parental allowance is paid to eligible employees on parental leave.

Remuneration of Employees

All employees must be treated equally when it comes to any sort of remuneration for work. The following individual circumstances of the employee may serve as a basis to differentiate in terms of remuneration:

rules regarding the remuneration of employees

- the nature, quality and the amount of work performed,
- the working conditions,
- the required professional qualification and prior professional experience of the
- employee,
- the physical or intellectual efforts made by the employee, or
- the responsibilities of the employee in the given position.

The base salary may be specified either on a time (month/week/hour) or a performance basis or may be a combination of the two. When the base salary is exclusively based on performance, a guaranteed salary equivalent to half of the base salary must be established as a minimum.

Currently, in Hungary, the minimum base salary is HUF 266,800 per month for employees working full time. If a degree is set as a minimum prerequisite for employment in a certain position, the minimum base salary is HUF 326,000 monthly.

The basis of calculating wage supplements (e.g. for night or Sunday work) may be agreed upon between the employer and the employee. In the absence of an agreement, the base salary will be the basis of the calculation. The parties may also decide to fix the base salary initially by taking into account and replacing all wage supplements or provide for a lump sum monthly compensation for wage supplements on top of the base salary.

How can VJT & Partners help?

The Hungarian labour authority may screen and carry out an inspection at any em- ployer, focusing on employment contracts and compliance with the rules related to work- ing hours and remuneration. To avoid high and extra costs that the employer may incur, VJT & Partners can support the development of a cost-effective working hours schedule and find the appropriate operation form best serving the employers' needs. Non- compliance with statutory labour law, in general, may result in paying a large amount of money enforced by the courts. VJT & Partners is highly ranked by international directories in employment law and provides valuable support to its clients regarding labour issues.

Termination of Employment

summary of terminating an employment relationship

An employment relationship can be terminated:

(i) by the mutual agreement of the parties,

(ii) by giving notice, or

(iii) with immediate effect.

Any statement aiming to terminate employment must be in writing. Non-compliance with this requirement results in unlawful termination and a heavy compensation obligation for the employer.

Termination of the Employment Relationship by Mutual Agreement

Termination of the employment relationship by the mutual agreement of both parties is a more amicable way of terminating an employment relationship than termination by notice or termination with immediate effect, and enables the parties to fully settle any claims they have or may have against each other in the future. Therefore, if there is a way, it is advisable to terminate the employment relationship by mutual agreement to eliminate uncertainties regarding potential employee claims after termination.

The employer and the employee can decide to terminate the employment relationship by mutual agreement at any time. Both fixed and indefinite term employment relationships can be terminated by mutual agreement. The parties can agree on any issues related to the termination of the employment relationship.

Termination by Giving Notice

The employment relationship can be terminated with notice both by the employer and the employee. Please note that the Labour Code protects certain groups of employees by offering both prohibitions and restrictions for termination. The protec- tion under the Labour Code means that the employment relationship (i) of certain employees, e.g. pregnant women, women on maternity leave, employees performing volunteer reserve military service, etc. cannot be terminated, or (ii) can be terminated based on very limited grounds, e.g. when attempting to end the employment of employees 5 years prior to the state retirement age.

the reason of the termination must be clear, true and causal

The employer must give reasons for the termination, except if the employee is a pensioner or an executive employee. The reason must be clear, true and justify the termination. It is also worth noting that the employer bears the burden of proof pertaining to the reasons for the termination. The reason for termination with notice can only be connected to:

- the employment-related behaviour of the employee,
- the skills of the employee, or
- the operations of the employer.

A change in the employer itself cannot serve as a reason for termination (see, "**Transfer of an Undertaking**").

Please note that the reasoning in the termination notice is crucial considering that at least half of the cases before the labour courts are about improper justifications that may result in the whole termination being declared void. Therefore, it is advisable to consult an attorney-at-law regarding the possibility and the proper reasoning for terminating before serving a termination notice.

Termination with Immediate Effect

Both the employer and the employee can terminate the employment relationship with immediate effect if the other party either deliberately or with gross negligence, materially breaches a significant employment obligation or behaves in a way that makes maintaining the employment relationship impossible.

An employment relationship may be terminated with immediate effect within 15 days from becoming aware of the grounds but, in any case, within 1 year from the event justifying the termination.

Both the employer and the employee can terminate the employment relationship generally without formal reasoning with immediate effect during the trial period of employment. The employer can also terminate the fixed-term employment contract without explanation and with immediate effect, but with the obligation to compensate the employee for their salary for the unserved period. This compensation is subject to a cap of 12 months' absentee pay. (Absentee pay is the average of the monthly base salary, any lump sum wage supplements and any performance fee, overtime, shift or other allowances paid during the 6-month period.)

Consequences of an Employment Relationship being Unlawfully Terminated

If the employer terminates the employment relationship unlawfully, the employee may claim compensation for damages. Compensation includes compensation for loss of income (which may be up to 12 months' absentee pay and in certain cases, severance pay). Instead of the compensation above, the employee may claim absentee pay for the notice period that would apply to them. In certain cases, the employee can also request their reinstatement.

Due to the serious consequences of unlawful termination, it is highly recommended to consult an attorney-at-law regarding both the possibility and justification of termination.

Transfer of an Undertaking

Definition of a "Transfer of an Undertaking"

Change of employer

Current Hungarian legal regulations regarding a change in employer comply with the EU's harmonisation requirements, in particular, Directive 2001/23/EC. A change in employer results from the contractual transfer of a business unit to continue or relaunch the business operation. (The labour law term "transfer of an undertaking" refers to this transfer of a business unit.) The transfer may take place, i.a. via sale and

purchase, exchange, lease, the formation of a new business corporation or entry into an already existing business corporation. Please note that the transfer of assets is not a precondition for a transfer of an undertaking to take place; and the transfer of certain tasks or clients may also constitute a transfer of undertaking.

For labour law, a change in employer (transfer of an undertaking) in itself has no effect on the employment relationship of the employees concerned and does not amend employment contracts or relationships. However, any other change in the terms of the employment will require the employment contract to be amended. Also, the new employer automatically (and by virtue of law) takes over all employment-related rights and obligations of the previous employer regarding the employees concerned. This includes the rights and obligations under any non-competition and educational assistance agreements. Employees on unpaid leave engaged in the business unit that is being transferred are also subject to the transfer of undertaking.

Termination Associated with the Transfer of an Undertaking

The new employer is not allowed to terminate the employee's employment based on the transfer of an undertaking alone.

However, a change in the employer can be detrimental to the employee, e.g. work conditions may change unfavourably to a disproportionate extent. In these cases, the employee is allowed to terminate employment and will have the right to all entitlements that would be due if the employment was terminated by the employer with notice with a reason connected to the employer's operations. The employee must justify this decision and must be able to evidence their reasons. This one-time opportunity is available to the employee within 30 days from the date of the transfer of the undertaking.

Employee claims

The previous employer will remain jointly and severally liable with the new employer for the employee's claims from before the transfer of the undertaking. Therefore, the employee may still enforce a claim at their discretion against either of the employers within one year from the date of the transfer of the undertaking.

Notification and Consultation Requirements

Prior to the date of the transfer of an undertaking, the previous employer must inform the new employer of the rights and obligations concerning the employees affected by the transfer. Both the previous and the new employer must inform the works council about the proposed transfer 15 days before the transfer at the latest and must engage in negotiations with the works council concerning the proposed measures affecting the employees. If a works council does not operate at the previous employer, the employees themselves must be notified in writing by the previous employer or, based on the agreement between the employers, by the new employer. On the day of

the effective date of the undertaking's transfer, the new employer must notify all affected employees of the change of employer and whether there has been any change to certain working conditions (e.g. daily working hours). The employer's failure to meet its notification and consultation obligations will allow the works council to start proceedings within 5 days on the grounds that their interests have been violated. The court will then establish whether the works council's rights have been violated, but this will not affect the validity of the transfer.

As the very first step of a transfer of an undertaking, the employer must, before deciding whether to implement the transfer of the undertaking, ask for the works council's view on the project.

A trade union is also entitled to express its ideas and judgments regarding the proposed transfer of the undertaking and, to this effect, has the right to invite the employer for consultations.

How can VJT & Partners help?

VJT & Partners has gained substantial experience in supporting transfers of undertaking from the very first step. Given the numerous mandatory requirements that must be followed throughout the transfer, it is strongly advised to engage an experienced law firm.

FAQ

1. Do EU citizens need a work permit to perform work in Hungary?

No. Only the citizens of third countries, i.e. citizens of non-EEA countries, need a work permit.

2. How long does processing a work permit take?

As a general rule, it takes 70 days but this also depends on the type of permit applied for.

3. As an employer, what should I observe when terminating employment?

The employer needs to consider the following:

- the termination must be made by the person exercising the employer's rights over the given employee or this must be approved by the person exercising the employer's rights,
- the termination must be in writing,
- the termination with notice and the termination with immediate effect become effective when delivered to the employee,
- the employer must give clear, true and valid reasons for the termination,

- the termination (except for termination by mutual agreement) must state the employee's right to challenge the termination, and
- the employer must observe the prohibitions and restrictions regarding the termination of an employment relationship protecting certain employee groups (see, "**Termination of Employment**" - "**Termination by Giving Notice**").

4. Are employees entitled to unpaid leave?

Yes. The employee has the statutory right to unpaid leave if the leave is to care for either the employee's child under a certain age, the employee's relative or to undertake voluntary military service.

Unpaid leave may also be granted at any time to an employee at the employer's discretion or may also be refused without justification.

5. Can I agree on more commercial terms with executive employees?

Parties to an executive employment contract enjoy considerable flexibility when setting the terms of the employment contract.

When drafting the terms of the executive employee's employment contract, the parties are allowed to deviate from almost any rule of the Labour Code both in and against the interests of the executive employee. Executive employees are not subject to collective bargaining agreements.

6. For how long can I put my employee on a trial period?

A trial period cannot be longer than 3 months. If shorter, the trial period may be extended once, but altogether it may not exceed 3 months. The duration of the trial period shall be fixed on a pro rata basis for employment contracts of up to 12 months. Example: if someone is hired for 3 months, a quarter of the 3 months (23 days) may be the trial period.

7. What do I need to consider if I would like my employee to agree to a non-competition clause?

If justified by the employee's position, either a special clause providing for a non-competition covenant may be inserted into the employment contract or a separate non-competition agreement may be entered into between the employer and the employee. Employees undertaking non-competition covenants must abstain from engaging in any matter jeopardising or violating the employer's rightful economic interests for a maximum of 2 years following the termination of the employment relationship. The employee is entitled to consideration in return for compliance with the non-competition covenant. This must be at least one-third of the employee's base salary that would be payable for the term of the non-competition undertaking if spent in em- ployment.

8. Does a change in the employer's ownership mean a change of employer?

No. The change in the employer's ownership does not fall under the regime of a transfer of undertakings from the labour law perspective.

Financing Matters

This chapter aims to summarise various financial issues, e.g. how to secure bank credit in Hungary, whether there are any obstacles to repatriating profits realised in Hungary and the incentives for investment that the Government ensures. Additionally, in this chapter, we also briefly introduce the possible implications of insolvency, e.g. bankruptcy and liquidation procedures.

Access to Finance

In Hungary, there is a diverse range of financing options available. In general, any business seeking to raise capital is required to prepare a solid business plan including a brief description of the business, as well as an operating plan and a financial plan. Businesses are also required to submit a credit report and offer certain collateral (for more information about the main types of collateral, see our FAQ). However, despite the broad range of financial sources, it is to be noted that, in the last decade, credit conditions have continually tightened and the availability of financing has reduced for many businesses, e.g. requiring higher equity, higher margins, etc. As a result, the importance of state financial support for companies has increased (more information about these programs can be found below).

Credit

Overview of Credit

Bank loan vs bank credit

The most popular type of financing is bank credit but there are some alternative sources; for these, please see our FAQ. When companies apply for credit, banks usually run a full credit check. This involves the analysis of the companies' entire financial status (for more information regarding the credit check process, see our FAQ).

To understand the nature of credit, it is important to clarify the difference between a bank loan and bank credit. A bank loan means that a bank actually lends money to a client who has to pay it back with interest within a predetermined period of time. On the other hand, bank credit means that the bank holds a "credit line" at the client's disposal which then turns into a bank loan once the client makes a drawdown request. The bank charges a fee to keep the facility amount available until it is drawn down.

There are several types of bank credit available to companies. Usually, long-term credit with security has a lower interest rate and short-term credit without security has a higher interest rate. Generally, Hungarian banks are familiar with all kinds of modern banking products, including overdraft facilities, working capital credit, project financing, Lombard credit or syndicated credit.

Funding of SMEs

Today, in a time of stringent credit conditions, access to credit is particularly difficult for micro-, small- and medium-sized enterprises ("SMEs"). Therefore, the Hungarian Central Bank has launched several lending schemes that aim to restore the functioning of the SME loan market (for more information regarding which enterprises can qualify as an SME, see our FAQ). SMEs registered in Hungary with small credit needs can apply for credit through these programmes, which aim to give financial support to SMEs.

State Financial Support Framework

The state gives financial support directly to companies through tenders or via individual governmental decision (for more information about individual government decisions, see "Incentives for Investment"). The EU, through the European structural and investment funds, provides a source of state aid. The EU supports predetermined Operational Programmes within the framework of its regional policy, for which member state governments can apply by submitting a project plan to the European Commission. The companies may be eligible for direct state aid from the government if their business plan covers at least one area contained in the Operational Programmes, such as creating new jobs or R&D.

How can VJT & Partners help?

We have a broad range of experience in financial matters. We provide legal advice to corporate clients about financing and refinancing asset purchases and business expansion. In particular, we have expertise in structuring, drafting and executing complex collateral structures required for cross-border and domestic financing transactions over borrowers' assets in Hungary. Therefore, we encourage you to contact us when any kind of financing matters arise.

Repatriation of Profit, Withholding Tax

Act XXIV of 1988 on the investment of foreigners in Hungary grants full protection to the investments of foreign investors; namely, it guarantees that foreign investors are treated in the same manner as domestic investors (taking into consideration the rules of national security screening relating to certain sectors of national security interest, see "National security screening of foreign investments"). Note that there are no laws in force in Hungary preventing the repatriation of profit realised by foreign investors in Hungary. Also, there is no withholding tax on dividends, interest or royalty paid by a Hungarian company to a foreign company.

Incentives for Investment

non-refundable subsidies and other incentives

As foreign investments are crucial for Hungary's economic development, Hungary provides investors with a wide range of possible financial state assistance. This section offers a short overview of the main forms of financial support an investor might count on when investing in Hungary (for information on EU co-financed tenders, see "**Access to Finance"**.)

Subsidy Based on the Government's Individual Decisions

The Hungarian budget provides investors with a relatively flexible type of non-refundable subsidy based on individual government decisions.

The incentive scheme's primary goal is to give investors who are considering start-up investments in Hungary access to resources. The scheme covers, i.a. prospective research and development, competitive production, high value-added services, shared service centres and tourism industry-related investments.

The individual character of the decision means that the final decision in each case depends on individual government decisions.

General rules applicable to obtaining a subsidy based on the government's individual decision

Who can apply?

The following may apply for these resources: an economic entity, a European limited company by shares or a European Cooperative with a registered seat, permanent establishment or a branch office in Hungary.

Aims of the subsidy

These resources may be used for the following main purposes:

- an initial investment for SMEs and large companies to perform a new economic activity, and
- an initial investment for job creation.

An applicant has to meet basic criteria, e.g. the number of new jobs to be created and a specific amount of eligible costs:

- the minimum number of new jobs to be created is 50, and
- the minimum amount of eligible costs needed varies between EUR 5 million and 10 million (depending on other conditions).

However, for the R&D sector, more favourable conditions apply (the number of jobs to be created is only 10, and eligible costs start from EUR 1 million).

Although it is based on an individual government decision, there are specific terms that determine the maximum amount of aggregated state subsidy that an applicant may receive. This is called "an intensity ratio" and depends on the following factors:

- the eligible expenditure of the investment,
- the size of the enterprise, and
- the development level of the region where the investment will be implemented.

This last factor means that the more developed a region is, the lower the intensity ratio will be. For example, the intensity ratio in Baranya county, Borsod-Abaúj-Zemplén county and Heves county is 60%, it is 50% in Central Hungary, Northern Hungary, the Great Plain and in Southern Transdanubia, while it is 30% in Central and Western Transdanubia.

The situation of Central Hungary is unusual because, from 1 July 2014, regional aid is no longer available in Budapest. However, outside Budapest, in Central Hungary, from 2022, there is an intensity ratio of 50%.

Hungarian Investment Promotion Agency and the method of application

To obtain the subsidy, the first step is to start negotiations with the respective government institution – the Hungarian Investment Promotion Agency ("HIPA"). The applicant must submit a notification containing all the relevant core investment information to HIPA. The investor and the government must also conclude an agreement on the exact terms of the subsidy disbursement. For HIPA's contact information, please visit the following website: https://hipa.hu/main#contact_us.

Tax Allowance for Development

Hungary further supports investment by providing investors with tax allowances in the form of a reduced corporate tax obligation. The investor is eligible for a tax allowance for up to 13 years and, according to a general limitation, the tax allowance may result in corporate income tax being reduced by 80%.

To qualify for the tax allowance, the investment must be a start-up investment that is:

- carried out by a SME, or
- carried out by a large business in the planning and statistical regions of Northern Hungary, the Northern Great Plain, the Southern Great Plain, Southern Transdanubia, Central Transdanubia, Western Transdanubia or Pest.

Investors may be entitled to a tax allowance for:

- investments of a value equal to or exceeding HUF 3 billion,

- investments of a value equal to or exceeding HUF 1 billion if the investment is realised in the territory of a supported local community,
- investments that create new jobs,
- investments made by SMEs of a value equal to or exceeding HUF 50 million for small-sized and HUF 100 million for medium-sized enterprises if the investment creates a new facility or results in a new method of service,
- an investment of strategic importance for the transition to a net zero-emission economy,
- investments of a value equal to or exceeding HUF 100 million within a special scope determined by law.

The job employment level needs to be maintained for at least four years in some cases.

The application for a tax allowance must be submitted to the Minister of Finance.

Other Employment-Related Forms of Incentives

There are also other types of incentives related to employment issues, e.g.:

- wage support promoting the employment of the disabled,
- training subsidies,
- subsidies to expand employment, and
- regional investment and employment subsidies.

How can VJT & Partners help here?

Our law firm is keen to provide you with information regarding the legal details and precise requirements of the state support mentioned above. We are happy to assist you through the whole procedure, starting with contacting the respective government offices, all the way through to the end of the monitoring processes.

Insolvency: Bankruptcy, Liquidation and Fraudulent Conveyance

procedures to follow in the case of insolvency

Insolvency is the situation when a company is unable to pay its debts. Insolvency creates a risk situation for the debtor, creditor and for virtually all of the players in the relevant market. Bankruptcy and liquidation are procedures aimed at balancing the interests of these participants. These rules are supplemented with special provisions in Hungarian law against fraudulent conveyance and the liability of the CEOs and the owners of the debtor. This section provides you with basic information in this area.

Insolvency

Legally speaking, insolvency is established by the court in the following situations, i.a.:

- the debtor failed to pay its undisputed debt within a certain period of time,
- the debtor failed to pay its debt established in a court order,
- the enforcement procedure against the debtor was unsuccessful, or
- the debtor failed to pay its obligations following a settlement in a bankruptcy or liquidation procedure.

Bankruptcy Proceeding

In a bankruptcy proceeding, the debtor applies for a moratorium at the court to gain time to restructure its debts by concluding a settlement with its creditors and thus improve its financial condition. Generally, during the moratorium period, the debtor is relieved of its payment obligations.

If the court grants the moratorium on the payment of the debtor's debts, within a 180-day period the debtor may try to conclude a settlement with creditors. The settlement, if concluded, still needs the court's approval. If the debtor and creditors cannot reach a settlement, the bankruptcy proceedings turn into liquidation proceedings.

Liquidation

Liquidation proceedings take place when the court establishes the debtor's insolvency. Liquidation aims to distribute the debtor's remaining assets among the creditors and terminate the debtor as an entity.

When the court establishes the debtor's insolvency, it orders the commencement of the liquidation, appoints a liquidator and calls upon the creditors to file their claims against the debtor within 40 days of the publication of the liquidation decision, but no later than 180 days. With the appointment of the liquidator, the owners lose their right to make strategic decisions regarding the debtor company. The debtor's CEO has to hand over management to the liquidator. The liquidator must enforce the claims of the debtor against third persons and publicly sell the debtor's assets at the highest price available on the market. The proceeding ends with the order of the court which decides on the distribution of the assets and proceeds to satisfy the creditors as much as it is possible (the distribution follows a strict order of satisfying creditors according to categories that are determined by law) and terminates the debtor as an entity.

Fraudulent Conveyance and Liability of the CEOs and Owners of the Debtor

Hungarian law sets forth special provisions to protect the creditors' interests.

Under certain conditions, the creditor or the liquidator may challenge before the court the debtor's agreements concluded before the starting day of the liquidation and the fraudulent transfer of the debtor's assets that aims to prevent the satisfaction of the creditors.

Hungarian law also has a wrongful trading rule. During the liquidation process, in court, the creditor or the liquidator may try to establish the liability of the debtor's CEO for their wrongful actions against the creditors' best interest. If the court establishes the CEO's liability, the creditor may file a separate lawsuit against the CEO to satisfy its claim.

If the owner, having at least 75% of the votes in the debtor company pursues a permanently disadvantageous business strategy regarding the debtor company, the court may establish the unlimited liability of the owner for the debts of the debtor company.

How can VJT & Partners help here?

Our law firm has represented both debtors and creditors in all kinds of proceedings (including litigation) in connection with insolvency, e.g. drafting a payment notice, filing the creditor's claim with the liquidator, etc. We can also represent your company before the court regarding fraudulent conveyance issues.

FAQ

1. Why should you lease instead of using credit?

Leasing is considered to be a preferential method of financing, in particular regarding asset financing. In contrast to credit, the main advantage of leasing is that the lender simply retains its title to the leased asset and thus, often no additional collateral is required apart from the leased asset. On the other hand, the main disadvantage of this form of financing is that, in contrast to credit, the borrower becomes the owner of the financed asset only after the whole outstanding amount of debt has been paid.

2. Why use factoring instead of credit?

Factoring is an alternative method of financing commonly used to finance sales. In this transaction, the company, as a supplier, assigns receivables to the factor from the sale transaction at a discount. It can be a preferential method of financing for the

company given that the company may have access to factoring even when it does not have access to credit. In the first place, the factor examines the creditworthiness of the buyer/debtor and not the supplier. Furthermore, factoring can be carried on continuously which can be a good base for working capital financing. However, the disadvantage of factoring is that it can be rather costly (given the discounts, bonuses and other costs charged by the factor).

3. What kinds of collateral are usually required? What are the basic rules?

Although financial resources differ regarding the required collateral, the following kinds of collateral are "popular":

- a mortgage on real estate – the encumbered real property will remain in the borrower's possession. The security agreement needs to be concluded in writing. A mortgage needs to be registered in the land registry,
- a pledge on movables – to create a pledge on movables, it is necessary to conclude the agreement in writing in the form of a notarial deed. If the movable is registered in a pubic register, i.e. an aircraft or a ship, then the pledge over this movable must be registered in the respective public register as well. A pledge over movables not registered in any public registers must be registered in the security interest register maintained by the Hungarian Chamber of Public Notaries. The movable will remain in the ownership and possession of the pledger,
- a possessory lien on movables – to create a possessory lien on movables, in addition to signing the pledge agreement, the pledger needs to place the movable into the possession of the pledgee,
- a lien on a business share, i.e. shares in a kft. – the shares in a company can be encumbered by a lien. A pledge agreement needs to be concluded and the lien on the business share (including the data of the lien holder) must be registered in the company registry by the court,
- a security deposit – a security deposit is created by concluding a security agreement that secures the claim mainly in the form of cash, bank accounts and securities and handing over the collateral to the secured creditor. The secured creditor is entitled to satisfy its claim directly from the security deposit. A security deposit is often used as collateral for Lombard credit.

4. What kind of enterprises are covered under the definition of SMEs?

In general, under the SMEs framework, Hungarian law distinguishes between the following types of enterprises:

- Micro-enterprises – a micro-enterprise is an enterprise that has less than 10 employees and the annual net turnover or the annual balance sheet total does not exceed the HUF equivalent of EUR 2 million,
- Small enterprises – a small enterprise is an enterprise that has less than 50 employees and the annual net turnover or the annual balance sheet total does not exceed the HUF equivalent of EUR 10 million, and

- Medium-sized enterprises – a medium-sized enterprise is an enterprise that employs between 50 to 249 employees and the annual net turnover does not exceed the HUF equivalent of EUR 50 million or the annual balance sheet total does not exceed the HUF equivalent of EUR 43 million.

5. What is the process of granting credit/a loan?

The process of granting credit involves the following:

1. A company has to submit a written application for credit to the relevant bank. The application has to contain the following:
   - the purpose and amount of the credit,
   - the proposed collateral,
   - the annual financial reports for the last 2-3 years, and
   - a business plan.
2. Upon receipt, the bank assesses the application and examines the formal requirements of the application. Resubmission is allowed if a formal error is made in the application.
3. A risk assessment of the company in which the company's creditworthiness is examined. In Hungary, banks and other credit institutions use the Central Credit Information System to identify companies with a bad credit history.
4. A credit assessment of the company takes place in which the bank examines whether the credit application is adequately underpinned by financial and economic factors.
5. The bank officer dealing with the application submits a summary of the application to the censure committee.
6. The censure committee decides on the merit of the application.
7. The bank lends money or holds a credit line at the company's disposal.
8. Credit monitoring occurs where the credit institution carries out continuous reassessment on the company's creditworthiness and if necessary, it modifies the terms and conditions of the credit agreement or withdraws from it.

6. Are any areas or companies excluded from the scope of the subsidy based on the individual decision of the government?

Specific investment areas are excluded from the scope of the subsidy, e.g. the shipbuilding industry, coal industry or companies that are facing financial difficulties or are under liquidation.

7. What does "start-up investment" exactly mean in the sense of the laws regulating subsidies based on the Government's individual decision?

A start-up investment is an investment into assets or immaterial goods in connection with:

- setting up new facilities,

- improving existing facilities,
- diversifying the product range of the facilities by adding a new product,
- fundamentally changing the whole production process of existing facilities, or
- acquiring, by a third-party investor, the assets of an establishment which has been or would have been closed.

8. What kind of investments with an investment value of at least HUF 100 million may be eligible for tax allowances?

Investments eligible for this type of tax allowance include independent environmental investments or investments in the film industry, research and development or food hygiene (with further special conditions to be fulfilled).

9. The investor might be eligible for corporate tax allowance for up to 13 years. Which will be the first year relieved by the tax allowance?

The first year affected by the allowance will be the tax year following the operational date of the investment.

10. How much does it cost for a creditor to report its claim to the liquidator in a liquidation process?

In general, the claim registration cost is 1% of the value of the claim (minimum HUF 5,000, maximum HUF 200,000).

11. From which date may the CEO's actions be deemed as wrongful trading? What are the particulars of such actions?

The wrongful trading rule may apply to the CEO's actions taken while a situation threatening insolvency exists. A situation threatening insolvency occurs when the CEO could reasonably foresee that their company will not be able to pay its debts in due time. From such day, the CEO is required to act primarily in the best interests of the creditors instead of those of the company. Breaching this obligation may establish the wrongful trading liability of a CEO.

12. Is the liquidator liable for the damages caused by its actions?

The liquidator must act with the diligence expected from a holder of this position. The liquidator is fully liable for the damages caused by a breach of their duties.

13. As for challenging the debtor's agreements that aim to fraudulently transfer assets, which agreements can be successfully challenged before the court?

The following agreements concluded before the starting day of the liquidation will qualify as invalid agreements:

- Agreements and other legal statements that resulted in the reduction of the

debtor's assets qualify as a fraudulent agreement if they aim to deceive creditors and the other party of the agreement was aware or should have been aware of this intention,

- Agreements without consideration and agreements with conspicuously disadvantageous terms, or
- Agreements and legal statements that resulted in the preferential treatment of one creditor over other creditors.

Other Issues in Business Life

"A business is successful to the extent that it provides a product or service that contributes to happiness in all of its forms."

—Mihály Csikszentmihályi

*The third part of the handbook highlights some issues not necessarily arising during the life of a business entity. However, these topics are also worth noting, in particular the rules of Hungarian and European competition law (**Competition Law**), the new screening procedure with regard to foreign investments harming Hungary's security interests (**National Security Screening of Foreign Investment**) as well as some thoughts about data protection, doing business online and intellectual property (**Intellectual Property, Doing Business Online** and **Data Protection**), and the main aspects of the private wealth planning (**Private Wealth**).*

Competition Law

Hungarian competition law basically follows that of the EU being a highly harmonised legal field, i.e. similar areas have the attention of all the European competition watchdogs, e.g. agreements restricting competition, abuse of dominant position, merger control and lastly, unfair commercial practices. Competences between EU and national-level watchdogs depend on different thresholds (e.g. companies' turnovers). Apart from their relationships with the EU, member states' watchdogs also work in close cooperation with each other. In this chapter, we will give you an overview of these areas.

Agreements Restricting Competition

What are restrictive agreements?

agreements preventing, restricting or distorting competitio- are prohibited

The concept of agreements under Hungarian competition law is different from the ordinary definition of an agreement (under civil law). Not only are oral or written agreements or implicitly concluded agreements considered to be agreements under competition law, but an agreement also includes "gentlemen's agreements" or agreements made via the decisions of associations of undertakings or concerted practices. A concerted practice means that undertakings have not explicitly mutually intended to act together but there is an implicit common understanding amongst the competitors about their way of conducting their businesses.

A restrictive agreement can be concluded between undertakings that are independent of each other. Both agreements between competitors (horizontal agreements) and between undertakings operating on different levels of the market, e.g. producers and distributors (vertical agreements) are subject to competition law restrictions.

In some cases, even if an agreement is restrictive by its nature, it might not be considered anti-competitive. This may be the case, e.g. if the agreements are of minor importance or concluded between non-independent undertakings.

On the other hand, "hard-core" agreements are always regarded as anticompetitive and illegal. These are concluded between competitors and typically aim to set prices, allocate markets, restrict quantities, establish cooperation in tenders or prohibit the seller from exporting, etc. (commonly known as a "cartels").

Abuse of Dominant Position

The Definition of "Dominant Position"

An undertaking holds a dominant position in the market if it has such significant market power that this position enables the undertaking to act largely independently of its competitors, suppliers, buyers and customers. When determining a company's dominant position, the size of the market share has great significance but that itself does not define whether an undertaking is in a dominant position.

Abuse of dominant position

The following also have great significance besides market share:

- entry and expansion limits (e.g. administrative and legal burdens, technological capacity or already existing infrastructure),
- the lack of buyers' power,
- the characteristics of the relevant market, and
- the number and size of the other market players.

Abusing a Dominant Position

It must be stressed that a dominant position itself is not prohibited; only abus- ing this position is unlawful. The whole concept of "abuse of a dominant position" is about the undertaking being in a dominant market position having a stricter, objec- tive responsibility.

Business behaviour is considered "abuse" if it has the actual or potential effect of reducing the existing competition in the relevant market or preventing the increase of competition.

Here are some examples of abuse of a dominant position:

- Imposing unfair trading conditions, e.g. establishing overly-high prices,
- Limiting production or technical development to the disadvantage of customers,
- Applying dissimilar conditions to equivalent transactions with other market participants or even squeezing competitors out of the relevant market, e.g. by using predatory prices,
- Refusing a contractual relationship or terminating a business relationship with other market participants (not customers!) without a rational reason, or
- Making the conclusion of contracts subject to the acceptance, by other parties, of irrational and unnecessary obligations, e.g. product bundling where the customer has to buy an unneeded supplementary product.

Merger Control

The Definition of a Merger

conglomeration of two or more companies

The term "merger" refers to cases where two or more undertakings agree to continue as a single new undertaking, rather than remaining separate entities.

Gaining control over another undertaking or group of undertakings will – if certain thresholds are reached – incur an obligation to notify the Hungarian Competition Authority ("HCA") of the merger. (For the exact limits, please see the related FAQ.) The merger may not be executed before the HCA issues clearance or acknowledges the merger.

Based on the complexity of the merger, the HCA will conduct either a simplified or a full procedure, at the end of which it will decide upon the clearance of the merger. If the HCA does not either initiate the assessment of the application or reject it within 8 days from its receipt, the merger is considered to be cleared and the HCA issues an official certificate on the clearance. When assessing an application for clearance, the HCA examines the advantages and disadvantages of the proposed merger, the structure of the relevant market and the effect of the merger on suppliers, business partners and ultimately, consumers. If the HCA does not issue a decision by its deadlines, the approval may be considered to have been granted.

There are some examples where government decrees exempt mergers from the HCA's notification and investigation. In these cases, the mergers are considered to be of such national significance that they may be concluded without the HCA's intervention.

Unfair Commercial Practices

Overview of Unfair Commercial Practices

What are unfair commercial practices? First, these are practices directed at consumers. Second, in practice, these include the conduct, activity, omission, advertising, marketing or other commercial communication of market actors directly related to the sale, supply or promotion of goods to consumers.

The HCA has authority if the commercial practice may have substantial influence over economic competition. The reason why the HCA is involved is that the unfair practice of the companies may both affect the consumers and influence the market. As a result, companies can influence more consumers and increase their share of the market.

"Substantial influence" is hard to define. It may depend on the extent of the com-

mercial practice, the size of the company that has the practice and its net income.

However, substantial influence is established if:

- the commercial practice takes place through a media service provider providing national media services, or
- the commercial practice is carried out through a national periodical or daily newspaper distributed in at least three counties, or
- direct marketing is directed at consumers in at least three counties, or
- local sales promotion practices are organised in at least three counties.

The abstract legal framework of unfair commercial practices is cemented by the case law of the HCA. According to some of its most significant decisions, classic examples of unfair commercial practices include:

- advertising a service as free of charge, whilst it is not really possible to access the essence of the services free of charge, i.e. actual participation in the process (e.g. the sending of messages) is only possible for a fee,
- promoting the "free cancellation" of a service whereas consumers are, in fact, only able to make use of this option for a limited period of time and pay a higher price than for the same accommodation without the option of "free cancellation",
- exerting psychological pressure on consumers by posting untrue and misleading messages that create a sense of urgency,
- influencer marketing without transparently communicating that the posts contain paid promotions through sponsorship, or
- promoting by inducing a false and misleading concept of medicinal or healthbeneficiary effects.

Other roles of the HCA in the Hungarian legal system

The HCA serves as the contact authority under Regulation (EU) 2022/2560 of the European Parliament and of the Council on foreign subsidies distorting the internal market.

Starting from February 2024, compliance with the Digital Services Act (DSA) Regulation (Regulation 2022/2065 of the European Parliament and of the Council) will become mandatory and in this context from March 2024 onward the HCA will be endowed with increased enforcement powers allowing it to take action to shut down harmful websites in the course of its proceedings.

How can VJT & Partners help?

Since every company is obliged by law to assess the legal or unlawful (anti-competitive) nature of its own proposed agreement(s) with its competitor(s) or its business partners, it

is essential for a company to consult a professional legal practitioner before concluding such an agreement. VJT & Partners regularly advises its clients on matters involving the assessment of agreements from a competition law perspective.

Assessing the existence of a dominant market position and whether it is abused is a difficult question. Therefore, we strongly advise companies to consult a professional legal practitioner in such cases. VJT & Partners can help its clients in assessing both questions.

With our significant experience in litigation and competition law, VJT & Partners can provide our clients with reliable, high-quality representation before the HCA or the courts in connection with alleged violations of the Competition Act or the TFEU.

Regarding merger control cases, VJT & Partners stands ready to help its clients with any legal advice, as well as to draft and complete all necessary documentation when applying for the approval of a merger by the HCA. Due to our strong M&A practice, VJT & Partners also has diverse experience in representing clients before the HCA in merger control cases.

Lastly, VJT & Partners has extensive experience in assisting clients in cases that started before the HCA because of unfair commercial practices.

FAQ

1. What am I risking if I want to conclude an agreement that possibly restricts competition or abuses a dominant market position in Hungary?

First, you need to consider that an agreement restricting competition is null and void. Second, if the HCA – following its investigation – rules that the agreement would restrict competition, it will impose a fine of up to 10% of the net turnover you (or your group of undertakings) have achieved in the year preceding the HCA's decision.

2. What can I do if I become aware of a third-party agreement restricting competition that adversely affects my business?

First, you can officially notify the HCA of the agreement by completing a form and providing all the information available. If the case is well-founded, the HCA will start its proceedings against the parties involved in the agreement.

Second, you can also file a claim for damages in court against the parties to the agreement. If the case concerns a cartel, there is a legal presumption that the prices have been influenced by 10%.

3. Do all mergers need to be notified?

No. Under certain conditions, the Hungarian merger control system is based on an obligatory notification to the HCA. Therefore, merging undertakings must be reported if:

(i) the aggregate net revenue of the undertakings' sales directly or indirectly involved in the transaction in the preceding business year exceeds HUF 20 billion, and

(ii) among the groups of undertakings concerned, there are at least two groups each of whose total net revenue of sales in the business year prior to the merger, together with the net sales revenue of undertakings controlled by the members of the same group jointly with other undertakings, exceeds HUF 1.5 billion (groups of enterprises concerned means any direct participants, plus the indirect participants with which they are affiliated).

A merger can be reported even if the threshold is not met when:

(i) it is not obvious that the merger does not materially restrict competition in the relevant market, and

(ii) the net sales revenue of the groups of undertakings involved in the merger exceeds HUF 5 billion.

Since this can be difficult to assess, it is advisable to engage a lawyer or an expert economist in competition matters to evaluate whether a notification must be made.

4. What are the financial risks involved in violating competition law provisions?

If an infringement is established, an administrative fine can be imposed. The maximum amount of this fine is 13% of the net turnover, achieved in the business year preceding that in which the HCA's decision is adopted.

A procedural fine can be imposed on those who engage in an act or demonstrate conduct that has the object or result of protracting the proceedings, preventing the facts of the case from being established or on those who otherwise culpably fail to meet an obligation. The minimum procedural fine is HUF 200,000 for undertakings and HUF 50,000 for natural persons not qualifying as undertakings. For undertakings, the maximum is 1% of the net turnover in the business year preceding the adoption of the order imposing the procedural fine and HUF 500,000 for natural persons not qualifying as undertakings.

National Security Screening of Foreign Investment

In matching the trend of recent years on establishing foreign investment review mechanisms, Hungarian legislation has followed the example of the United States, China, Russia, Germany and a dozen other EU countries, in line with the EU regulation in force since 11 October 2020.

*Hungary has introduced several provisions that supplement the existing foreign direct investment regime ("2**018 FDI regime**") (i.e. the two regimes exist parallelly). A parallel FDI regime ("**2020 FDI regime**") has also been adopted in 2020, and then redrafted in 2022 ("**2022 FDI regime**"). Nevertheless, the 2022 FDI regime is only slightly different from the 2020 FDI regime.*

2018 FDI regime

Sectors

The screening procedure under the 2018 FDI regime concerns only companies with the following business activities and as further specified in the relevant government decree (each is referred to as a "**Sensitive Activity**"):

- manufacture of weapons, ammunition, production of military technology and equipment that is subject to licencing,
- production of dual-use goods,
- production of intelligence services equipment,
- provision of financial services and the operation of payment systems,
- certain electricity, natural gas, public water and electronic communication services that are essential to maintaining vital societal functions,
- participation in the establishment, development or operation of electronic information systems for public and local governmental bodies and participation in the investigation of security incidents and examination of the vulnerabilities of those systems, and
- insurance and reinsurance activities under the Hungarian Insurance Act and activities directly related to insurance activities.

Foreign Investment

The screening mechanism under the 2018 FDI regime is required if a foreign investor:

- acquires (including establishment), directly or indirectly, a shareholding of over 25% (10% in case of public companies limited by shares) or dominant influence in a company with a registered seat in Hungary that conducts a Sensitive Activity or if, as a result of the acquisition, the shareholding of foreign investors exceeds 25% in such company (except for public companies limited by shares),
- establishes a branch in Hungary to undertake a Sensitive Activity, or
- acquires the right to operate or use the infrastructure, equipment or assets that are essential to carry out a Sensitive Activity.

Procedure

Notification Obligation

Notification on the investment must be made to the Head of the Cabinet of the Prime Minister (being responsible for the management of the civil national security services) ("Minister") within 10 days of the conclusion of the respective agreement, pre-contract, term sheet, letter of intent, etc. Alternatively, if the notification obligation arises from a newly commenced Sensitive Activity, notification must be made within 10 days of the registration of such Sensitive Activity with the trade registry.

The notification must contain, *inter alia*, the ownership structure and the beneficial owners of the foreign investor, the estimated value of the investment, the concerned EU countries in which the Sensitive Activity is carried out, information on the financing of the transaction, as well as the planned completion date of the investment. Official Hungarian translation of the transaction documents must also be attached.

Outcomes of the Procedure

The Minister must make his decision on the acknowledgement or prohibition of the investment and respond to the foreign investor's notification within 60 days. However, the deadline may be extended under extraordinary circumstances or for the purposes of fulfilling the obligations under the EU screening mechanism by an additional 60 days. The Minister investigates whether the foreign investment would harm Hungary's national security interests, and the Minister may:

- prohibit the investment, or
- acknowledge the notification, in which case the foreign investor may complete the transaction.

The Minister may only prohibit the foreign investment that takes place through a legal entity registered in the EU, EEA or Switzerland if he concludes that the EU, EEA or Swiss entity was set up to bypass the screening procedure.

The prohibition may not be appealed. The prohibition may only be challenged

against procedural errors or if the Minister found that an EU, EEA or Swiss entity was set up merely to bypass the screening procedure.

Sanctions

Non-compliance may result in a fine capped at HUF 10,000,000 for legal entities and at HUF 1,000,000 for individuals. In addition to imposing an administrative fine, the Minister may enforce the sale of or the elimination of the foreign investment subject to the pre-emption right of the Hungarian State.

2022 FDI regime

Sectors

The screening procedure under the 2022 FDI regime concerns companies qualifying as so-called "strategic companies"' conducting a business activity classified as a "strategic business activity". A limited liability company, a private or public company limited by shares or an educational institution having its registered seat in Hungary, of which the main or other business activity is a strategic business activity, qualifies as a strategic company. Currently, 25 Nace Rev. 2. groups are contained in the relevant legislation (e.g. various manufacturing activities, retail and wholesale, telecommunication, IT, critical industrial sector, energy, healthcare, education, and nuclear sectors) are considered to be strategically important. Given the fact that the scope of the strategic business activities is rather wide, it is likely that a potential Hungarian target company qualifies as a "strategic company".

Foreign Investment

The screening mechanism under the 2022 FDI regime is applicable if a foreign investor, whether directly or indirectly:

- acquires (excluding through establishment) a stake of at least 5% (in the case of public companies, 3%) in a strategic company or if, as a result of the acquisition, the shareholding of foreign investors would exceed 25% in such company (except for public companies limited by shares),
- acquires majority influence in a strategic company, or
- acquires the right to operate or use the infrastructure, equipment or assets that are essential for the respective strategic business activity.

Acquisition of a stake does not trigger the notification obligation if the value of the transaction does not exceed HUF 350 million (approx. EUR 850,000). However, the

value of the transaction is irrelevant if the transaction concerns the acquisition of assets and equipment critical for the respective strategic business activity.

Foreign Investor

A foreign investor is:

- a citizen of a third country or a legal entity or other organisation registered in a third country, or
- a legal entity registered within Hungary, the European Union, the EEA or Switzerland, if it is under the majority control of a citizen of a third country or a legal entity or other organisation registered in a third country.

In the case of acquisition of majority influence (whether directly or indirectly) over a strategic company, entities registered within the European Union (excluding Hungary), the EEA or Switzerland also qualify as foreign investors.

Procedure

Notification Obligation

Notification must be made to the Minister of Economic Development (being responsible for the management of domestic business affairs) ("Minister of Economy") within 10 days from the conclusion of the respective agreement, pre-contract, term sheet, letter of intent, etc. The notification must contain, *inter alia,* the ownership structure and the beneficial owners of the foreign investor, the detailed description of the transaction and the facts relevant from the perspective of the transaction. Official Hungarian translation of the transaction documents must also be attached.

Outcomes of the Procedure

The Minister of Economy must make his decision on the acknowledgement or the prohibition of the transaction and respond to the investor's notification within 30 working days. However, the deadline may be extended under extraordinary circumstances by an additional 15 days.

The Minister of Economy investigates whether:

- the completion of the transaction would actually or potentially violate or endanger the national interest, public safety or public order in Hungary, especially the security of supplying fundamental social needs,

- the investor is under the direct or indirect control of an administrative body of a country outside the European Union due to its ownership structure or significant financing,
- the investor has been affected in any member state of the European Union by an activity endangering security or public order, or
- there is a significant risk that the investor will conduct a criminal activity.

As a result of the investigation and assessment, the Minister of Economy will:

- prohibit the investment, or
- acknowledge the notification, in which case the foreign investor may complete the transaction.

Sanctions

In the event of failure to notify the respective transaction:

- the transaction agreements are null and void,
- the Minister of Economy may impose a fine on the investor of up to double the amount of the transaction value on the investor, and
- the entry into the company register of the change of ownership is prohibited.

How can VJT & Partners help?

Due to the novelty of the screening mechanism, the confidential nature of the procedure and lack of publicly available documentation, as well as the lack of detail and clarity on what conduct qualifies as harmful from Hungary's national security perspective, legal support is strongly advised. VJT & Partners can help clients in all phases of the screening procedure and help determine whether the planned transaction falls under the scope of the screening mechanism and if so, how to proceed.

FAQ

1. Who is a foreign investor?

According to the FDI 2018 regime:

- A non-EU, non-EEA or non-Swiss citizen, legal entity or other entity.
- A legal entity registered in the EU (including Hungary), the EEA or in Switzerland, if that legal entity is controlled by a non-EU, non-EEA or non-Swiss citizen, legal entity or other entity with majority control.

According to the FDI 2022 regime:

In addition to the above, a citizen of another EU Member State, EEA state or the Swiss Confederation, or a legal entity or other entity registered in such states also

qualify as a foreign investor if the transaction involves the acquisition of the majority control over a strategic company.

2. What is majority control?

Majority control means a relationship where a natural person or legal entity directly or indirectly controls over 50% of the voting rights in or has a dominant influence over a legal entity.

3. What is a dominant influence?

An investor is considered to have a dominant influence over a legal entity if:

(i) it has the right to appoint and recall the majority of the executive officers or supervisory board members of the specific legal entity, or

(ii) based on an agreement, the rest of the shareholders of the legal entity vote in concert with the dominant influencer or that the remaining members or shareholders of the legal person exercise their rights through the dominant influencer if, together, they hold more than half of the voting rights in the legal person.

4. What are the main characteristics of the 2022 FDI regime?

The procedure is similar to the one under the 2018 FDI regime, but the concerned sectors are wider. These sectors include, inter alia, energy, transport, communication, other critical infrastructures, e.g. water, health, media, data processing or storage, aerospace, defence, electronic infrastructure and finance. Also, there is a difference to whom the notification must be made. Whereas, in the case of the 2018 FDI regime, the notification must be made to the Head of the Cabinet of the Prime Minister, under the 2022 FDI regime the notification must be made to the Minister of Economic Development.

Intellectual Property

Intellectual property is a key asset and part of businesses, especially for those operating in the information technology, communication and health sectors. This chapter introduces the structure of intellectual property as a whole and we provide a practical overview of the issues that may emerge when operating a business in Hungary.

protection of creators of intellectual goods and services

Intellectual property ("IP") law aims to protect the creators of intellectual goods and services by granting them certain time-limited rights to control the use of those creations. IP is divided into two main areas:

- copyright - which protects literary, scientific and artistic creations, and
- industrial property - which protects inventions (patents), utility models, trademarks, designs and geographic indications.

In Hungary, the principle of simultaneous protection applies, i.e. if the work is protected by more than one type of protection (for example, know-how is also a patentable invention), the right-holder can choose between the different claims or even assert them simultaneously.

Copyright

Hungarian copyright regulations in general

copyright protection under Hungarian law

All literary, scientific and artistic creations are protected by copyright. A creation enjoys copyright protection due to its individual and original nature deriving from the creator's intellectual activity. Such creations may be, e.g. literary works, musical works, radio and television plays, photographic creations, maps, architectural works and plans, computer programs and their related documentation (software), etc. Ideas, principles and theories are not subject to copyright protection.

Copyright is held by the author from the moment the work is created. No application or registration procedure at any authority is required in this respect. If several authors created the work, they are jointly entitled to copyright. The authors' rights consist of the collection of moral rights and economic rights.

Moral rights

The author has the exclusive right to:

- disclose the work,
- withdraw it from the public,
- have their name indicated on the work, and
- prevent any distortion, mutilation or any other modification of the work which would be prejudicial to the author's honour or reputation.

The authors' moral rights cannot be transferred; even if the work is sold or passes to the employer, the author's moral rights are retained.

Economic rights

As part of their economic rights, authors have the exclusive right to use and to authorise the use of their work in certain ways, e.g. for reproduction, distribution, public performance and communication to the public. The author is entitled to remuneration in return. However, the author may waive the claim to remuneration by making an explicit statement to that end.

As a general rule, the author may not transfer economic rights either. Nevertheless, economic rights can be inherited and, in certain cases, can be transferred, most importantly concerning software, databases and cinematographic creations.

IP works of the employee

If the employee's job involves creating copyrightable work (e.g. a programmer, design engineer), the economic rights to the work created are automatically transferred to the employer. This obligation of creative production may be stipulated in the employment contract or the job description. In such case, the employee who created the work is also entitled to remuneration as a general rule.

We strongly recommend that you consult us from both an employment law and IP law perspective if your business is heavily involved with IP, to avoid additional costs later and to ensure that your IP assets are protected.

Licence agreement

Based on a licence agreement, authors may authorise the use of their work and the user is obliged to pay remuneration for this use. Licence agreements are complex from a legal perspective with a number of mandatory limitations.

Therefore, it is highly recommended to consult these matters with an attorney-at-law. VJT & Partners has special expertise in copyright matters including software licensing.

Collective right management

If the circumstances and nature of the work's use (radio, television broadcast, etc.) prevent the authors from exercising their copyrights individually, collective right managing organisations collect royalties and forward the royalties to the authors. This is generally useful for hotels, restaurants, retail shops and other public premises which do not have to obtain licences individually from the authors. There are several different organisations in Hungary, usually associations, that focus on a specific IP field (e.g. Artisjus for composers or songwriters).

Software and database

protection of software and databases

Economic rights to software and databases may be transferred under Hungarian copyright regulations. In the case of non-exclusive licences to software and databases recognised as a compilation, it is not obligatory to conclude the agreement in writing.

Certain rules for remuneration do not apply to software created as part of an employment relationship.

Voluntary register of works

It is possible to register copyright works in the voluntary register managed by the Hungarian Intellectual Property Office ("HIPO") The voluntary register of works makes it easier for the author or the holder of rights to prove their identity as the author or holder of rights; on the other hand, it does not create a right to the intellectual work (for detailed information regarding the voluntary register of works, see the FAQ below).

Time of protection

In principle, copyright provides protection during the author's life and for 70 years after death.

Industrial property

The collection of industrial property rights aims to protect intellectual creations that are technical in nature.

It should be noted that unless a provision of an international treaty provides otherwise, foreign applicants (meaning applicants that are not domiciled in Hungary) must be represented by an authorised patent attorney or an attorney-at-law resident in Hungary in all patent, design or trademark matters within the competence of the HIPO. However, this rule does not apply if the foreigner is a natural person or a legal entity whose permanent residence or domicile is in an EEA Member State.

Patents

patents

Patents are granted for any invention in any field of technology that is new, involves an inventive step and is suitable for industrial application. The right holder of the invention has an exclusive right to make use of the solution of the invention, but the period and the territorial validity of patent protection are limited. Patent protection is valid for 20 years starting from the date of filing the patent application.

A Hungarian patent may be obtained through a national or European application or through an application submitted in the framework of the Patent Cooperation Treaty ("PCT"). If the application and the invention comply with the requirements regarding the relevant patent type (i.e. national, European or PCT application), the patent will be granted in a procedure taking place before the competent authority.

Under a patent license agreement, the patentee may license the right to use an invention and the person using the invention (licensee) is required to pay royalties. The patent license agreement covers all patent claims and every form of use without limitation in time or territory. However, the right of use is only exclusive if expressly stipulated in the contract.

Service invention is defined as an invention made by an employee under the obligation to develop solutions in the field of the invention. An employee invention is an invention made by a person who, without being obliged to do so, creates an invention, the use of which falls within the field of business of their employer. The right to a patent for a service invention belongs to the employer. The right to a patent for an employee invention belongs to the inventor, but the employer is entitled to use the invention. The employer's right of use is non-exclusive. The inventor is entitled to remuneration in both cases, usually governed by an invention fee agreement between the parties.

Designs

Design protection is granted for any design that is new and has an individual character.

Design protection in Hungary may be obtained:

- by filing a design application to the HIPO,
- by filing an international application under the Hague Convention Concerning the
- International Deposit of Industrial Designs, or
- by Registered Community Design ("RCD") which is valid in the EU.

time of protection

The design protection is for 5 years, beginning from the date the application is filed. This term can be renewed for further periods of five years each, four times at maximum.

Trademarks

Trademark protection is granted to any sign that:

(i) is capable of distinguishing goods or services from those of others, and

(ii) can be illustrated graphically.

Apart from the usual signs that can be subject to trademark protection, e.g. words and logos, the Hungarian Trademark Act allows for a liberal approach and permits, in particular, the following signs to be registered as well:

- two- or three-dimensional forms, including the shape of goods or of their packaging,
- colours, combination of colours,
- light signals, holograms,
- sound signals,
- words,
- figures, and
- any combination of these.

The following trademarks may enjoy protection in Hungary:

- National trademarks are filed with the HIPO/ and the protection extends only to the territory of Hungary,
- International trademarks: the HIPO forwards the international trademark application based on the Madrid Agreement or the Protocol to the World Intellectual Property Organisation, and
- European Union trademarks: the application is to be filed with the European Union Intellectual Property Office (EUIPO). The protection of a European Union trademark extends to the whole of the EU.

Term of protection

The national procedure is conducted by the HIPO. If the trademark application meets all the requirements, the HIPO publishes the application in their official journal online and the opposition period of 3 months starts. If the 3 months have passed without opposition (or the opposition did not meet the necessary requirements), HIPO registers the trademark in the Trademark Register and issues a trademark certificate.

Trademark protection is for 10 years from the date the application is filed. Protection can be renewed for an additional 10 years at the request and the number of renewals is unlimited (for additional information on the renewal procedure, see the FAQ below).

How can VJT & Partners help here?

If your business needs any advice either in dealing with copyright questions or in industrial property matters, you can turn to VJT & Partners. With our acquired extensive experience in licensing matters, IP-related due diligence during M&A deals, trademark protection, managing IP in employment relationships, out-of-court settlements and other various aspects of intellectual property, we are happy to help you at any time.

FAQ

1. Do I have to request authorisation from the author for any use?

Generally, yes. Only in certain limited cases (usually for educational use), the law allows for the use of an author's works without the author's consent. In legal jargon, this is called "free use".

2. How do I renew a patent?

A patent as a general rule cannot be renewed after the expiry of the 20-year period of protection. As per the EU regulations the invention might be granted a supplementary protection after the expiry of the patent protection. Yearly maintenance fees shall be paid for the period of the supplementary protection and after the 4th year of the basic patent protection period as well.

3. How do I renew a trademark?

Trademarks can be renewed for an unlimited time after the 10-year expiry. The registry office sends a reminder of the expiry and the renewal application may be submitted within 6 months before the expiry date, or if this deadline is not met, within 6 months after the expiry date subject to the payment of additional fees. During the renewal procedure, the registered trademark cannot be modified and the underlying list of goods cannot be extended.

4. Is there any link between trademarks and domains?

The registration of domains may raise legal issues relating to registered trademarks; therefore, it is recommended to search the trademark register to avoid a potential trademark infringement and the consequences of such.

Domain names can be trademarks, but not necessarily. They can also be commercial names (e.g. the name of the company, brand name/slogan). Domain registration in Hungary is done through one central association (Magyarországi Internet Szolgáltatók Tanácsa Tudományos Egyesülete, "The Scientific Association of the Council of Hungarian Internet Providers") which conducts the registration proceedings and manages dispute resolution as well.

5. Are simple commercial names protected?

The name of the company registered in Hungary, as well as well-established brand names of good standing can be protected as commercial names, even if they are not registered trademarks. This could come in handy in domain and unfair market practice disputes.

6. What can I do if a registered trademark is infringed?

The registered owner of the trademark has the right to take legal action and claim:

- the declaration of an infringement by the court,
- the discontinuation of the infringement,
- reparative action by the infringer, e.g. by way of a declaration, made public if necessary,
- the collection of profits obtained by infringing the registration,
- the supply of information concerning the infringement,
- the seizure of equipment used for infringement and infringing products,
- measures by the customs authorities to prevent the free circulation of the infringed goods, or
- compensation for damages.

Doing Business online

A large part of our lives is now dependent on the digital space. For example, we handle our business and private matters online, we advertise online, we spend money online, and we sign contracts online. Simply put, we spend a considerable part of our lives in the online world. In this chapter, we provide a snapshot of some of the most relevant digital issues.

Establishing online business

There is no substantial difference between the establishment of online businesses and brick-and-mortar businesses.

In general, there is no general permit requirement for pursuing an online business but, like any other commercial activity, it must be reported to the notary based on the business' registered office. In addition, for certain online businesses (e.g. fintech companies, video-sharing-content providers) additional sector-specific notifications and licences may apply.

It is important to highlight that some products (e.g. tobacco, veterinary medicine and dangerous products) may not be sold online.

Concluding contracts online

There are online options to conclude a contract in Hungary.

In the case of an exchange of email or other equivalent individual communications, the contract is formed when one party clearly declares its offer (indicating the key terms) and the other party approves the offer. In the case of other forms of distance contracts, the business must acknowledge the user's order within 48 hours by electronic means (otherwise, the user is relieved from any contractual commitments).

'Click-wrap' contracts are generally enforceable if the user can review the terms and give their affirmative acceptance (e.g. ticking the checkbox).

In the context of business-to-consumer online sales, consumers may withdraw from an electronic contract within 14 days of its conclusion. Businesses must adequately inform consumers about this right; otherwise, the withdrawal deadline will extend up to 12 months.

Electronic signatures

A legal document will be qualified as written if: (1) it can be proved that the content of the document is unchanged, (2) the signatory is identifiable, and (3) the time of signing is identifiable. Where a written form is required (e.g. sale agreements or copyright agreements), parties must primarily use a qualified electronic signature and time stamp or an advanced electronic signature and time stamp. As a general rule, other forms of agreements, e.g. agreements made via DocuSign or AdobeSign, an exchange of emails or clicking an acceptance button, may not be qualified as 'written'.

E-signature services must be provided by a trusted service provider registered in Hungary or another EU country. The list of registered trusted service providers for the whole of the EU can be found here: https://eidas.ec.europa.eu/efda/tl-browser/#/screen/home.

Advertising online

The main legal framework for advertising is set in the Advertising Act which, regarding its procedural and enforcement rules, is supported by the Consumer Protection Act. Direct e-mail marketing, as a form of online advertising, is regulated specifically in the E-Commerce Act. In addition, the Unfair Commercial Practice Act sets out the rules against misleading advertising (see the Competition law chapter). The legal framework is supported by the activity of the Hungarian Advertising Association and the Self-Regulating Advertising Corporation as self-regulatory organisations concerning ethical and professional rules.

The Hungarian E-Commerce Act defines electronic communication as any commercial ads or notices communicated via an information society or electronic communication service relating to social aims. In general, an advertisement does not have to be strictly separated from online editorial content, but its placement in the content must clearly indicate its promotional nature by design.

Promoters must notify about the electronic communication in a clear manner about:

- the fact that it is an electronic communication,
- the advertiser, and
- promotional offers or games (if applicable).

Under the E-Commerce Act, prior consent is needed to send electronic communications (e.g. direct marketing emails). However, based on the Hungarian Data Protection Authority's practice, additional electronic marketing communication may be sent to existing customers on an opt-out basis.

Hungarian advertising law has restrictions and bans (e.g. banning tobacco ads and, under certain conditions, alcohol, firearm or gambling ads). However, in principle, all products that may be advertised offline may be advertised online as well. An exception applies to reminder advertising of over-the-counter medicinal products or therapeutic medical devices that are not supported by the social security service, as such reminder advertising may not be carried out via the internet.

How can VJT & Partners help?

Since every company may face situations where online forms of business activities come into play, it is essential for a company to consult a professional legal practitioner before commencing these activities. VJT & Partners regularly advises a Big Tech client on its digital products.

FAQ

1. Can a website provider be liable for mistakes in the information that it provides online?

As a general rule, as long as the website provider is a content provider and not an intermediary provider (e.g. a host, search engine or cache provider), it is liable for any of its own content made available on its site. This liability cannot be removed with a unilateral disclaimer notice. The website provider is also liable for third-party content but it can avoid such liability under certain conditions (e.g. it has a proper notice-takedown mechanism for inappropriate user comments or it republishes defamatory content but cites the source and allows for the possibility of the other party to react).

2. Can a website owner use third-party content?

A website owner may use third-party content on its website without permission, only if there is a specific permitted case of fair use (e.g. citation, a free lecture, parody, orphan works) to the extent it is used within the specific limits of fair use set out in the Copyright Act. Otherwise, the website owner's unauthorised use of third-party copyright work can constitute copyright infringement and the potential consequences can be civil in nature and lead to criminal consequences.

3. Can a website owner link to third-party websites or platforms without permission?

This must always be assessed on a case-by-case basis. In general, if the third-party website targeted all internet users and it was not protected (e.g. subject to a paywall), a link to a third-party website is permissible. Users must always have the clear ability to identify the original source and to understand that the website owner merely links to a third-party website (without having any relationship with the third-party websites). If the linked third-party website is unauthorised content, the website owner may be also liable.

4. Are any remedies available for the breach of digital contracts?

Based on the Hungarian implementation of EU Directive 2019/770 and 771, as of 1 January 2022, consumers have new special remedies in the context of the non-conformity of goods with digital elements, digital content and digital services ("digital products"). The consumer may ask to bring the digital products to conformity (unless it is impossible or would impose disproportionate costs). If the business fails to do so, the consumer may request a proportionate reduction in price or to terminate the contract. The rule of the reversal of the burden of proof (i.e. the consumer does not have to prove that the item was defective at the time of supply as it is assumed by law) is extended from six months to one year for digital products.

5. Are there any particular laws that limit the choice of governing law when entering into digital contracts?

In general, based on the Rome I Regulation, in the case of a choice of law, digital contracts may not derogate from Hungarian mandatory provisions where business-to-consumer (B2C) contracts apply or the overriding Hungarian mandatory provisions where business-to-business (B2B) contracts apply .

6. Are there any particular laws that limit the language of contracts when entering into digital contracts?

As regards B2C contracts, the Hungarian consumer protection authority requires the Hungarian language based on the general fairness principle. As regards B2B contracts, the Hungarian language is not a requirement but, in the case of platform-to-business contracts, it is possible that the competent Hungarian authority will require the Hungarian language based on the fairness and transparency principle.

Hungarian advertising law has restrictions and bans (e.g. banning tobacco ads and, under certain conditions, alcohol, firearm or gambling ads); however, in principle, all products that may be advertised offline may be advertised online as well. An exception applies to reminder advertising of over-the-counter medicinal products or therapeutic medical devices that are not supported by the social security service, as such reminder advertising may not be carried out via the internet.

Data Protection

As an EU member state, Hungary must comply with Regulation 679/2016/EU on the protection of natural persons regarding the processing of personal data and on the free movement of such data. The Regulation is commonly referred to as the General Data Protection Regulation or the GDPR. The GDPR establishes both general and detailed data protection rules and creates transparency and an expected homogeneity of law enforcement throughout the EU.

The Regulation brings huge benefits for data subjects; however, it does so at the cost of a tremendous effort required from businesses. With its strict requirements, the GDPR has become the toughest regulation ever made in privacy circles. Data controller companies may face fines of up to EUR 20 million or 4% of their total worldwide annual turnover if they do not comply. The GDPR also requires companies to be conscious of their data-processing activities. With these incredibly high fines, the GDPR imposed several new administrative burdens on companies. From detailed rules on providing information to the data subject and data processing agreements, through handling data breaches and completing data protection impact assessments, to regulating the status of the data protection officers, the GDPR lays down complex and strict provisions. It requires an innovative way of thinking. Self-regulation carries an important role in complying with the GDPR's requirements.

In April 2019, Hungary implemented the GDPR by amending 86 sectoral acts in numerous sectors including finance, healthcare and marketing. The Hungarian Data Protection Act itself also added some specific local requirements including extending the GDPR to include manual data processing even where the personal data is not part of a filing system and in some instances, even to the processing of a deceased person's personal data.

The Hungarian Data Protection Authority ("DPA") has been always considered to be a conservative privacy watchdog due to its strict interpretation of data protection laws. It is considered particularly strict in interpreting basic data protection principles, e.g. purpose limitation and data minimisation. In practice, there is also a shift from traditional GDPR issues to cybersecurity and data breach management where the DPA imposed a particularly high fine, compared to its practice (close to EUR 250,000).

Bearing all this in mind, it is worth reviewing your data protection practices regularly to be sure the rules imposed by the GDPR and the Hungarian data protection laws are consistently followed. Also, if you have not yet done so, it is vital to consult a data protection expert before:

(i) commencing any further data processing activities, or

(ii) analysing the operation of your company within the framework of a data protection audit to check whether it complies with European and Hungarian data protection laws.

Since the GDPR has been in effect for more than five years now, it is high time to take all the necessary precautions to be sure that your data protection practice is GDPR compliant. Since its obligatory enforcement as from May 2018, the DPA has provided guidance on the practical application of GDPR requirements.

How can VJT & Partners help here?

Having acquired extensive experience in data protection and being honored to be the winner of the Wolters Kluwer Award in the "Best data protection team" category, VJT & Partners can provide you with the necessary assistance to answer any data protection question.

FAQ

1. What does the GDPR's accountability principle mean?

Now that the GDPR has entered into force, it will not be enough for companies to act in line with the regulation, even if their processes are compliant with the law. The GDPR requires companies to be able to prove that they are doing so. This means that all data protection-related situations have to be documented (e.g. documentation about impact assessments being carried out or documentation of how the legitimate interest test has been passed, records of processing activities, etc.).

Naturally, these all place a great administrative burden on businesses.

2. What do privacy by design and privacy by default mean?

Although new to Hungarian law, both concepts were already known in privacy circles.

Privacy by design means that companies must consider the key data protection concerns in the early stages of a project and then throughout its lifecycle. For example, if a company wants to implement a new database software, it must assess potential data protection issues and fix them before implementation.

Privacy by default means that a company securely processes only the data that is processed by default which is strictly necessary for each specific purpose. For example, a company that sends out online newsletters to its clients does not need to hold telephone numbers as it is not necessary for this purpose. Privacy by default also requires minimising access. For example, the payroll department should not have access to data that is only relevant to the recruitment team. Privacy by default is a great challenge for businesses as most businesses still have databases that are generally accessible to all members of the organisation.

3. What is a personal data breach? Are they all subject to notification?

Personal data breaches are security breaches that relate to personal data, e.g. unauthorised access, unintended alteration, loss or disclosure.

Since the category of personal data breaches is quite broad, not all data breaches need to be reported to the data protection authority or to the data subject. In general, reporting is required when the breach means a risk for the person concerned. However, regardless of if reporting is necessary, all personal data breaches need to be documented.

The key differences between reporting and documentation may be highlighted with this example. If a company manager loses a company laptop with personal data stored on it, but the data is pseudonymised, the encryption key is stored separately and there is a back-up for the lost personal data, then the data is likely to be inaccessible to anyone who finds it. Therefore, the laptop being lost is not likely to be a risk for a data subject. This event does not have to be reported, but it must still be documented by the company. On the other hand, if it later becomes evident that the encryption key was compromised, then the risk will change and the event must be reported to the data protection authority.

4. What is the difference between pseudonymisation and anonymisation?

When someone hides personal data under a pseudonym, that data is coded, but that data may be still tracked back to a data subject by decoding the data (even if this requires additional effort).

On the other hand, when a company anonymises data, it means that the connection with a data subject can never be restored. So, if done properly, anonymisation places the processing and storage of personal data outside of the scope of the GDPR.

5. Why is pseudonymisation important for businesses?

Pseudonymisation is listed in the GDPR as a key obligation to make data processing more secure.

Under certain conditions, the GDPR allows the processing of pseudonymised data for use beyond the purpose for which the data was originally collected, without the need to obtain additional consent.

In certain cases, if data is pseudonymised, a personal data breach does not need to be reported to the data protection authority.

6. Is all data processing legal if I have consent?

Consent alone does not fulfil all the general data protection principles. For example, if a person gives consent to handling data that is not necessary for the processing (e.g. a phone number for email newsletters), this goes against the GDPR's data minimisation rule.

7. Is GDPR only relevant when it comes to structured data processing?

Data processing applies to all data processing, not just that which occurs in a structured system (e.g. a CRM database). Unstructured data covers all information that emerges when a business manages its everyday life but is not in a recognisable structure or in a database. This may include presentations, excel sheets, emails and more. Researchers have concluded that unstructured data can add up to 70% of all business data in an average organisation. This data may contain personal data and if it does, it falls under the GDPR's scope.

This may seem to be an excessive administrative burden, but modern software solutions are available that help to identify personal data and locate redundant data.

Private Wealth

Private wealth planning is becoming more and more popular in Hungary. High-net-worth individuals and families are seeking solutions to preserve their wealth and to plan for business succession.

Private Wealth Planning

Private wealth planning is a relatively new practice in Hungary. In recent years, high-net-worth individuals and families have become more interested in finding solutions for their business succession to keep their assets together and to go on holiday without worrying about the management of their company. Private wealth planning also includes estate planning and tax planning.

Inheritance and matrimonial property questions are also essential parts of private wealth planning. In Hungary, under the Civil Code, if there is no matrimonial property agreement between the spouses, the statutory matrimonial property regime is applicable. This is the same for inheritance. If one does not determine where their assets will go, the statutory property regime will be applicable. If a person wants to keep their assets together even in the case of divorce or death, inheritance and matrimonial questions cannot be avoided.

In Hungary, two institutional solutions can help individuals and families make the owner independent of his/her estates but keep them together. These two solutions are 'the wealth management foundation' ("WMF") and 'the trust'. These institutions can manage for example family asset management and succession problems (e.g. there is no descendant who intends to take over company management).

These institutions provide a flexible regulatory framework that allows derogations from the strictly regulated inheritance and matrimonial property rules. This way, it is ensured that the beneficiaries may receive adequate benefits while maintaining the unity of the ownership and control over the assets.

Setting up a Wealth Management Foundation

In the summer of 2019, new legislation introduced provided the possibility to set up a WMF in Hungary. WMFs have several advantages, e.g. tax benefits, business succession planning; as a result, an increase in the popularity of setting up WMFs is to be expected.

A WMF may be established to manage assets (at least with a value of HUF 600 million ordered by the founder and to manage income). A WMF must be registered with the competent Hungarian court (the statutory timeframe for registration is 60 days).

A WMF requires one curator or a curatorium of several members managing the foundation, a supervisory board of at least 3 members or a supervisor and an auditor.

The main function of a WMF is to manage the asset(s) provided by the founder to the WMF and to provide benefits to the beneficiary or beneficiaries appointed by the founder.

Creditors of the founder may have no claim against the assets placed with the WMF (unless this is wilfully abused). A WMF also overrides inheritance since the ownership of the assets belongs to the foundation, not the founder.

Trust for business owners

Trusts have been available in Hungary since 2014. A trust agreement must be concluded in writing between the settlor and the trustee. The contract with the trustee may be concluded either for an undefined term or a defined term, but in either case, the maximum term is 50 years. In principle, the client may terminate the contract with the trustee at any time (as agreed in the contract); as a result of which, the assets will be returned to the client.

Creditors of the client have no claim against the assets placed with the trustee (unless this is wilfully abused). The trust agreement also overrides inheritance since the ownership of the assets belongs to the trustee, not the client.

The trustee can be a professional (who has several clients) or a non-professional (who has a single client). In concluding a trust agreement, the ownership of the assets included in the agreement passes to the trustee. This means that the settlor cannot instruct the trustee once the assets have been passed to the trustee.

In the trust agreement, the settlor can appoint beneficiaries who will be entitled to receive benefits based on the trust agreement. Anyone can be the beneficiary, but the settlor cannot be the sole beneficiary.

A trustee must be either a Hungarian limited liability company, a Hungarian branch of an undertaking domiciled within the EEA or a law firm domiciled in Hungary. Private individuals may also be non-professional trustees. The trustee must be registered with the Hungarian National Bank. A professional trustee must also hold a licence issued by the Hungarian National Bank (the statutory timeframe for issuing a licence is 9 months). The trustee must have its own equity and security corresponding to the assets managed, but each must be at least HUF 70 million. Professional trustees must have at least one economist, one lawyer and an auditor.

How can VJT help?

We provide legal assistance in every field of private wealth management. We can help our clients with inheritance planning and matrimonial property matters (e.g. matrimonial property agreements).

We can assist in setting up wealth management foundations or trusts. We help our clients with drafting trust agreements and managing the other legal aspects of such agreements. We can also assist in business and estate planning.

We regularly work together with tax advisers to find the best tax structure for our clients.

FAQ

1. What do wealth management foundations and trust solutions have in common?

In both institutions, the ownership of the assets is transferred to a wealth management institution (i.e. to a trustee or a WMF). Both institutions may keep the assets together and provide benefits for chosen persons. If the assets are owned by these institutions, the creditors of the private individuals may not claim the transferred assets.

2. What is the main difference between wealth management foundations and trust solutions?

A WMF may be established to manage assets with a minimum value of HUF 600 million ordered by the founder. For trusts, there is no minimum asset value that can be transferred to the trust. Furthermore, while a trust agreement can be concluded for up to 50 years, WMFs can be established for an undefined period.

3. How should I decide whether to opt for a wealth management foundation or a trust solution?

The client must have a clear goal that they want to reach and manage with the given solution. Then, it must be assessed which solution can be tailored to the client's needs. For example, if the client would like to remain anonymous, the trust may be more favourable but if he/she wants to keep more control over the assets, a WMF may be the better choice.

Glossary

List of Abbreviations

BSE / BÉT	Budapest Stock Exchange / Budapesti Értéktőzsde
CBH / MNB	Central Bank of Hungary / Magyar Nemzeti Bank
CEO	chief executive officer / vezető tisztségviselő
CJEU	Court of Justice of the European Union
CTM	Community Trademark
DCP	Decentralised Procedure
EEA	European Economic Area
GCP	Good Clinical Practice
gp. / kkt.	general partnership / közkereseti társaság
HCA / GVH	Hungarian Competition Authority / Gazdasági Versenyhivatal
HEA / MEKH	Hungarian Energy and Public Utility Regulatory Authority / Magyar Energetikai és Közműszabályozási Hivatal
HIPA	Hungarian Investment Promotion Agency / Nemzeti Befektetési Ügynökség
HIPO / SZTNH	Hungarian Intellectual Property Office / Szellemi Tulajdon Nemzeti Hivatala
HITA	Hungarian Investment and Trade Agency / Nemzeti Külgazdasági Hivatal
IP	Intellectual Property
llc. / kft.	limited liability company / korlátolt felelősségű társaság
ltd. / zrt.	private company limited by shares / zártkörűen működő részvénytársaság
M&A	Mergers & Acquisitions
MRP	Mutual Recognition Procedure
NCPHP / NNGYK	National Center for Public Health and Pharmacy National Institute of Pharmacy and Nutrition / Nemzeti Népegészségügyi és Gyógyszerészeti Központ Országos Gyógyszerészeti és Élelmezés-egészségügyi Intézet
NMIA / NMHH	National Media and Infocommunications Authority / Nemzeti Média- és Hírközlési Hatóság
NTCA / NAV	National Tax and Customs Administration / Nemzeti Adó- és Vámhivatal
OHIM	Office for Harmonisation in the Internal Market
PCT	Patent Cooperation Treaty
plc. / nyrt.	public company limited by shares / nyilvánosan működő részvénytársaság
RCD	Registered Community Design
SMEs / kkv.	small and medium-sized companies / kis- és középvállalkozás
TFEU	Treaty on the Functioning of the European Union

Index

Why Choose VJT & Partners?

VJT & Partners is a leading Hungarian full-service commercial law firm. We advise international and domestic corporate clients and entrepreneurs.

We are experts

We are experts in a variety of legal fields. We understand the commercial realities of business and at the same time, we are masters of collaboration.

We understand business

We do not speak legalese; we talk business. We pride ourselves in giving direct, honest and practical advice, tailored to each client's individual needs.

We act in line with our values

The values that lie at the heart of our business ethos are the building blocks of our business. Nurturing the following values brings the 'hearts and minds' of VJT & Partners' lawyers together to create one successful team.

- Inspiring leadership

  That's why we develop, enjoy our work and become real masters of collaboration.
- Striving for perfection

  That's why we are always at the cutting edge, continuously pushing our boundaries.
- Commitment

  That's why we have a clear idea of what we want to achieve and that we are committed to reaching our goals.
- Courage

  That's why we are not afraid to try something new and we take responsibility for everything we do.
- Harmony

  That's why every contract, every presentation, every meeting, and everything we create reflects harmony.

We are ranked highly

The leading legal directories rank VJT & Partners highly across a wide range of practice areas. We are a full-service law firm but we are especially highly ranked in the following areas:

Transactions

We work for companies aiming to grow and expand and that want to enter the markets in the Hungarian and Central European regions by acquiring companies. We also work with medium and large-sized Hungarian companies looking to sell to domestic and foreign buyers.

"Our ultimate aim is to see the legal and business world through our clients' eyes."

- As an experienced market participant, we know everything about both acquisitions and sales.
- We provide more than legal advice. We provide tailor-made services by adjusting every segment of the deal planning to the client's business needs.
- We have a global reach. We have learned how to work with foreign law firms and how to manage teams of international lawyers.

Corporate advisory

Our firm is a trusted corporate advisor to a number of large firms in Hungary, providing support in all areas of corporate matters, e.g. corporate restructuring, capital structuring, loan syndication, employment, data protection and litigation.

"Sophisticated structuring is key for quality-driven advisory work."

- We translate legal jargon and legalese into business language.
- We always find innovative solutions for even the most complex corporate structures.

Digital transformation

Many of our clients are at the forefront of the digital transformation. We regularly examine issues that constantly arise in the context of digital transformations, e.g. finding the right IP strategy for new digital products and drafting contracts to mitigate the risks that come with transformation or compliance with regulations, in a challenging environment where technologies often evolve faster than law.

"Digital transformation drives the future and we are constantly working on becoming part of this future."

- We have decades of experience. We help our clients with digital transformation issues as soon as trends emerge.

- We dived right into the middle of the digital revolution. For years, we have been representing a Big Four Tech company on new emerging technologies.
- We are tech-savvy and up-to-date in terms of both technical knowledge and the laws that affect digital transformation businesses.

Regulatory & compliance

Our team has a vast experience in a broad scale of regulatory sectors including competition (covering all areas from consumer protection to cartel cases), data protection, anti-money laundering, energy, transportation, healthcare/pharma specific regulation and many other fields.

"Non-compliance risks have been continuously growing in the past few years."

- We assist businesses in internal audits, in-house training, legal advice, representation in front of regulators, litigation or whichever issue needs a level-headed legal evaluation.
- We strive to achieve a bulletproof, compliant solution, without compromising the clients' business needs.

Thank you for reading our handbook

We hope that our guide proved useful and gave you the information you need on how to do business in Hungary.

Please do not hesitate to contact us for more information.

Office:
1126 Budapest
Kernstok Károly tér 8.
Hungary

Contact:
Tel: +36 1 501 9900
Fax: +36 1 501 9901
E-mail: office@vjt-partners.com
Web: www.vjt-partners.com

00 36 1 501 9900

www.vjt-partners.com

office@vjt-partners.com

Kernstok Károly tér 8., 1126 Budapest, Hungary

VJT
&
PARTNERS