

Global Restructuring & Insolvency Guide

Hungary

Overview and Introduction

This Guide discusses various formal administrative procedures available to insolvent companies. The main objectives of Hungary's insolvency law are to protect and maximise the value of the insolvent company for the benefit of all creditors and also to reverse the company's financial position to one of solvency if possible.

As a member of the European Union, the Republic of Hungary continues to implement EU regulations relating to restructuring and insolvency.

Applicable Legislation

The legislation governing insolvency proceedings is Act XLIX of 1991 on Bankruptcy Proceedings and Liquidation Proceedings (the "**Bankruptcy Act**"), while the legislation governing the winding-up of a solvent company is Act V of 2006 on Public Company Information, Company Registration and Winding-up Proceedings. Act V of 2013 of the Civil Code (the "**Civil Code**") regulates the foundation, organisation and operation of business associations with a registered office in Hungary; the rights, obligations and responsibility of the founders and members (shareholders) of business associations; and the transformation, merger and demerger of business associations, as well as the winding-up of such associations without legal succession.

Corporate Restructuring and Insolvency

As a general rule, the Bankruptcy Act applies to economic operators (mostly companies) ("**companies**") and their creditors regarding bankruptcy and liquidation proceedings.¹ The Bankruptcy Act does not apply to individuals. The provisions of the Bankruptcy Act apply to associations and foundations if special legislation pertaining to those entities does not provide otherwise.

The Bankruptcy Act covers bankruptcy proceedings and liquidation proceedings.

Meanings of "Bankruptcy" and "Liquidation"

In a "bankruptcy proceeding" the debtor is granted a moratorium to negotiate and enter into debt restructuring agreements with its creditors ("**bankruptcy**").

"Liquidation" is the proceeding aimed at providing satisfaction to the creditors of an insolvent debtor upon its dissolution and termination of its corporate existence ("**liquidation**").

All assets held by the company under a bankruptcy or liquidation proceeding at the time of the opening of the proceeding, as well as all assets acquired during the proceeding, are the subject of the bankruptcy or liquidation proceeding. The assets of an economic operator comprise all assets that it owns or controls.

Bankruptcy and liquidation proceedings are non-judicial proceedings conducted – as a general rule – by the tribunal (the "**tribunal**") of competence and jurisdiction by reference to the debtor's registered office of record on the day when the request for opening the proceedings was submitted. A request for the opening of bankruptcy proceedings submitted at other courts will be automatically refused – or if a

¹ In addition to companies, the Bankruptcy Act applies to other legal entities, e.g. public-benefit organisations, law offices, European public limited liability companies, European cooperative societies, water management companies and forest management associations. Special rules may apply to certain of these entities.

proceeding has been opened, the progress will be terminated – and will be transferred to the competent court.

Bankruptcy

Bankruptcy can be initiated at the request of the debtor.

Debtor's Petition for Bankruptcy

The debtor – through its mandatory legal representative – may submit a petition if in possession of the prior consent of the supreme body of the debtor exercising founders' (shareholders') rights. In the case of companies with a sole shareholder, the petition may be submitted by the shareholder at his own discretion. Employees and trade unions, as defined in the Hungarian Labour Code, or the competent workers' councils (shop stewards) must be duly informed when such a petition is filed.

The petition may be submitted electronically on a standard template form prescribed in specific legislation.

Commencement of the Bankruptcy Procedure

The bankruptcy proceeding opens on the day on which the final ruling of the tribunal ordering the bankruptcy procedure is published in the Hungarian *Company Gazette* (the "**Commencement Date**").

Debtor's Petition for Bankruptcy – Temporary Moratorium

Upon the debtor's request for the opening of a bankruptcy proceeding, the tribunal provides – within one working day – for the publication of the request in the *Company Gazette*. The debtor is entitled to a temporary moratorium from the date on which the request is published in the *Company Gazette*.

The Temporary Moratorium and the Moratorium

The objective of the temporary moratorium and moratorium (hereinafter referred to collectively as the "**moratorium**") is to preserve the assets under bankruptcy protection with a view to reaching a compromise with the creditors. During the moratorium the debtor, administrator, financial institutions maintaining the accounts and creditors must refrain from taking any measure contrary to the objective of the moratorium.

The moratorium is effective from the Commencement Date and expires at 00:00 hours on the second working day after a 120-day period following publication in the *Company Gazette*.

Registration of the Claims

The creditors must register claims arising before the Commencement Date within 30 days after the Commencement Date, or within eight working days for claims arising after the Commencement Date.

Within five working days following the Commencement Date, the debtor must also directly notify its creditors – in a daily newspaper of national circulation and also on its website (if available) – to register their claims. The registration of claims is subject to a registration fee payable by the creditor to the administrator's current account.

Debt Restructuring Negotiation with Creditors

The debtor calls a meeting of creditors within a 60-day period following the time of the opening of bankruptcy proceedings for debt restructuring negotiation. The administrator and all registered creditors must be invited directly, with certain documents attached. Unknown creditors are invited by way of a posted notice.

The debtor – assisted by the administrator – prepares a restructuring plan or debt restructuring proposal to restore or preserve the debtor's solvency for presentation at the debt restructuring negotiation meeting.

A creditor holds voting rights in the debt restructuring negotiations if:

- It has registered its claim by the deadline specified in the Bankruptcy Act;
- It has paid the registration fee; and
- The claim is registered as acknowledged or uncontested.

The creditors have one vote awarded for each HUF 50,000 of their acknowledged or uncontested claim. Each creditor holding a claim below the HUF 50,000 threshold also has one vote.

A creditor who failed to participate notwithstanding the regular call will be counted as having voted "no".

Debt Restructuring

Debt restructuring means the debtor's agreement with the creditors laying down the conditions for debt settlement. In particular, this means: (i) any allowances and payment facilities relating to the debt; (ii) the remission or assumption of certain claims; (iii) the receipt of shares in the debtor company in exchange for a debt; (iv) guarantees for the satisfaction of claims and other similar securities; (v) the approval of the debtor's programme for restructuring and for cutting losses; (vi) and all other actions deemed necessary to restore or preserve the debtor's solvency, including the term of the debt restructuring agreement and the procedures to monitor the implementation of the debt restructuring arrangements.

A debt restructuring agreement may be concluded if the debtor is able to secure from the creditors a majority of votes in favour of the agreement. A debt restructuring arrangement applies to all creditors who registered their claims within 30 days after the Commencement Date, even if those creditors are non-consenting creditors who are otherwise entitled to participate in the debt restructuring agreement, and even if those creditors have failed to take part in the conclusion of the debt restructuring agreement. As a formal requirement, debt restructuring agreements have to be in written form.

Creditors who fail to register their claims within the 30-day deadline are not entitled to participate in the debt restructuring, and if the parties conclude a debt restructuring agreement, then the provisions of the agreement will not apply to such creditors. Furthermore, said creditors will no longer be entitled to enforce claims against the debtor that were not registered within the above-mentioned deadline. Notwithstanding the foregoing, if a third-party creditor initiates a liquidation procedure against the debtor, said creditors will be entitled to register their claims during the liquidation procedure, provided that those claims are not barred.

The debtor must notify the tribunal concerning the outcome of the debt restructuring conference within five working days – or 45 days before the expiry of the extended moratorium – at which time the tribunal delivers its decision on the approval of the debt restructuring arrangement. The tribunal approves the debt restructuring arrangements if the reports, agreements and statements verifying compliance with the above-mentioned regulations are attached.

If the parties fail to conclude a debt restructuring agreement, or if the arrangement is not in compliance with the statutory requirements, the tribunal *ex officio* will dismiss the bankruptcy proceedings and consequently declare the debtor insolvent in liquidation proceedings, at which time the tribunal is obliged to order the liquidation of the debtor.

Liquidation

Applicants for the Opening of Liquidation Proceedings

Liquidation proceedings are conducted, in the event of insolvency of the debtor, *inter alia*:

- *Ex officio* in the case of an unsuccessful debt restructuring negotiation as part of a bankruptcy proceeding;
- Upon request by the debtor or the debtor's receiver (in which case legal representation is compulsory);
- Upon request by a creditor (in which case legal representation is compulsory);

- Upon receipt of notice from the court of registry, if it has ordered the liquidation of the company; and
- Upon receipt of notice from a criminal court, if the enforcement procedure aiming for the collection of a fine imposed upon a legal person has failed.

If liquidation proceedings are requested by the debtor, the petition must comply with the relevant provisions applicable to the filing of a bankruptcy petition.

If liquidation is requested by a creditor, the petition must describe the legal title of the debtor's debt, the date of maturity (due date) and a summary of the reasons why the debtor is deemed insolvent. The foregoing must also be supported by documents attached to the request.

Commencement of the Insolvency Procedure

The tribunal investigates whether the debtor is insolvent (as described below) and orders the liquidation by decree if it finds that the debtor is insolvent. The tribunal opens liquidation within 60 days of the receipt of the petition for the liquidation proceedings. The date of the opening of liquidation proceedings is the date of the publication in the *Company Gazette* of the final decree opening the liquidation.

The tribunal declares the debtor insolvent in the following cases:

- Upon the debtor's failure to settle or contest its previously uncontested or acknowledged contractual debts within 20 days of the due date, and failure to satisfy such debt upon receipt of the creditor's written payment notice;
- Upon the debtor's failure to settle its debt within the deadline specified in a final court decision or payment order;
- If an enforcement procedure against the debtor was unsuccessful;
- If the debtor did not fulfil its payment obligation as stipulated in the debt restructuring agreement concluded in the course of bankruptcy or liquidation proceedings;
- If it has declared the previous bankruptcy proceedings terminated; or
- If – in proceedings initiated by the debtor or the receiver (appointed in case of the solvent winding-up of the company) – the debtor's liabilities exceed the debtor's assets, or the debtor was unable, and presumably will not be able, to settle its debt(s) on the date on which they are due, and – in proceedings initiated by the receiver – the members (shareholders) of the debtor fail to provide a statement of commitment, following due notice, to guarantee the funds necessary to cover such debts when due.

In the first two cases, liquidation proceedings may not be initiated if the amount of the claim against the debtor (not including interest and similar charges) does not exceed HUF 200,000.

If the debtor is not insolvent, the tribunal issues a priority order terminating the proceedings.

Registration of the Claims

The creditors must register their claims against the debtor within 40 days after the date of publication of the final decree upon opening the liquidation.

Appointment of the Liquidator

If the tribunal finds the debtor insolvent, the tribunal appoints a liquidator simultaneously with the opening of the liquidation.

The appointed liquidator takes control of the debtor from the directors, and only the liquidator is authorised to make any legal statements in connection with the assets of the company.

Creditors' Committee/Creditors' Representative

For the purpose of establishing a creditors' committee or appointing a creditors' representative, the liquidator convenes all registered creditors within 75 days following the date of publication of the opening of liquidation. The liquidator informs the committee, or the creditors' representative, at least 15 days in advance – or eight working days in advance in justified cases – of any contracts which exceed the scope of day-to-day operations, upon termination of valid contracts, and upon discarding the debtor's stocks, provided however, that the committee has the right to comment upon such actions within eight working days (or within five working days in justified cases) of receipt of notice. The liquidator forthwith informs the creditors' committee (or creditors' representative) of its reply to such comments, and of the measures taken in consequence. The liquidator sends a financial statement and gives an account of his activities to the committee (or creditors' representative) quarterly, and then reports on the financial status of the debtor and the costs of liquidation.

Role of the Liquidator

The liquidator analyses the financial standing of the company and the claims against it, prepares an opening liquidation account, estimates the costs of liquidation and sets up a timetable for its implementation. Upon request the liquidator presents the timetable to the creditors' committee, the creditors' representative or any of the creditors who are entitled to contest it in court.

The liquidator has powers (with limited exceptions, e.g. tenancy agreements of natural persons) to terminate, with immediate effect, the contracts concluded by the debtor or, if none of the parties rendered any services, the liquidator may rescind the contract.

The liquidator collects the claims of the debtor when due, enforces its claims and sells its assets. With the consent of the creditors, the liquidator may invest the debtor's property into private limited liability companies, public limited liability companies or cooperatives as non-pecuniary assets (contribution), if it promises to draw a better price this way.

The liquidator disposes of the debtor's assets through public sales at the highest market price by way of tender or auction. The liquidator may forego the application of these procedures only upon the prior consent of the committee, or if the estimated proceeds are insufficient to cover the costs of sale, or if the difference between the prospective proceeds and estimated costs is less than HUF 100,000. In the last case, the liquidator may utilise other public forms of sale for the purpose of achieving a more favourable result.

Clawback and Recovery Mechanisms

Liquidators have the power to investigate the affairs of the company and to take appropriate legal action against directors or third parties to recover certain assets or undo certain transactions for the purpose of increasing the estate available for distribution to creditors. Creditors also have the right to file a legal action before the court to contest certain contracts concluded by the debtor company for the purpose of increasing the insolvency estate (please see "*Actio Paulina*" below).

Liability of the Executives

Any creditor or the liquidator – in the debtor's name – may bring an action during the liquidation proceedings for the court to establish that the former executives of the company failed to properly represent the preferential rights of creditors in the three years prior to the opening of liquidation proceedings. This can be done in the wake of any situation carrying potential danger of insolvency, in consequence of which the company's assets have diminished, or where the executives failed to provide full satisfaction for the creditors' claims, or failed to carry out the cleaning up of environmental damages. Any persons with the power to influence the decision-making mechanism of the company will also be considered as executives of the company.

Any executive able to prove that, upon the occurrence of a situation carrying potential danger of insolvency, he took all measures that, within reason, are to be expected from persons in such a position in order to prevent and reduce the losses of creditors, and to prompt the supreme body of the debtor to take action, is not held responsible.

If the court establishes the liability of a former executive, any creditor may bring an action within a 60-day forfeit deadline following the final conclusion of liquidation proceedings. The court will order the debtor's former executive to satisfy the creditor's claim to the extent it has not yet been satisfied.

Actio Pauliana

The creditor and, on behalf of the debtor, the liquidator, may file a legal action before the court within 90 days from the time of gaining knowledge of the opening of liquidation proceedings, but not later than one-year from the date of publication, of the opening of the liquidation to contest:

- Contracts concluded by the debtor or its other commitments made within the five years preceding the date on which the tribunal received the petition for opening liquidation proceedings or thereafter, if intended to conceal the debtor's assets or to defraud any one creditor or the creditors, and the other party had or should have had knowledge of such intent;
- Contracts concluded by the debtor or its other commitments made within the two years preceding the date on which the tribunal received the petition for opening liquidation proceedings or thereafter, if intended to transfer the debtor's assets without any compensation or to undertake any commitment for the encumbrance of any part of the debtor's assets, or if the stipulated consideration constitutes unreasonable and extensive benefits to a third party; or
- Contracts concluded by the debtor or its other commitments made within the 90 days preceding the date on which the tribunal received the petition for opening liquidation proceedings or thereafter, if intended to give preference and privileges to any one creditor, such as the amendment of an existing contract to the benefit of a creditor, or to provide financial collateral to a creditor that does not have any.

If the contest is successful, the provisions of the Civil Code pertaining to invalid contracts will apply.

The liquidator, on behalf of the debtor, is also entitled to reclaim any service the debtor provided within a 60-day period preceding the date when the tribunal received the petition to open liquidation proceedings or thereafter, if it was provided to give preference to any one creditor and if such service is not usually provided under normal circumstances. Prepayment of a debt is, in particular, considered as giving preference or privileges to any one creditor.

Veil Piercing Rules in Connection with the Liquidation

In respect of the liquidation of a company under control by a qualified majority (75%), a sole member company or a sole proprietorship, the controlling party or the sole member (shareholder) is responsible, without limitation, for the company's liabilities not covered by the debtor's assets during the liquidation proceedings, if the court establishes the unlimited and full responsibility of such controlling party or member (shareholder) for the company's liabilities pursuant to a petition filed by the creditor during the liquidation proceedings or within a 90-day forfeit deadline following the final conclusion of liquidation proceedings, on account of such controlling party or member (shareholder) having had a history of making unfavourable business decisions from the standpoint of the debtor company.

Debt Restructuring Agreement in Liquidation

Following a period of 40 days subsequent to the publication of the opening of liquidation proceedings, the creditors and the debtor may, at any time, conclude a debt restructuring agreement before the final liquidation balance sheet is submitted.

A debt restructuring agreement is deemed valid if supported by the votes of at least half of the creditors with proper entitlement to conclude a debt restructuring agreement in all creditor groups – until their claims are satisfied – provided that the claims of these creditors account for two-thirds of the total claims of those entitled to conclude the debt restructuring agreement.

If solvency of the company is restored through debt restructuring, and the debt restructuring is in conformity with legal regulations, it is confirmed by the tribunal; otherwise the tribunal issues an order of rejection.

The tribunal terminates the liquidation proceedings if all registered debts, acknowledged or uncontested, of the debtor had been satisfied, and if the debtor provides guarantees for contested claims and for the liquidator's fee.

Rules of the Order of Satisfaction (Priority)

Secured Creditors

Secured creditors are entitled to enforce their security and accordingly, subject to the exception of the enforcement costs, will be paid in priority to all other debts to the extent of their security.

In order to ensure the priority ranking, the security holder must report its claim within 40 days. If the security holder fails to report its claim within 40 days, this does not prevent the sale of the pledged property; however, the proceeds must be handled separately and the security holder will be satisfied only if there are sufficient funds remaining after settlement is made according to the general rules of the order of satisfaction.

However, in case of any floating charge, only 50% of the proceeds from the sale of a charged property, less the costs of sale, will be used to satisfy the claims for which such property was charged.

General Order of Satisfaction

The debt of the company is satisfied from its assets subject to liquidation in the following order:

- (a) Liquidation expenses;
- (b) Claims secured by floating charge, up to the value of the pledged property and in consideration of the sums already paid, up to 50% pursuant to priority of the floating charge;
- (c) Alimony and life annuity payments, compensation benefits and income supplements to minors, which are payable by the debtor; furthermore, monetary aid granted to members of agricultural cooperatives in lieu of household land or produce, to which the beneficiary is entitled for his lifetime;
- (d) With the exception of claims based on bonds, other claims of private individuals not originating from economic activities (in particular claims resulting from insufficient performance or compensation for damages, also including the amount of the guarantee obligations ordinarily expected in the given trade, as calculated by the liquidator), claims of small and micro companies as well as small-scale agricultural producers;
- (e) Debts owed to social security funds, taxes and public debts collectable as taxes, repayable government subsidies, repayable state aid and financial aid from European Union and other international resources by virtue of international agreement, as well as public utility charges and condominium maintenance fees;
- (f) Other liabilities;
- (g) Irrespective of the time and grounds of occurrence, default interests and late charges, as well as surcharges and penalty and similar debts;
- (h) Claims (other than for wages and similar benefits, not exceeding six months' average earnings, that are less than double the prevailing minimum wage or, in the case of employees whose wages are paid on the basis of performance only, that are less than double the guaranteed salary specified in Subsection (6) of Section 138 of the Labour Code) held by:
 - (i) Any member (shareholder) of the debtor with majority control;
 - (ii) Any executive officer of the debtor;
 - (iii) Any executive employee of the debtor;

- (iv) The close relatives of the persons listed in (i) to (iii) above;
- (v) A company under the debtor's majority control; or
- (vi) A body (person) benefiting from the debtor's gratuitous commitments.

The liquidator must register the claims against the debtor which are reported after 40 days, but within 180 days of the publication of the opening of liquidation proceedings. These claims must be satisfied if there are sufficient funds remaining following the settlement of the debts according to the general rules of the order of satisfaction. Failure to observe the time limit of 180 days constitutes a waiver of rights.

Conclusion of Liquidation Proceedings

Based on the final liquidation balance sheet and the proposal for the distribution of assets, the tribunal rules on bearing the costs, the liquidator's fee, satisfaction of the claims of creditors, the closing of current accounts and abrogation of securities issued by the debtor by way of the central depository. Simultaneously, the tribunal concludes the liquidation and the dissolution of the debtor, along with the dissolution of any subsidiary of the debtor, where applicable.

If a debt restructuring agreement is concluded by the parties, the tribunal confirms the agreement by issuing a decree ruling on the conclusion of liquidation, the fee of the liquidator, the bearing of costs, and on the satisfaction of the claims of creditors excluded from the agreement.

If the debtor is dissolved by liquidation, the portion of assets remaining after the satisfaction of creditors' claims is distributed among the holders of capital notes in proportion to the subscribed capital shown in the closing balance sheet.

Special Regulatory Regime

A regulatory regime concerning particular companies has been implemented into the Bankruptcy Act. These particular companies comprise two groups:

- (i) The first group consists of companies (i) whose settlement of debt, debt restructuring or reorganisation assumes a strong national economical interest or privileged common interest or (ii) whose termination without a successor in a quick and transparent method assumes privileged national economic interests. The new regulatory regime implemented a detailed guideline upon which a company will be declared as a company of preferential status for strategic consideration by the government in the applicable governmental decree. Special provisions, as compared to the more general rules detailed above, apply to these companies, including, *inter alia*, (a) shorter deadlines for exercising rights and obligations under the Bankruptcy Act and (b) that administration of the liquidation process be undertaken only by a non-profit, state-owned entity appointed in the governmental decree.
- (ii) The second group consists of companies of preferential status for strategic consideration which also comply with additional requirements, i.e. they are secured by national security protection or they provide public services with international or national significance from a national security, law enforcement, military technology or energy supply perspective. Those companies will also be specifically appointed in a governmental decree by the government of Hungary. The provisions applicable with respect to the first group of particular companies apply to those companies, and the following special provisions also apply.

The tribunal will make an extraordinary moratorium available to these companies from the date the procedure begins until the tribunal decides on the insolvency of the debtor company, which moratorium will ensure the provisional ongoing operation of those companies. During the sale of the assets of the debtor company the common economic interest will be taken into account, and the state liquidator will sell the assets (including movables, real estate and intellectual property) as a working unit. Furthermore, it is not obligatory to organise a public procurement process; the assets of these companies may be sold via closed offering procedures at the discretion of the state liquidator.

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