

## Real Property Investment Law in Hungary



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## **TITLE**

### **Full ownership**

#### *General*

Full ownership of real property is recognised under Hungarian law. The Constitution of the Republic of Hungary guarantees the right to real property.<sup>1</sup> Expropriation shall only be permitted in exceptional cases when such action is in the public interest, in the manner stipulated by law and with provision of full, unconditional and immediate compensation.

#### *Acquisition*

Full ownership of real property is acquired by the registration of title in the land registry based on a written document countersigned by an attorney or prepared in the form of a notarial deed. This registration validates the transfer retrospectively as of the date of the registration application and makes the transfer of title binding on third parties. Ownership rights are proved by providing a land registry extract.

Real property may be acquired by:

- sale and purchase of the real property;
- lease of the property with an option to purchase;
- becoming a majority shareholder of a company that actually holds among its assets the real property;
- the contribution in kind of real property to a company, either upon establishment of the company or subsequently by way of an increase in capital where the totality of the new shares are obtained by the person contributing the real property and then subsequently the shares corresponding to the contribution of the real property are purchased by a purchaser;
- 15 years of continuous and non doubtful possession. Possession must be evident (through investments, maintenance etc.);
- succession or donation.

#### *Ownership of buildings and land use rights*

Generally, all buildings and structures erected on land belong to the owner of the land. However, it is possible in Hungary to acquire the ownership of a building without the underlying land. This may only occur if the owner of the land and the constructor enter into a written agreement before the construction of the building. In this case, the constructor is the owner of the building and benefits from a land use right over the land. A land use fee is paid by the owner of the building to the owner of the land. The land and the building are registered separately in the land register, where the land use right is mentioned. The owner of the land has a statutory pre-emption right in respect of the building, while the owner of the building has a statutory pre-emption right in respect of the land.

### **Limitations on acquisition**

The acquisition of full ownership over real property located in Hungary by foreigners or foreign companies requires a prior permit from the local administration office. Acquisitions made without the requisite permit are null and void. Agricultural land may not be acquired by Hungarian legal entities or foreigners except for farms not exceeding 6,000 sq. m. with a dwelling house.

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<sup>1</sup> Article 16 of the Constitution of the Republic of Hungary.



European Union companies<sup>2</sup> may acquire non-residential and non-agricultural property without limitation. EU citizens may freely acquire commercial property and residential property if they plan to establish their main residence in Hungary. EU citizens may not acquire secondary residences and agricultural land until 1<sup>st</sup> May 2011.

### **Protection of ownership by courts**

In Hungary there are no particular difficulties regarding protection of real property ownership. There is no uniform register of re-privatisation in Hungary. It is important to check whether there are any re-privatisation claims in relation to given real property.

## **INTERESTS IN REAL PROPERTY CAPABLE OF REGISTRATION**

The following interests and property-related rights, and the holders of such, may be recorded in the real property register: ownership rights (in Hungarian “*tulajdonjog*”), and asset management rights in respect of real estate owned by the state or local governments (in Hungarian “*vagyonkezelői jog*”), permanent right of use for members of housing cooperatives (in Hungarian “*állandó használati jog*”), land use on the basis of agreement or court decision (in Hungarian “*földhasználati jog*”), usufruct and the right of use (in Hungarian “*haszonélvezeti és használati jog*”), easement rights (in Hungarian “*szolgalmi jog*”), right of use for the placement of power supply equipment (in Hungarian “*villamosberendezések elhelyezését biztosító használati jog*”), cable rights (in Hungarian “*vezetékjog*”), water line and mining easement rights (in Hungarian “*vízvezetési és bányaszolgalmi jog*”), easement rights and utilisation rights in the public interest (in Hungarian “*közérdekű szolgalmak és használati jogok*”), contractual or statutory right of first refusal (in Hungarian “*törvényen vagy szerződésen alapuló elővásárlási jog*”) and right of repurchase (in Hungarian “*visszavásárlási jog*”) and option to purchase (in Hungarian “*vételi jog*”), right of support and life annuity (in Hungarian “*tartási és életjáradéki jog*”), mortgage and independent lien (in Hungarian “*jelzálogjog*” and “*önálló zálogjog*”), and right of legal enforcement (in Hungarian “*végrehajtási jog*”).

These interests can be granted either by an agreement concluded by the parties or by an administrative or court decision. Some of these interests may be granted for a definite period (e.g. option right may be granted up to 5 years) or an indefinite period (e.g. usufruct remains valid until the death of the beneficiary). An interest, being a right which affects the property of the land, is transferable with the land. The purchaser acting in good faith who acquires the land encumbered with a registered interest has the same obligations towards the beneficiary of the interest as the initial owner. Therefore, the acquisition of land or buildings requires a careful examination for the existence of interests.

## **THE DEVELOPMENT OF LAND**

### **Rezoning of agricultural land**

Agricultural land can be used for non-agricultural purposes after obtaining the authorisation of the local land registry office.<sup>3</sup> A new piece of legislation introduced in 2007, effective as of January 2008, entitled the Act on the Protection of Agricultural Land, provides for a novel type of fee, called ‘soil protection fee’ (in Hungarian “*talajvédelmi járadék*”) which is to be paid if agricultural land is rezoned and used for non-agricultural purposes, and it is meant to be incentive for developers to protect, re-use or sell humus-rich soil (given that the fee is reduced under these conditions).

<sup>2</sup> The same rule applies to companies from the European Economic Area.

<sup>3</sup> Article 9 of Act CXXIX of 2007 on the Protection of Agricultural Land.



These plots may only be incorporated in urbanised areas or rezoned for development in compliance with the progress of the local master plans. An issued authorisation shall become void if the alternative use is not commenced within 4 years or if the holder of the authorisation states in writing that he does not avail himself of the rights conferred by the authorisation.

### **The master plan and local plan**

The Construction Act 1997<sup>4</sup> determines that the local government shall adopt a structural plan, a zoning map and a local building code in respect of each settlement. In the case of Budapest, each local municipality decides planning matters with regard to the master plan of Budapest, the local structural plan and local building code.

### **Building permitting process**

#### *Preliminary building construction permit*

A person interested in ascertaining the requirements to construct a building may apply to the local municipality to issue a final and enforceable preliminary permit (in Hungarian “*elvi építési engedély*” or “*elvi telekalakítási engedély*”).<sup>5</sup> Such permit is valid for one year. Its validity may be extended once by no more than one additional year provided that the relevant legislation has not changed.

#### *Building construction permit*

Under the provisions of the Construction Act 1997, a building authority permit (in Hungarian “*építési engedély*”) shall be obtained from the local municipality for the construction, remodelling, expansion, renovation, rehabilitation, improvement, demolition, relocation or modification of the original function of a structure or a section thereof or group of buildings. A building authority permit may be conditional.

In order to obtain a permit, an application must be made to the local municipality by submitting the title deeds, the architectural drawings, the structural drawings, and the electrical and mechanical installation drawings. The plans have to comply with the applicable zoning requirements. The building authority will conduct an on-site inspection as part of the permit application evaluation procedure. If the application is complete, the authorities shall grant the permit within 60 days at the most. If the application is incomplete or irregular in any way, the permit will be issued only after the deficiencies or errors are remedied. A fee is charged for the construction permit.

The specialised authorities and other organs specified in separate legal regulations and the registered technical experts participate in the permitting procedure and give their approval prior to the issuing of the building authority permit; the deadline for their approval is 15 days, which can be extended for another 15 days, outside of the deadline of 60 days for the permit.

The construction must start within two years from the issuance date of the construction permit. If construction does not commence within two years, a renewal of the permit can be requested.

#### *Occupancy permit (use of the construction)*

The developer is required to obtain an occupancy permit (in Hungarian “*használatbavételi engedély*”) from the local municipality for all structures and sections thereof for which a building permit was required. Without the occupancy permit the structure cannot be used.

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<sup>4</sup> Act LXXVIII of 1997 on the Formation and Protection of the Built Environment (in Hungarian “*az épített környezet alakításáról és védelméről*”).

<sup>5</sup> Article 35 of the Construction Act 1997.



The application for an occupancy permit must attach declarations from the appropriate specialised authorities, the relevant public utility companies, the chimney sweeper company (building engineer) and the construction superintendent. These declarations must state that the structure and the work completed are conformed to the building permit, to the approved permit plans and that the building is suitable for proper and safe occupancy. If the application or declarations are in some way deficient a conditional occupancy permit may be granted.

## **LEASES**

Hungarian law distinguishes between two types of leases: commercial leases and leasehold. Leasehold is typically used for agricultural land.

### **Commercial leases**

Commercial leases are regulated by the Hungarian Civil Code and the Lease Act 1993.<sup>6</sup>

### **Leasehold**

Under a leasehold agreement<sup>7</sup>, the tenant is entitled to use and collect the proceeds of a designated parcel of agricultural land or other profitable property for a specific period of time. The tenant is obliged to pay appropriate rent for this privilege. A written contract is required to lease agricultural land and administrative approval may be required by law. Leasehold payments may be made in cash or in kind. Leasehold payments are made in arrears as required by law.

The tenant shall be entitled to use and collect the proceeds of the leased land only in accordance with the principle of proper management. Unless otherwise prescribed by law, any sublease of agricultural land shall be null and void.

## **COMMERCIAL LEASES**

### **Leasing with an option to purchase**

Leasing with an option to purchase is a *sui generis* contract not regulated in the Hungarian Civil Code. The applicable rules stem from civil law, banking law, tax law and case law. This type of contract combines the rules on lease agreements<sup>8</sup> and some of the rules on payments in instalments.<sup>9</sup> There are two primary forms of leasing with an option to purchase: (1) a simple leasing with an option to purchase (in Hungarian “*lizing*”) and (2) a financial leasing (in Hungarian “*pénzügyi lizing*”).

Simple leasing with an option to purchase is a lease contract for a determined duration at the end of which the landlord grants the tenant an option to purchase the real property.

Financial leasing is a lease under the terms of which a leasing company (credit institution) acquires a real property pursuant to the request of a client, in order to lease that real property to that client for a certain duration. The leased property is registered in the financial accounts of the beneficiary during the performance of the contract. The client pays for all the expenses incurred in the acquisition and lease transaction in exchange for the use and quiet enjoyment of the real property.

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<sup>6</sup> Act LXXVIII of 1993 on the lease of dwelling apartments and other premises.

<sup>7</sup> Articles 452-460 of the Hungarian Civil Code.

<sup>8</sup> Article s 423 and 434 of the Hungarian Civil Code.

<sup>9</sup> Article 376 of the Hungarian Civil Code.



At the end of the lease, the client has the option to acquire the real property or surrender the lease to the leasing company.<sup>10</sup> Only institutions authorised by the Hungarian Financial Supervisory Authority may grant financial leases. The instalments paid by the tenant to the landlord during the lease period may not entirely be taken into account - subject to the applicable tax regime - as costs against income from accounting and tax purposes.

### **Operative leasing without option to purchase**

Operative leasing (in Hungarian "*operatív lízing*") without an option to purchase is a *sui generis* contract, not regulated in the Hungarian Civil Code. The applicable rules stem from civil law, banking law, tax law and case law. Operative leasing agreements combine the rules on lease agreements<sup>11</sup> and some of the rules on payments in instalments<sup>12</sup>. The commercial and bookkeeping treatment of operative leasing is similar to that of the financial leasing. The main difference is that a tenant of an operative leasing agreement may not purchase the real property at the end of the lease period. The real property needs to be physically handed back to the landlord who owns the real property during the entire lease period. The tenant may consider the paid instalments as operational costs, and may deduct them - subject to the applicable tax regime - from the realised income of the company.

### **Statutes regulating the leasing of commercial premises**

The Hungarian Civil Code and the Lease Act 1993 regulate the leasing of commercial premises.<sup>13</sup> The Hungarian regulation of lease agreements is characterised by freedom of contract.

### **Form**

Commercial leases are usually concluded in writing. There are no other legal requirements regarding the form of the lease agreement.

### **Duration**

Hungarian law does not specify the duration of commercial leases. Therefore, definite or indefinite terms are possible.

### **Termination**

Any lease agreement may be terminated by the mutual agreement of the parties. Unless otherwise agreed, subject to a notice period any party may at any time unilaterally terminate a commercial lease where the term is for an indefinite period. Unless agreed otherwise, the notice period is at least one year in case of termination by the landlord and at least 15 days in case of termination by the tenant.

### **Right of renewal**

The tenant has no statutory right of renewal.

### **Pre-emption right of tenant**

Hungarian law does not grant a tenant pre-emption rights over commercial premises.

### **Rent and rent cap**

It is mandatory to indicate the rent in HUF or in another currency at the moment of finalisation of the lease agreement, otherwise the lease is considered null and void. Hungarian law does not provide for any rent caps for commercial leases.

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<sup>10</sup> Establishment of Credit Institutions and Financial Enterprises Act 1996 (Act CXII of 1996).

<sup>11</sup> Article s 423 and 434 of the Hungarian Civil Code.

<sup>12</sup> Article 376 of the Hungarian Civil Code.

<sup>13</sup> Act LXXVIII of 1993 *on the lease of dwelling apartments and other premises*.



### **Rent review**

Hungarian law does not stipulate any rent indexation provisions for commercial leases. Therefore, rent is adjusted in accordance with contractual provisions agreed by the parties. European Consumer Price Indexes, US Consumer Price Indexes or the Consumer Goods and Services Price Index published by the Hungarian Statistics Office are often used.

### **Costs rechargeable to tenants**

Generally, all costs may be recharged to a commercial tenant.

### **Improvements**

Unless otherwise agreed, after termination the tenant must return the leased premises in their initial condition; subject to usual depreciation. It is customary to settle these questions in the lease contract by stating that if a tenant has carried out improvements, the landlord is entitled, at the end of the lease, either to keep the improvements in consideration for a payment equal to their value at the time the leased premises reverts to the landlord or may require the tenant, at his expense, to restore the leased premises to their original condition.

### **Transfer of lease by tenant**

Transfer of the lease by the tenant without the prior consent of the landlord is not permitted.

### **Sublease**

Subletting without the prior consent of the landlord is not permitted.

### **Maintenance**

During the term, the landlord must maintain the building and its essential equipment (central heating, gas and water pipes, elevator etc.). The tenant is responsible for minor maintenance and renovation. The parties should clearly specify maintenance obligations because the provisions of the Hungarian Civil Code concerning maintenance obligations are open to interpretation.

### **Permitted use**

The parties are not obliged to indicate the nature of the business to be exercised in the premises. Some uses require the prior approval of local authorities. The tenant is responsible for obtaining this approval.

## **TAX**

### **Transaction costs**

*Sale of land and buildings*

### **VAT**

Value added tax (in Hungarian "*általános forgalmi adó*" or "*ÁFA*") is governed by the new VAT Act 2007<sup>14</sup> (applicable as of 1<sup>st</sup> January 2008) and the 2006/112/EC VAT Directive.

In principle, the sale of immovable property (including buildings and connected land, as well as other land) is tax exempt, except for the following:

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<sup>14</sup> Act CXXVII of 2007 repealing Act LXXIV of 1992.



- a building and its land if not yet put into use;
- a building and its land if already in use but the occupancy permit was issued not earlier than 2 years prior to the sale; or
- building plots.

The applicable VAT rate is 20%.

However, taxpayers may opt for the application of the general VAT regime when selling property even if the sale would be exempt from VAT. The choice for the latter should be filed with the tax authority by 31<sup>st</sup> December of the year preceding the VAT-able sale. If this is not filed in time, there is no possibility to charge VAT on the sale, and the input VAT incurred on goods and services received in relation to the sale will not be deductible. In the case of a choice for taxation, the taxpayer may not return to the tax exemption for five years.

No VAT is due upon the sale of a participation in a real property company.

### Stamp duty

The transfer of real property for consideration is subject to transfer tax (in Hungarian "*visszterhes vagyónátruházási illeték*") payable by the purchaser, calculated on the market value of the property transferred.

The duty on transfer is usually 10% of the market value, while the duty on the transfer of residential property is 2% for the first HUF 4 million (approximately EUR 15,500) and 6% for anything above that amount.

The acquisition of a building site may be exempt from stamp duty provided that the purchaser undertakes to build a residential building on the real property within four years.

The acquisition of real property by a property investment fund or by an entrepreneur engaged in trading property or financial lease may qualify for a special regime, in which the purchase is only subject to a duty of 2% transfer tax.

Contributions in kind of real property to a company are subject to the same transfer tax as other acquisitions. However, the assets acquired by the legal successor through a transformation are exempt from stamp duty.

If real property is sold by selling the shares of a company holding real property no transfer tax liability would arise.

## **Taxation of capital gains**

### *Capital gains realised by a private individual*

Personal income tax (in Hungarian "*személyi jövedelemadó*") is regulated by the Personal Income Tax Act 1995.<sup>15</sup> All gains arising from the sale of real property are subject to tax as of the date of filing the sale and purchase contract with the land registry or, if there is no such obligation, as of the date of the signature of the sale and purchase contract. The tax rate applicable to income arising from the transfer of the property is 25%.

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<sup>15</sup> Act CXVII of 1995.



The taxable income is the income received for the property reduced by the following charges:

- the original acquisition price of the property and related costs;
- the investments increasing the value of the property; and
- other expenses incurred in the course of the sales transaction.

The tax regime changed considerably as of 1<sup>st</sup> January 2008. Until that date, the sale of residential property was exempt from tax if the income received was used to acquire another residential property within the 12 months preceding or within the 60 months following the sale. This exemption has been abolished.

As a general rule, the legislation continues to provide that for the sale of real property, the taxable income is gradually reduced by a certain percentage each year starting from the 6<sup>th</sup> year after the original acquisition, making the sale exempt from income tax if the sale happens in the 15<sup>th</sup> or further years after the original acquisition. From 1<sup>st</sup> January 2008, for the sale of residential property, the taxable income will gradually decrease from the second to the fourth year after the original acquisition, making the sale fully exempt from income tax already from the 5<sup>th</sup> year after the original acquisition.

The profits of contribution in kind of property, or of attached rights, are taxed in the same way as profits made through the sale. In such a case, the profit is calculated based on the value of the property as indicated in the articles of association of the company receiving the contribution.

#### *Capital gains realised by a corporate entity*

Hungarian corporate income tax (in Hungarian "*társasági adó*") is governed by Corporate Income Tax Act 1996.<sup>16</sup>

Corporate profits including income from the lease or sale of property are subject to a 16% corporate income tax and a 4% "solidarity" surtax. Under certain conditions, the corporate income tax is only 10% of the portion of the positive tax base up to 50 million HUF, and 16 % for the part above that sum.

Under the corporate income tax rules, accounting depreciation is a tax base increasing item while tax depreciation reduces the tax base. The Corporate Income Tax Act 1996 sets out the tax depreciation rates between an annual 2% to 6%, depending on the structure of buildings.

Local business tax at a maximum of 2% of the annual adjusted turnover (i.e. the net sales revenue minus acquisition cost of goods sold, mediated services and cost of materials) may also apply on the sales income. This tax is levied by the local municipality, and as such the rates may differ in each local jurisdiction. 200% of the local business tax is deductible for corporate income tax purposes if relevant conditions are met. The Municipality of Budapest levies a 2% local business tax.

#### **Leases**

##### *VAT*

The lease of any property is exempt from VAT. However, taxpayers may opt for the application of the general VAT regime when letting property. The choice for the latter should be filed with the tax authority by 31<sup>st</sup> December of the year preceding the VAT-able lease. If this is not filed in time, there is no possibility to charge VAT on the rent, and input VAT incurred on goods and services received in relation to the letting activity will not be deductible. In the case that the taxpayer chooses taxation, the taxpayer may not return to the tax exemption for five years.

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<sup>16</sup> Act LXXXI of 1996.



### *Personal income tax*

The proceeds of lease or rental of property is considered as income, subject to tax at a 25% rate.

### *Corporate income tax*

Income resulting from the lease of property is taxed as part of the corporate profits at 16% CIT and 4% "solidarity" surtax, both taxes being levied on the modified accounting profits.

In general, real property used for retail, logistics or offices may be depreciated at a rate of 2% - 6% (the actual rate depends on the expected lifespan of the material of the superstructure). If the real property is leased, the landlord may apply an annual depreciation rate of 5%. Rights connected to real property may be depreciated at a rate defined by the accounting policy of the company.

## **Property tax**

### *Building tax*

Property tax on buildings (in Hungarian "*épitményadó*") may be imposed by local municipalities. It is an annual levy on the persons registered as the owners as of 1<sup>st</sup> January of the given year. The tax may either be calculated based on the area of the building or on its adjusted market value, depending on the decision of each local municipality. The adjusted market value of the property is 50% of the market value for transfer tax purposes.

The annual rate is determined by the local municipality and therefore varies from region to region. The upper limit of the rate is fixed at HUF 900/sq. m. (approximately EUR 3.5/sq. m.) or at 3 per cent of the adjusted market value of the building.

The following real properties are not subject to building tax:

- premises of social organisations, religious organisations, foundations, public service organisations, public corporations, non-profit companies, etc., if in the previous year they incurred no corporate tax liabilities as the result of business activities;
- buildings used by social, health, educational and child welfare institutions, or for public administration, and buildings used for the purpose of animal husbandry, etc;
- registered historical buildings that are to be renovated, for 3 years after the construction permit has been issued.

### *Land tax*

The owner of undeveloped land situated in the territory of an urban area may be taxed (in Hungarian "*telekadó*") by the relevant local municipalities. The tax is payable by the person who is the registered owner on the 1<sup>st</sup> January of the given year.

The method of calculation is the same as that for the building tax. According to the decision of the local authority it may be calculated on the basis of the area of the land or its adjusted market value.

Land used for public transport, land subject to building prohibitions and land subject to building tax are exempt from land tax.

The upper limit of the tax is fixed at HUF 200/sq. m. (approximately EUR 0.77/sq. m.) or at 3% of the adjusted market value of the land.



## **LEGAL COSTS REGARDING REAL PROPERTY ACQUISITIONS**

### **Notary fees**

Notarial deeds are not required for real property transactions.

### **Lawyers**

All documents related to real property transactions which are filed with a land registry for registration must be executed in writing and countersigned by a Hungarian attorney. Lawyers and their clients are free to determine the fees charged for the due diligence, the drafting of the contract and the land registry procedure.

### **Land registry**

Entries into the Land Registry (in Hungarian "*ingatlannyilvántartás*") are subject to fees of a nominal amount.

### **Publication**

There is no specific obligation of publication. The Land Registry itself is public.

## **SECURITY USED IN REAL PROPERTY FINANCINGS**

### **Mortgage**

Hungarian law recognises the mortgage as the only type of lien pertaining to land and buildings. The parties may also create a limited security lien to secure claims originating from a legal relationship or a legal title stipulated in the lien agreement. A floating charge may also encumber all assets of a person, including real property.

Only real property that is individually registered in the land registry can be subject to a mortgage. An agreement establishing a mortgage over property must be concluded in writing and the mortgage must be entered in the land registry.

Mortgages generally terminate when obligations arising from the main agreement between the parties are wholly performed. A mortgage may also terminate if the property is sold by common agreement of the parties. In such a case, the creditor has a pledge on the purchase price of the real property sold.

The mortgage ends if the mortgaged property is sold to the mortgagee. However, the mortgage subsists towards the creditors with a lower ranking. Mortgage agreements usually provide that the mortgagor must not do any of the following without the prior consent of the mortgagee (unless expressly permitted):

- create or permit to subsist any security on the real property (other than the security created by the security agreements with the financing bank);
- sell, transfer, license, lease or lend or otherwise dispose of the real property; or
- take any measures or make any declarations which infringe or limit the mortgagee's rights under the mortgage agreement in any material respect.

Unless otherwise provided by law, satisfaction from the mortgaged property may only occur on the basis of a court order by a writ of execution.



The security holder may also require the registration of a restriction on transferring and encumbering the real property in the land register.

#### *Formalities*

The mortgage can be registered based upon a notarial deed or an agreement countersigned by a Hungarian attorney. Usually notarial deeds are preferred, since the execution of a notarial deed is easier.

#### *Costs*

The costs in connection with the registration of a mortgage consist of the costs of (1) the preparation of the notarial deeds (based upon the fee tariff for notaries which depends on the amount of the mortgage), and (2) the registration fee at the land registry (not a significant amount).

### **Other common security**

#### *Cash and securities deposits*

Financial collateral may be provided under a financial collateral arrangement to secure cash, money on account, debt or equity securities and other financial instruments. In each case the collateral is effective upon delivery of the relevant financial collateral.<sup>17</sup> If the financial collateral given as security is constituted on any other asset, such as movable property, for example, the laws and regulations on mortgages and pledges shall apply. Delivery means any procedure upon which the financial collateral is transferred from the possession of the depositor to the possession of the beneficiary. Therefore delivery will occur when a beneficiary's bank account, securities account or securities deposit account is credited.

#### *Security assignment of rights or receivables*

An obligor may assign its commercial, trade or other financial receivables as security interests via a security assignment agreement. The assigned receivables are collected in a receivables account maintained with the assignee (in case it is a bank). The assignor may use the balance of the collection account until the occurrence of an event of default. The security assignment agreement does not need to be notarised or registered in any public record in order to be valid. Though the assignment of accounts or accounts receivable is not part of the rules relating to security interests under the Hungarian Civil Code, it is very often used in Hungary in various corporate and finance activities.

#### *Pledge over contractual rights/claims and bank accounts*

A pledge can be taken over a contractual right and/or claim. A pledge must take the form of a written agreement. No additional requirements are necessary. It may include future rights and claims that are created in favour of the pledgor. If the right or claim is evidenced in an official record (e.g. the land register) and the formal registration is a legal prerequisite, the pledge over rights and/or claims shall be effective only from the date of registration.

A pledge over bank accounts takes the form of a notarised document. In this manner the document can be registered in the pledge register. Typically, in a pledge of bank accounts agreement the pledgor (the borrower) pledges all of its rights in respect of all of the security assets (all of the pledgor's rights in respect of any amount standing to the credit of any security account and/or payable under any security account) to the pledgee (the bank) to secure all present and future obligations and liabilities of the borrower (secured obligations). The notary's fees will depend on the value of the security given.

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<sup>17</sup> Article 270 of the Hungarian Civil Code.



### *Pledge over shares and/or quotas*

Another common form of security is a pledge over the shares or quotas (in Hungarian “üzletrész”) of the project company (borrower). The pledgors (shareholders of the borrower) will pledge the whole of the borrower’s registered capital (shares or quotas) owned by them or held by any nominee on their behalf by way of the shares or quota pledges.

Pledges over shares or quotas take the form of a notarised document. In this manner the document can be registered in the chattel register kept by public notaries. The notary’s fees will depend on the value of the security given.

### **Fixed charge**

No specific legislation exists under Hungarian law concerning fixed charges. Therefore, a fixed charge can be any of the following:

- (a) a mortgage over real property; or
- (b) a mortgage over specific movable properties, whether created directly pursuant to a contract, or through conversion of a floating charge which is registered in the chattel register; or
- (c) a possessory lien; or
- (d) a pledge over rights and claims.

### **Floating charge**

A floating charge security interest can be created over all or part of the changing assets of a company. It is created by a security document which is notarised and then registered in the chattel register kept by public notaries. The floating charge catches (subject to its precise terms) any and all present and future property owned by the obligor. It is effective against third parties from the date of registration in the chattel register. Other security interests may rank prior to the floating charge if (1) registered first in time or (2) a fixed charge (except for mortgage over specific chattel properties) at anytime.

On the occurrence of certain specified crystallisation events (e.g. insolvency or an event of default) the floating charge "crystallises" on all of the assets of the obligor *or the beneficiary may, alternatively, specify the assets on which the floating charge "crystallises"*. As a result, the assets (or specified assets) of the obligor will be charged with specific, crystallised fixed charge security interests. The (fixed charge) security interest(s) created by the crystallisation must be registered into the chattel register or the land register (as appropriate) in order to be valid.

### **Corporate guarantees and suretyship**

It is common practice for a beneficiary to request corporate guarantees from creditworthy business associations, parent companies, international trade organisations or insurance companies. There are no rules on such guarantees in the Civil Code. Therefore, the rules relating to bank guarantees are applied, which require that they be (1) up to a specific amount (2) for a predetermined time (3) enforceable under certain conditions. In practice, such guarantees are often expressly stated to be irrevocable and unconditional. Often these guarantees will themselves be secured.

In Hungary a suretyship must take the form of a written agreement. The obligation of a surety always depends on the secured obligation. However, it includes any accessory services (such as eventual cost and/or payment obligations) that are due after the suretyship is undertaken. The surety may invoke the same objections as those available to the obligor against the beneficiary. A surety is entitled to request that the beneficiary first seek satisfaction from the debtor and/or from other sureties who assumed suretyship before it (*simple suretyship*). This shall not be the case if (1) the parties have agreed otherwise, (2) a suretyship was assumed for indemnification, or (3) suretyship was assumed by a bank (*absolute suretyship*).



### **Lender's right of purchase**

This is a specific type of quasi-security arrangement which is particular to Hungary. The obligor may grant a right of purchase (a call option) to a beneficiary (almost always a bank lender) in respect of any of its property (real property, stock, cars, other assets etc.) exercisable from the date of occurrence of an event of default. If the right of purchase is given in respect of real property then it must be registered with the land register in order to be enforceable against third parties. The security document needs to stipulate carefully the events of default under which the beneficiary may exercise the right and the purchase price of the relevant property. Right of purchase, being a call option, can be established for a maximum period of 5 years.<sup>18</sup> Should the parties wish to extend the right, they ought to consider agreeing a separate contract that would enter into force at the time prior to the initial contract expiry for a further term of 5 years. Upon exercise of the right of purchase, the beneficiary becomes the owner of the asset. The obligor must grant possession of the real (or other) property to the beneficiary within a time period specified in a call notice set out in the right of purchase. The beneficiary will have to sell the “purchased” property in order to recover the (cash) amount owed to it.



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<sup>18</sup> Articles 375(4) and 374(2) of the Hungarian Civil Code.



### *About the Law Firm*

**Gide Loyrette Nouel** is an international law firm that has been advising real estate investors since 1920. Gide Loyrette Nouel has been present in Central and Eastern Europe since 1991.

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