The Corporate Governance Review

Third Edition

Editor
Willem J L Calkoen

Law Business Research

The Corporate Governance Review

Reproduced with permission from Law Business Research Ltd.

This article was first published in
The Corporate Governance Review, 3rd edition
(published in April 2013 – editor Willem J L Calkoen).

For further information please email
Adam.Sargent@lbresearch.com

The Corporate Governance Review

Third Edition

Editor
Willem J L Calkoen

Law Business Research Ltd

THE LAW REVIEWS

THE MERGERS AND ACQUISITIONS REVIEW

THE RESTRUCTURING REVIEW

THE PRIVATE COMPETITION ENFORCEMENT REVIEW

THE DISPUTE RESOLUTION REVIEW

THE EMPLOYMENT LAW REVIEW

THE PUBLIC COMPETITION ENFORCEMENT REVIEW

THE BANKING REGULATION REVIEW

THE INTERNATIONAL ARBITRATION REVIEW

THE MERGER CONTROL REVIEW

THE TECHNOLOGY, MEDIA AND
TELECOMMUNICATIONS REVIEW

THE INWARD INVESTMENT AND
INTERNATIONAL TAXATION REVIEW

THE CORPORATE GOVERNANCE REVIEW

THE CORPORATE IMMIGRATION REVIEW

THE INTERNATIONAL INVESTIGATIONS REVIEW

THE PROJECTS AND CONSTRUCTION REVIEW

THE INTERNATIONAL CAPITAL MARKETS REVIEW

THE REAL ESTATE LAW REVIEW

THE PRIVATE EQUITY REVIEW

THE ENERGY REGULATION AND MARKETS REVIEW

THE INTELLECTUAL PROPERTY REVIEW

THE ASSET MANAGEMENT REVIEW

THE PRIVATE WEALTH AND PRIVATE CLIENT REVIEW

THE MINING LAW REVIEW

THE EXECUTIVE REMUNERATION REVIEW

THE ANTI-BRIBERY AND ANTI-CORRUPTION REVIEW

THE CARTELS AND LENIENCY REVIEW

THE TAX DISPUTES AND LITIGATION REVIEW

THE LIFE SCIENCES LAW REVIEW

www.TheLawReviews.co.uk

PUBLISHER
Gideon Roberton

BUSINESS DEVELOPMENT MANAGERS
Adam Sargent, Nick Barette

MARKETING MANAGERS
Katherine Jablonowska, Thomas Lee, James Spearing

PUBLISHING ASSISTANT
Lucy Brewer

PRODUCTION COORDINATOR
Lydia Gerges

HEAD OF EDITORIAL PRODUCTION
Adam Myers

PRODUCTION EDITOR
Jo Morley

SUBEDITOR
Charlotte Stretch

EDITOR-IN-CHIEF
Callum Campbell

MANAGING DIRECTOR
Richard Davey

Published in the United Kingdom
by Law Business Research Ltd, London
87 Lancaster Road, London, W11 1QQ, UK
© 2013 Law Business Research Ltd
www.TheLawReviews.co.uk
No photocopying: copyright licences do not apply.
The information provided in this publication is general and may not apply in a specific situation. Legal advice should always be sought before taking any legal action based on the information provided. The publishers accept no responsibility for any acts or omissions contained herein. Although the information provided is accurate as of April 2013, be advised that this is a developing area.
Enquiries concerning reproduction should be sent to Law Business Research, at the address above. Enquiries concerning editorial content should be directed to the Publisher – gideon.roberton@lbresearch.com

ISBN 978-1-907606-62-5

Printed in Great Britain by
Encompass Print Solutions, Derbyshire
Tel: 0844 2480 112

ACKNOWLEDGEMENTS

The publisher acknowledges and thanks the following law firms for their learned assistance throughout the preparation of this book:

A&L GOODBODY

ADVOKATFIRMAET STEENSTRUP STORDRANGE DA

ALUKO & OYEBODE

ASTERS

BÄR & KARRER AG

BREDIN PRAT

CAMPOS FERREIRA, SÁ CARNEIRO & ASSOCIADOS

THE DELAWARE COUNSEL GROUP LLP

DENTONS

GILBERT + TOBIN

HENGELER MUELLER PARTNERSCHAFT VON RECHTSANWÄLTEN

HERGÜNER BILGEN ÖZEKE ATTORNEY PARTNERSHIP

MANNHEIMER SWARTLING ADVOKATBYRÅ

NAGY ÉS TRÓCSÁNYI ÜGYVÉDI IRODA

NAUTADUTILH

NISHIMURA & ASAHI

NOMURA & PARTNERS

OSLER, HOSKIN & HARCOURT LLP

PLESNER LAW FIRM

QUISUMBING TORRES

SLAUGHTER AND MAY

STEPHENSON HARWOOD

STUDIO LEGALE PAVESI GITTI VERZONI

TSIBANOULIS & PARTNERS

ȚUCA ZBÂRCEA & ASOCIAȚII

URÍA MENÉNDEZ

WACHTELL, LIPTON, ROSEN & KATZ

WERKSMANS INC

WONGPARTNERSHIP LLP

CONTENTS

EDITOR'S PREFACE

I am proud to present to you the new edition of *The Corporate Governance Review*.

In this third edition, we can see that corporate governance is becoming a more prominent topic with each year. We see that everyone wants to be involved in 'better corporate governance': parliaments, governments, the European Commission, the SEC, the OECD, the UN (as demonstrated in its 'protect, respect and remedy' framework), the media, supervising national banks, shareholder activists and other stakeholders. The business world is getting more complex and overregulated, and there are more black swans, while good strategies can become quite quickly outdated. Most directors are working diligently; nevertheless, there have been failures in some sectors and this means that trust has to be regained. How can directors carry out their increasingly complex work and communicate with all the parties mentioned above?

What should executive directors know? What should outside directors know? What systems should they set up for better enterprise risk management? How can chairs create a balance against imperious CEOs? Can lead or senior directors create sufficient balance? Should outside directors understand the business? How much time should they spend on the function? How independent must they be? Should their pay be lower? What about diversity?

Governments, the European Commission and the SEC are all pressing for more formal inflexible legislative Acts, especially in the area of remuneration. Acts set minimum standards, while codes of best practices set aspirational standards.

More international investors, voting advisory associations and shareholder activists want to be involved in dialogue with boards about strategy, succession and income. Indeed, wise boards have 'selected engagements' with stewardship shareholders in order to create trust. What more can they do to show stakeholders that they are improving the enterprises other than by setting a better 'tone from the top'. Should they put big signs on the buildings emphasising: integrity, stewardship and respect?

Interest in corporate governance has been increasing since 1992, when shareholder activists forced out the CEO at General Motors and the first corporate governance code – the Cadbury Code – was written. The OECD produced a model code and many countries produced national codes along the model of the Cadbury 'comply-or-explain' method. This has generally led to more transparency, accountability, fairness and responsibility. However, there have been instances where CEOs have gradually amassed too much power, or companies have not developed new strategies and have fallen into bad results – and sometimes even failure. More are failing in the financial crisis than in other times, hence the increased outside interest in legislation, further supervision and new corporate governance codes for boards, and stewardship codes for shareholders and shareholder activists.

This all implies that executive and non-executive directors should work harder and increasingly as a team on strategy and innovation. It is still a fact that more money is lost due to lax directorship than to mistakes. On the other hand, corporate risk management is an essential part of directors' responsibilities, and sets the tone from the top.

Each country has its own measures; however, the various chapters of this book show a convergence. The concept underlying this book is to achieve a one-volume text containing a series of reasonably short, but sufficiently detailed, jurisdictional overviews that will permit convenient comparisons, where a quick 'first look' at key issues is helpful to general counsel and their clients.

My aim as editor has been to achieve a high quality of content so that *The Corporate Governance Review* will be seen, in time, as an essential reference work in our field.

To meet the all-important content quality objective, it was a condition *sine qua non* to attract as contributors colleagues who are among the recognised leaders in the field of corporate governance law from each jurisdiction.

I thank all the contributors who helped with this project, and I hope that this book will give the reader food for thought; you always learn about your own law by reading about the laws of others.

Further editions of this work will obviously benefit from the thoughts and suggestions of our readers. We will be extremely grateful to receive comments and proposals on how we might improve the next edition.

Willem J L Calkoen
NautaDutilh
Rotterdam
April 2013

Chapter 9

HUNGARY

Ildikó Varga and Viktória Szilágyi[1]

I OVERVIEW OF GOVERNANCE REGIME[2]

The Budapest Stock Exchange ('the BSE') opened its doors on 21 June 1990 with 41 founding members and one listed company, IBUSZ. Today, the shares of 73 issuers are listed on the BSE.[3] (The Exchange traces its roots back to 1864, and Hungary had a vibrant stock and commodities exchange until the middle of the last century.) The main sources of corporate law are Act IV of 2006 on Business Associations ('the Companies Act') and Act V of 2006 on Publicity of Companies, Company Registration Procedures and Winding up of Companies ('the Company Registration Act').[4] Capital markets are regulated primarily by Act CXX of 2001 on Capital Markets ('the Capital Market Act'), which provides the rules for the operation of the BSE, issuing and listing procedures, internal trading and operation of other market participants, such as investment funds and hedge funds. Act CXXXVIII of 2007 separately regulates investment service providers and commodity exchanges and their allowed activities. Besides these main sources of law, several other decrees regulate specific legal aspects related to the stock exchange and listed companies.

The BSE has issued several regulations, including:

a Regulations of Operational Risk Management;
b Regulations of the BSE for Listing, Continued Trading and Disclosure;
c Code of Trading (Trading Regulation of the BSE);

1 Ildikó Varga is a partner and Viktória Szilágyi is an associate at Nagy és Trócsányi Ügyvédi Iroda.

2 In the preparation of this chapter, the authors have used Kisfaludi András, *Társasági jog* (CompLex Wolters Kluwer, 2007) as a source.

3 Source: BSE website, www.bse.hu.

4 Note that this chapter focuses primarily on public companies limited by shares.

d Regulations on the Operation and Use of Remote Trading;
e By-laws of the BSE on Exchange Regulation Procedures and on the Rules of Official Publication; and
f Regulation on Section Membership.

The regulations and other publications, including BSE Corporate Governance Recommendations, are available and may be freely downloaded from the BSE's website.[5]

The regulatory regime is enforced through several bodies, depending on the type of regulation. The corporate regime is primarily enforced by the companies courts registering public companies limited by shares. The competent companies courts are attached to the 19 county courts of Hungary and to the Metropolitan Court of Budapest. Territorial competence depends on the registered address of the public company limited by shares. The BSE may also to some extent enforce the governance regime of listed companies through the 'comply or explain' rules in the Corporate Governance Recommendations. The ultimate supervisory body of the BSE and enforcement regime of listed companies from capital market aspects is the Hungarian Financial Supervisory Authority.[6]

II CORPORATE LEADERSHIP

i Board structure and practices

One-tier or two-tier structure, composition of the board

Under Hungarian corporate law, public companies limited by shares may operate either under a one-tier or a two-tier system. Under a two-tier system, the board of directors is the management body of the company and a separate supervisory board shall be appointed. Under a one-tier system, the company is governed by a unified board performing both management and supervisory functions. The one-tier system was implemented in 2006 when the Companies Act came into force, and only a few public companies limited by shares operate under a one-tier structure in Hungary.

Generally, under a one-tier system, the board shall have a minimum of five and a maximum of 11 members. The maximum number may be increased by the deed of foundation to ensure employee participation. Under a two-tier system, the board of directors shall have a minimum of three and a maximum of 11 members; the supervisory board shall have a minimum of three and a maximum of 15 members.

Under a one-tier system, the majority of the board shall be independent members, although the deed of foundation may require a higher percentage of independent members. The Companies Act provides that a person may qualify as independent only if that person has no other legal relationship with the company other than membership of the board. In addition, the law provides a non-exhaustive list of circumstances when a person does not qualify as independent. When electing board members, the shareholders' meeting shall ensure that these conditions are met.

5 www.bse.hu/topmenu/marketsandproducts/rulesandregulations/bserules.
6 www.pszaf.hu/en.

Company representation

Under Hungarian law, management and representation of the company must be distinct. Management means decision-making in issues falling within the competence of the management of the company, and as such belongs to the internal matters of the company. Representation, however, means the communication of the decided issues towards third parties, (i.e., in external relations of the company). In the case of public companies limited by shares, this duality is also reflected in the organisation rules: the board exercises its rights and tasks as a body in connection with all management issues of the company, whereas all board members may represent the company personally.

The statutory representation right of the board members may be restricted by the deed of foundation of the company, but such restriction is not effective against third persons, where everybody qualifies as a third person, save the company and the board member. Such restriction is basically the allocation and division of competences among the bodies of the company, meaning in practice that consent of the supreme body is required for an issue falling into management competence.

The board members represent the company in writing by way of their signatory right, which may be individual or joint. One member may sign on behalf of the company in all issues either individually or jointly. It is not possible to authorise the same member to sign individually in some issues and jointly in other issues. It is possible, however, that one member (for example, the chair of the board) signs individually and two other members sign jointly.

The Companies Act provides the possibility for board members to authorise employees of the company to represent the company. This right is especially important in large organisations, where it is impossible for the board members to take care of all daily management issues. The representation right of employees derives from the board members and not from the law, and cannot be a general representation right, but shall be limited to a specific group of issues.

The CEO of the company is generally an authorised employee who stands at the top of the organisation of the company. Under Hungarian law, this type of CEO shall be distinguished from a CEO that may be appointed instead of a board at private companies limited by shares. The CEO appointed instead of the board, who need not be an employee and is appointed by the supreme body of the company, replaces the board in all respects. This type of CEO may not be appointed at public companies limited by shares, whereas a CEO as a chief executive employee may be authorised by the board at public companies limited by shares as well.

Responsibilities of the board

In general, Hungarian corporate law sets forth a list of issues that fall within the exclusive competence of the supreme body of the company, which statutory list may be supplemented by the company's deed of foundation. All issues not falling within the exclusive competence of the supreme body by virtue of law or by provision of the deed of foundation shall be within the competence of the management.

Some of the issues for which management are responsible are provided by the Companies Act. These include:

a notification of the companies court regarding establishment of the company;

b changes of corporate data;

c exercising employer's rights; and
d the obligation to provide information to specific persons regarding specific issues and data of the company.

In addition, some issues relevant to both private and public companies limited by shares are also provided by the Companies Act. Such issues are:
a management's reporting obligation to the shareholders' meeting at least once a year, and to the supervisory board every three months, or more frequently if so provided by the deed of foundation;
b keeping the books and records of the company;
c presenting the annual financial report to the shareholders' meeting;
d convening the shareholders' meeting;
e proposing dividend payments;
f providing sufficient information to the shareholders;
g recording the shareholders' registry; and
h indicating on share certificates the acquisition of the share by way of inheritance, legal succession, court resolution or auction.

The Companies Act further provides issues for which boards of public companies limited by shares are specifically responsible if the company's shares are listed on the BSE: the board shall annually prepare a responsible governance report, which shall be approved by the shareholders' meeting and shall be published on the website of the company; and the board shall comply with the regular and extraordinary information obligation provided by Capital Market Act.

The board shall of course be responsible for all issues not expressly listed in the Companies Act, but provided by other sources of law or falling in general to the competence of the management of the company.

Operation of the board

As already mentioned, the board exercises its rights and tasks as a body in connection with all management issues of the company. Boards generally act and make decisions as a body. Nevertheless, the Companies Act provides the possibility for the members of the board to allocate tasks and responsibilities among the members in the by-laws of the board.

Boards make decisions in meetings, at which the board members must be present personally as the Companies Act excludes the possibility of representation. The by-laws of the board may provide, however, that the board meetings may be held by electronic communication equipment, in which case the by-laws shall define in detail the rules of such meetings.

The operation of the board is regulated in detail by its by-laws, which must be approved by the board itself. In the by-laws the board shall elect a chair among themselves who shall be responsible for governing the operation of the board. The chair may also be appointed from among the board members by the shareholders' meeting, if the deed of foundation reserves this right to the shareholders' meeting.

Committees

Under Hungarian law, the only mandatory committee is the audit committee in the case of public companies limited by shares. The audit committee shall have a minimum of three members, elected by the shareholders' meeting from among the independent members of the board and, if applicable, the supervisory board. The law also requires that at least one of the members of the audit committee shall have accounting or auditor skills, or both.

The law provides a minimum list of responsibilities for the audit committee, which may be supplemented by the deed of foundation. According to the law, the audit committee shall:

a opine on statutory financial reports;
b monitor the audit of the statutory financial report;
c make proposals regarding the auditor and its remuneration;
d prepare the agreement to be concluded with the auditor and sign the agreement on behalf of the company if the deed of foundation so provides;
e monitor the auditor activity (coordination of the cooperation with the auditor);
f evaluate the operation of the financial reporting system and suggest necessary steps in this respect;
g help the activity of the board and supervisory board to monitor the financial reporting system; and
h monitor the effectiveness of the internal control and risk management system.

The company may set up other committees it may deem appropriate to help the operation of the company.

ii Directors

Appointment procedure of directors

The first directors (members of the board) are appointed in the deed of foundation when the company is established. Following the establishment, directors are appointed by the shareholders' meeting, with a simple majority, unless the deed of foundation requires a higher percentage. Directors may be appointed for an indefinite term, or, alternatively, for a maximum five-year definite term. Once appointed, the directors shall sign a declaration in which they accept their position. The change of directors shall be registered with the companies court; all directors must be listed in the companies court's registry to give corporate effect to the appointment. The directors may be withdrawn or may resign at any time without giving a specific reason. In cases of public companies limited by shares, the deed of foundation may limit the number of directors that may be replaced at the same time.

Independence of directors

If a public company limited by shares operates under a one-tier system, the majority of the directors appointed to the board must be independent, unless the deed of foundation requires a higher percentage. A director shall qualify as independent in cases where a particular director does not have any other legal relationship with the company than the board membership. The law also provides a non-exhaustive list of circumstances when a director shall not qualify as independent, such as if the director:

- *a* is an employee of the company or was an employee less than five years ago;
- *b* is an expert or other contractor of and for the benefit of the company or director of the company acting for consideration;
- *c* is a shareholder who holds directly or indirectly at least 30 per cent of the votes, or is a close relative of such a person;
- *d* is a close relative of any non-independent director or the CEO of the company;
- *e* is entitled to remuneration based on his or her directorship in cases of profitable operation of the company or is entitled to any other remuneration from the company or related entity other than the one received for the board membership;
- *f* has a legal relationship in another company with a non-independent shareholder based on which the non-independent shareholder has controlling rights;
- *g* is an independent auditor of the company or employee or partner of the auditor or has been within the past three years; or
- *h* is a board member or CEO in another company where the independent board member is also a member of the board of directors of the company.

Exclusion rules, conflict of interest of directors

The exclusion rules are the same for all types of companies. A person who was sentenced to jail may not be appointed as a director until all offences are spent. A person who was prohibited by final court order from performing director activities may not be appointed as a director while such prohibition is effective, nor may a person prohibited by final court order to perform another profession while the prohibition is effective be director of a company having such profession as its main activity. If a company was dissolved as a result of a termination procedure, any person serving as a director during the calendar year prior to the date of termination may not be appointed as a director for five years as of that date. Finally, a person who was a director or majority shareholder of a company, whose contract was terminated without legal succession and whose liability was established by the court for the claims unpaid in the procedure that resulted in termination without legal succession, and who has not fulfilled his or her payment obligation thereunder, may not be appointed as director for five years as of the date when the enforcement procedure against the former director or majority shareholder was declared unsuccessful. Further incompatibility rules of the Companies Act are that a person who had a fine imposed on him or her by the court of registry in a judicial oversight proceeding and failed to pay this fine may not be appointed as a director. In addition, a person who did not fulfil his or her liabilities after withdrawal from a partnership in accordance with Companies Act may not be appointed as a director. In both cases the prohibition shall apply for a period five years from the time of failure of the enforcement procedure conducted against that person.

Directors may not acquire an interest (except in public companies limited by shares) and may not be director in another business association having the same main activity as the company where the director is a member of the board, unless the deed of foundation provides otherwise or the supreme body of the company consents to such appointment. The director and close relative of the director may not conclude, in the director's own name and behalf, deals falling within the main activity of the company. The director and the director's close relatives may not be appointed as supervisory board members at the same company. The auditor appointed to or otherwise performing auditor services for the company may not be appointed as a director of the company.

Liability of directors

A distinction must be made between internal and external liability of directors.

Internal liability concerns liability towards the company. Directors shall be liable in accordance with the general rules of the Civil Code towards the company for the damages caused by their imputable breach of the law, the deed of foundation, the resolutions of the supreme body and their management obligations. The directors have civil liability even if they are employed by the company. To establish civil liability, four conjunctive conditions shall be met: actual damage occurred, the action of the director was unlawful, the damage was factually and legally caused by the unlawful action, and the unlawful action was imputable to the directors. Damages may be claimed by the company or by a 5 per cent minority of the shareholders on behalf of the company if the company does not enforce the claim.

The Companies Act provides some exceptions where different liability rules apply. The notification of the companies court regarding establishment of the company or changes in the corporate data is the directors' responsibility, and the directors shall have unlimited, joint and several liability for all damages caused by failure of the directors to notify the court.

The general rule of external liability is that any damage caused by the directors – acting in their capacity as directors – to third persons may be claimed only from the company and not from the directors (i.e., the company shall be held liable for all damages caused by its directors).

A special rule of the Companies Act concerns the liability of the directors in insolvency situations. The general rule is that the directors are obliged primarily to consider the interest of the company when performing their duties. If, however, the company is in a position where insolvency is threatened, the directors must primarily consider the interest of the creditors. If the directors imputably breach this obligation and the company indeed becomes insolvent, the directors may be held liable in accordance with specific insolvency laws. The directors may also be held liable based on a special regulation if the company is terminated without legal succession irrespective of its solvency being investigated.

III DISCLOSURE

All companies are subject to several financial reporting rules, including state and local tax returns, and statistic data collection. All companies must prepare financial reports annually for the end date of their business year, which is 31 December unless otherwise provided by the deed of foundation of the company. Public companies limited by shares are also subject to the following specific financial reporting rules, provided that the shares of the company are traded on the BSE.

The board of the company must prepare and submit to the shareholders' meeting, together with the annual financial report, the company's responsible corporate governance report, which summarises the responsible governance practice of the past business year and declares why and how the governance regime of the company deviates from the Corporate Governance Recommendations of BSE. The report shall be published on the company's website and must be approved by the shareholders' meeting.

Simultaneously with the convening of the annual shareholders' meeting, information shall be published on the company's website each year concerning the directors, and supervisory board members if applicable, listing their names and their remuneration in cash or in kind paid to them in their capacity of directors and supervisory board members, showing each title of payment separately. The company shall provide continuous access to these data on its website without any interruption.

According to the Capital Market Act, the issuer of publicly traded shares must regularly inform the public regarding the main data of its finances, income and operation in the form of annual reports, semi-annual reports and interim board reports. Such reports shall be published and the Hungarian Financial Supervisory Authority shall be informed about their publication. The reports shall be accessible for at least five years. According to the Capital Market Act the issuer must also, in the framework of its extraordinary information requirements, inform the public within one business day regarding all information affecting either directly or indirectly the value or yield of the shares or the company's strategy.

The Corporate Governance Recommendations of the BSE operates the 'comply or explain' model. The Recommendations are not mandatory but rather guidelines it is advisable to comply with. The Recommendations consider the Commission Recommendation of 30 April 2009 as regards the regime for the remuneration of directors of listed companies (2004/913/EC) and the Commission Recommendation of 15 February 2005 on the role of non-executive and supervisory directors of listed companies and on the committees of the (supervisory) board (2005/162/EC). According to the Recommendations, listed companies must declare their governance practices in two ways. In the fourth part of their report an accurate overview of their practice shall be provided, including their governance policy and possible special circumstances. In the second part of their report compliance with the specific points of the Recommendations shall be reported in accordance with the 'comply or explain' model.

IV SHAREHOLDERS

i Shareholder rights and powers

Equality of voting rights

According to the Companies Act, the voting rights represented by the shares depend on the nominal value of the shares, unless the law or the deed of foundation restricts or excludes the voting right with respect to the specific group of shares.

General voting restrictions mean that shareholders may not vote if:

a they would be released from obligation or liability;

b they would be otherwise favoured by the resolution;

c they would be party to the agreement to be concluded on the basis of the resolution or would have to be sued on the basis of the resolution; or

d their legal relationship with the company, its establishment, content and termination would be affected by the resolution.

A public or private company limited by shares may not vote with its own shares, nor may a shareholder vote with a share that is not fully paid up.

The law restricts voting rights with respect to certain priority shares when stating that the deed of foundation may restrict or exclude voting rights with respect to these types of shares, otherwise the voting rights shall depend on the nominal value.

Both public and private companies limited by shares may issue priority shares providing voting priority. The voting priority means either priority in time or priority in amount (i.e., more votes).

Powers of shareholders to influence the board

The activity of the board may be influenced by the shareholders by decreasing the board competences and reserving these to the shareholders' meeting. Two issues shall be considered in this respect. First, the more issues that are defined as being relevant for decisions at the shareholders' meeting, the more actively the shareholders' meeting shall participate in the day-to-day operation of the company. Second, the board competences cannot be fully removed and the board may not be defined as a simple executive body acting on the basis of the shareholders' decisions.

The Companies Act provides that the board members may not be instructed by the shareholders' meeting; therefore it is not possible to influence the operation and decisions of the board directly.

However, several indirect mechanisms may be included in the company's deed of foundation and by-laws to ensure that the operation and decisions of the board are under control, including proposal and appointment mechanisms of board members, electing the chair of the board by the shareholders' meeting and giving authorisation to the chair of the board of directors to act as CEO and to take care of the day-to-day operation and business of the company.

Decisions reserved to shareholders

As mentioned above, the Companies Act provides a list of issues in which the decisions are exclusively reserved to the shareholders. The below list may be supplemented with further issues, but these powers cannot be extended to leave the board devoid of powers. In the case of public companies limited by shares, this list includes:

a decision-making regarding the establishment and amendment of the deed of foundation;

b change of form of operation of the company;

c transformation and winding-up of the company;

d appointment, remuneration and removal of members of the board of directors, members of the board of supervisors and auditor;

e approval of the financial statements prepared pursuant to the Accounting Act and the declaration of dividends;

f payment of interim dividends;

g conversion of certificated shares into dematerialised shares;

h conversion of shareholders' rights pertaining to certain share series, transformation of share series and classes, unless otherwise stated in the Companies Act;

i issuance of convertible bonds or bonds representing subscription rights;

j increase or decrease of the registered capital, unless otherwise stated in the Companies Act;
k abolishment of preferential subscription rights or authorisation to the board of directors to restrict or abolish such rights;
l directives and framework of long-term remuneration and incentivisation of the board of directors and supervisory board members as well as chief executive employees, which decision shall be mandatory or optional as provided by the deed of foundation;
m appointment of the members of the audit committee; and
n approval of the financial reports prepared in accordance with the Accounting Act.

Minority shareholders rights

According to the Companies Act, minority shareholders rights, with some exceptions, may be exercised by shareholders holding at least 5 per cent of the initial capital of the company. Minority shareholders holding such percentage may:

a request the management at any time, providing the reason and the purpose, to convene a shareholders' meeting;
b request the companies court to order inspection by an auditor of the latest annual financial report or any action in the management of the company in the past two years, provided that the shareholders' meeting ignored a sufficient proposal in the same matter and did not bring a resolution; or
c bring, on behalf of the company, any claims against any shareholder, member of the board of directors, member of the supervisory board or appointed auditor of the company, provided that the shareholders' meeting voted against such proposals or ignored a sufficient proposal in such a matter and did not bring a resolution.

In addition to the above, in the case of public companies limited by shares, shareholders holding at least 1 per cent of the initial capital may exercise the shareholders' right to supplement the agenda of the shareholders' meeting, and they may also propose draft resolutions in connection with any issues on the agenda.

ii Contact with shareholders

In the case of public companies limited by shares, the shareholders' meeting shall be called by a public invitation in accordance with the company's deed of foundation, but as a bare minimum by an announcement on the company's website at least 30 days before the meeting. Detailed information regarding the draft of the annual financial report, the report of the board of directors and supervisory board, statistics regarding the shares and voting rights, and summary of the proposals forming part of the agenda, shall be published at least 21 days before the start date of the meeting. The board of directors shall provide further information regarding any item on the agenda upon written request of any shareholder submitted to the board eight days before the meeting, at the latest. Such information may only be withheld if providing it would harm the business secrets of the company.

Shareholders who wish to participate in the shareholders' meeting or their proxies must be recorded in the share registry of the company at the latest at 6pm on the second business day preceding the day of the meeting. Only shareholders registered by this deadline may exercise shareholders' rights on the meeting.

The shareholder may be represented by proxy at the shareholders' meeting. The company auditor, a member of the board, a member of the supervisory board or the CEO may not be a proxy, unless they have written voting instructions from the shareholder regarding each proposed resolution on the agenda. Authorisation for the proxy shall be submitted to the company in the form of a public or private deed.

In addition to being registered in the share registry, a shareholder must be identified by way of the shareholder identification procedure if such shareholder holds the original share certificate, or a share deposit certificate if the share certificates are deposited, or an ownership certificate regarding dematerialised shares.

V OUTLOOK

Since 14 January 2010, the BSE has been a subsidiary of CEESEG AG holding company, which owns 68.8 per cent of the BSE and also owns 100 per cent of the Wiener Börse and majority shares of the Prague and Ljubljana stock exchanges. With this background, the BSE is expected to become an increasingly important market for Hungarian and foreign investors. Simultaneously, corporate governance should improve to meet the expectations of national and international investors and to comply with EU and international legal standards.

Appendix 1

ABOUT THE AUTHORS

ILDIKÓ VARGA

Nagy és Trócsányi Ügyvédi Iroda

Ildikó Varga is an executive partner at Nagy és Trócsányi in Budapest and head of the corporate and M&A group. Her main areas of work include corporate law, cross-border transactions, project finance, energy and media law. She advised on the creation of several leading foreign direct investments. She advises investors in the energy sector, with special emphasis on renewable energy. She regularly advises lenders and borrowers of syndicated credit facilities. Ms Varga is a member of the New York Bar and the Budapest Bar. She joined White & Case in New York in 1990 as a foreign attorney, before moving to Arent Fox in Washington, DC, in 1991. She joined Nagy és Trócsányi in 1993.

VIKTÓRIA SZILÁGYI

Nagy és Trócsányi Ügyvédi Iroda

Viktória Szilágyi graduated from the Faculty of Law of Eötvös Loránd Tudományegyetem in Budapest and has worked at Nagy és Trócsányi since she left university. She works mainly on mergers and acquisitions; as part of her cross-border transaction practice she has participated in more than 30 due diligence reviews in the past five years. Her practice also covers corporate matters, real estate issues and greenfield investments, project finance and financial restructuring. She also has experience in the legal issues of the energy (including renewable energy) and pharmaceutical sectors. Ms Szilágyi has been a member of the Budapest Bar since 2009.

NAGY ÉS TRÓCSÁNYI ÜGYVÉDI IRODA
Ugocsa utca 4/B
1126 Budapest
Hungary
Tel: +36 1 48 78 700
Fax: +36 1 48 78 701
varga.ildiko@nt.hu
www.nt.hu