

newsletter

MONTHLY LEGAL UPDATE | HUNGARY |

MARCH 2014

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CIVIL LAW

Effect of the New Civil Code on existing legal relations

On 15 March 2014, the New Civil Code entered into force (“Entry Into Force”) and its provisions shall apply to all legal relations and declarations made after this date. Nevertheless, specific rules in Act CLXXVII of 2013 on the transitory and authorizing provisions related to the entry into force of the New Civil Code include further guidance on the situation of existing companies.

Reference to the New Civil Code in the company’s founding document

When amending its founding document for the first time after the Entry Into Force, a company already incorporated in the companies registry must adopt a resolution stating that its further operation will be in compliance with the rules set out in the New Civil Code.

Such resolution must be filed with the court of registration along with the first registration of changes in the company’s data after the Entry Into Force. In the absence of amendment to the articles of association, the latest date on which a company must apply the provisions of the New Civil Code is 15 March 2015 for unlimited partnerships (*közkereseti társaság* or *kkt.*) and limited partnerships (*betéti társaság* or *bt.*), and 15 March 2016 for limited liability companies (*korlátolt felelősségű társaság* or *kft.*) and public/private limited companies (*zártkörűen/nyilvánosan működő részvénytársaság* or *zrt./nyrt.*).

Companies must ensure that, after the first amendment made to their founding document following the Entry Into Force, or after 15 March 2015 or 15 March 2016 as applicable, their founding document does not contain any provisions that are non-compliant with the New Civil Code.

Compliance with minimum capital requirements

Additionally, considering the increase in the minimum capital amount to HUF 3 million for limited liability companies, limited liability companies already incorporated or in the process of incorporation at the time of Entry Into Force and with registered capital below HUF 3 million must either increase their registered capital, or transform into another company form by 15 March 2016.

Restriction of establishment of public limited companies

After the Entry Into Force, only private limited companies may be established and public limited companies may only be constituted by changing the company's form of operation from private to public limited company. This occurs with the admission and listing of a company's shares on a stock exchange.

Public limited companies already incorporated or in the process thereof at the time of Entry Into Force and that do not have shares listed on a stock exchange, must obtain admission to a stock exchange and list their shares by 15 March 2016 or adopt a resolution to change their corporate form.

PROPERTY LAW**New act to eliminate pocket agreements**

During the term of the land acquisition moratorium - preventing EU and third country nationals from acquiring lands in Hungary - in force until 1 May 2014, agreements known as "pocket agreements" have become a flourishing instrument to avoid the statutory restrictions on acquiring or using agricultural land.

The term "pocket agreement" stands for agreements enabling foreign nationals to acquire ownership rights on a plot of agricultural land as a counterpart for a reasonable consideration, however the agreement is disguised as leasehold, usufruct, or mortgage agreement, in order to circumvent legal restrictions on land acquisition.

Besides the act on agricultural lands, which will result in many significant changes as of 1 May 2014 as already indicated in our previous newsletters, the new Act VII of 2014 entered into force on 13 March 2014 to combat this practice and improve the detection and prevention of pocket agreements.

Under the new act, pocket agreements and all other legal acts or procedures related thereto shall be considered as null and void. The new act excludes all legal remedies related to such agreements, as no claim arising from such legal act may be court-enforced. Pocket agreements concluded before the entry into force of the new act may be terminated by the parties by mid-April on a voluntary basis, and in this case the consequences of invalidity shall not apply.

Additionally, the new act states that, if the agreement can be reasonably suspected of being a pocket agreement, the public prosecutor will be in charge of launching an investigation upon notification. The public prosecutor may require information from all authorities and may initiate court proceedings to establish the invalidity of the agreement, and request the transfer of ownership of the respective agricultural lands to the Hungarian State.

Lastly, the new act considers the conclusion of pocket agreements as a crime. Thus, as of 1 May 2014, the Criminal Code provides that pocket agreement and the land use based on such agreements, are punishable by imprisonment of up to 3 years, or between 1 and 5 years as applicable. Previously concluded contracts may therefore also be subject of investigation. If, however the contracting parties voluntarily disclose that they entered into a pocket agreement prior to an investigation by the competent authority, the extent of the penalty may be reduced without limitation.

LABOUR LAW

Harmonisation of the Labour Code with the New Civil Code

The entry into force of the New Civil Code on 15 March 2014 led to the necessity of harmonising certain provisions of the Labour Code with the New Civil Code. Besides technical modifications that are due to ensure the same wording and the appropriate references, the Labour Code has been materially modified. The main modifications are detailed below.

Clarification of the 'Common Rules of Conduct' (Paragraph 6 of the Labour Code)

The Common Rules of Conduct of the Labour Code have been completed with the rule of attributability as defined in the New Civil Code. This rule provides that a party whose conduct is contrary to his previous conduct, which the other party had ground to trust in, is in breach of his obligation of acting in good faith and mutual respect.

Modifications related to the injury fee ("sérelemdíj" in Hungarian) of the New Civil Code

The Labour Code has been modified to reflect the term 'personality rights' instead of 'personal rights', as used in the New Civil Code.

The Labour Code also clarifies that, when applying the provisions of the New Civil Code relating to the injury fee, the provisions of the Labour Code on liability for damages (i.e. limited liability) shall prevail. Consequently, the employee's liability for damages remains limited also in the case of an injury fee payment.

The Labour Code now provides that persons without legal capacity and persons with limited legal capacity cannot be required to pay damages or injury fees in employment relations.

Another modification concerns the prescription period of 5 years for injury fee claims.

Modifications related to the rules on legal capacity

In accordance with the modified Labour Code, the consent of the legal representative is required for the validity of the legal acts (i.e. conclusion, modification, termination of an employment contract or the undertaking of a commitment) of young employees and persons with limited legal capacity in employment relations.

Formal requirements of legal acts

The formal requirements of certain acts have been softened: a limited list of acts (e.g. making a work schedule public, ordering overtime, etc.) can be considered as having been made in writing if they are published by means considered as commonly known and as the usual method of communication.

Completion of the rules on the nullity of agreements

The Labour Code now includes that agreements that clearly go against good morals shall be considered null and void.

Modifications related to the restoration of an employment relationship at the employee's request

The conditions pertaining to the restoration of an employment relationship by the courts at the employee's request have been clarified and remove the uncertainty related to the judicial practice: the period between the termination and the restoration of employment must be considered as a period of employment as regards the rights due following the termination of employment.

Consequently, in the event of employment restoration, employees must be compensated for lost salary, lost allowances and other damages. Employees' absence fees must to be considered as lost salary.

Modifications related to responsibility for damages

In order to further develop the judicial practice, the Labour Code has been supplemented by a new section which makes it clear that when calculating loss of income, social security contributions must be deducted.

Compliance with European law as regards maternity leave

In order to ensure even further compliance with Council Directive 92/85/EEC, the Labour Code has been supplemented with the obligation for mothers to take at least two weeks of the twenty-four weeks of consecutive maternity leave.

It has also been clarified that executive employees shall be exempt from the requirement of availability and from work duty for the period of medical treatment related to an IVF procedure and for a period defined by the Labour Code during the first six months of breastfeeding. It has also been further clarified that rules on maternity leave are also applicable to executive employees: the employer may neither terminate the employment relationship by notice during such employees' pregnancy and maternity leave, nor order the employee to carry out night shifts from the time the employee's pregnancy is diagnosed until the child reaches the age of three years.

Non-compete and study agreements

References to the provisions of the New Civil Code related to penalty payments have been included in the Labour Code.

TAX LAW**Tax audit focuses in 2014**

The Hungarian Tax Authority has published the focus areas for the 2014 tax audits, establishing the criteria for the tax audit selection process, the main focus as to economic activities and industries, and the objectives of the audits.

As regards VAT, the main areas of investigation will be compliance with invoicing obligations and the existence of transactions on the basis of issued invoices. Tax audits will continue to focus on the most typical forms of fraud, such as chain transactions.

As regards corporate income tax, the Tax Authority will pay particular attention to the following elements: unjustified expenses, determination of the arm's-length price used - specifically in the case of non-conventional calculation methods -, classification of R&D activities and use of tax incentives. Transactions between Hungarian companies and their related foreign parties will also be strictly examined.

In addition to the above, the Tax Authority has determined the following economic activities to be audited with particular attention:

- meat processing and preservation, as well as the grain industry in the agricultural sector,
- production of metal structures, building residential and non-residential buildings in the industrial sector,
- car repair services and car maintenance services as well as the retail of car components as trading activities;
- wholesale of sugar, sweets, fruit and vegetables,
- wholesale of livestock, meat and meat products,
- advertising agency activities,
- labour rental,
- personal defence activities.

According to the published brochure, the Tax Authority seems to wish to strengthen audit activities.

Tax implication of trusts

As indicated in our January newsletter, the detailed regulations pertaining to trusts have been adopted by the Hungarian Parliament.

Act XV of 2014 on trusts and the regulation of trust activities (the "**Act**") entered into force on 15 March 2014. The Act comprehensively regulates the issues of trusts including taxation-related questions in respect of asset assignment, asset management and asset disbursement.

As of the effective date of the Act, the related tax legislation has been amended to ensure that the establishment of a trust does not entail tax consequences that would hinder the practical use of the newly introduced legal institution.

As a general rule, the acquisition of assets by a trustee is not subject to transfer tax, while the acquisition by the individual beneficiary is exempt from personal income tax. The yield of the assets is however taxed as dividend on the private individual, and the managed assets are subject to both corporate income tax and local business tax.

Simplification of the residence permit

The simplification of the foreign residence permit was adopted on 1 January 2014, in line with taxpayer demands. Accordingly, in line with the new regulations, if no English-language certificate is issued by the country of residence, the Hungarian Tax Authority will accept the professional Hungarian translation of the original certificate, regardless of its language of issue.

However, tax residence will still need to be certified for every tax year, even if it remains unchanged from the previous certificate that has been filed to the tax authority.

CONTACTS

FRANÇOIS D'ORNANO
ornano@gide.com

ESZTER KAMOC SAY-BERTA
kamocsay-berta@gide.com

ÁKOS KOVÁCH
kovach@gide.com

You can also find this legal update on our website in the News & Insights section: gide.com

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