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Acknowledgement


INSOL International is very pleased to present a technical paper titled Directors in the Twilight Zone - Hungary by Zoltan Fabok and Gábor Kökényesi, DLA Piper Posztl, Nemescsói, Györfi-Tóth & Partners Law Firm, Hungary.

In Hungary, prior to 2006, there was virtually no legal protection afforded to creditors in relation to the actions or inaction of the directors of insolvent companies. In 2006, by transplanting the English legislative provisions in relation to wrongful trading, the Hungarian legislator introduced the long-awaited and much-needed wrongful trading rules into the Hungarian legal system. This paper provides members with a detailed overview of Hungarian insolvency law in relation to wrongful trading and other actions potentially giving rise to liability for directors, managers, advisors and other third parties who trade companies in the 'twilight zone' of insolvency. During this period transactions entered into by a company are also vulnerable to attack and the paper examines on what basis such transactions may be set aside and the relevant 'look back' periods.

The authors have provided detailed answers to the template of questions set for the 5th edition of the Directors in the Twilight Zone V publication which was published in May 2017 in ebook format. This paper has been included as an additional country chapter to the publication and [Directors in the Twilight Zone V](#) now covers 31 different jurisdictions and provides an excellent resource to our members.

INSOL International sincerely thanks Zoltan Fabok and Gábor Kökényesi for this detailed analysis and for writing this excellent technical paper and additional country chapter for the Directors in the Twilight Zone publication.

July 2019



Directors in the Twilight Zone V – Hungary

By Zoltan Fabok and Gábor Kökényesi, DLA Piper Posztl, Nemescsói, Györfi-Tóth & Partners Law Firm, Hungary* **

1. The directors and the start and duration of the twilight period

(a) How are directors identified / defined?

(b) What is the length of the period ending with formal insolvency proceedings during which transactions entered into by a company are vulnerable to attack or are liable to give rise to personal liability on the part of directors and / or others involved in the management of the company (the twilight period)?

1.1 Preliminary remarks

1.1.1 Prior to 2006, virtually no civil law protection was available in Hungary for creditors with regard to the action or inaction of the directors of an insolvent company.¹ Provided that the company was not formally insolvent (no insolvency proceedings had been opened) in most cases directors were free to operate the debtor company without any relevant restrictions.²

1.1.2 In 2006, the Hungarian legislator imported the English concept of liability for “wrongful trading”. This legal transplant,³ while having common roots with the English wrongful trading rules, has some distinctive features, reflecting the characteristics of the Hungarian legal system. For example, there is a two-stage litigation process in place in Hungary: the first stage of the litigation aims to establish the director’s liability and, if such liability is established, the second stage of the litigation determines the amount of compensation that the director is liable to pay to the creditors on a *pro rata* basis (for further details, see section 5.1 below). Another peculiarity of the Hungarian legislation is that the liability for wrongful trading is not reserved to the directors of the debtor company. The Hungarian legislation places the majority shareholder of the debtor in the position of guarantor of the director regarding any liability for wrongful trading (see section 3.1.4).

1.2 Identification and definition of directors

1.2.1 Directors – wrongful trading

1.2.1.1 In Hungary, the concept of director refers first to *de jure* directors, those who occupy the position of director, howsoever described in the specific statute.⁴ For certain legal entities (for example, foundations, business organisations) *de jure* directors are required to be registered with the companies’ registry. For other legal entities, such registration is not obligatory (for example, law firms, patent law firms).⁵

1.2.1.2 Beyond that, the statute provides that any legal or natural person who has in fact exercised dominant

* The views expressed in this paper are the views of the author and not of INSOL International, London.

** This paper is up to date as of 11 April 2019. It has been prepared for information purposes only. As such, the information presented is confined to answering the questions set and the paper does not go into the further detail of Hungarian law. The paper is not intended to be a substitute for professional advice.

Parts of this paper were sourced from a chapter by Zoltan Fabok (the co-author of this paper) titled “‘Wrongful Trading’ in England and Hungary: A Comparative Study” which first appeared in the publication ‘Harmonisation of European Insolvency Law’ (INSOL Europe 2017) Dr Jennifer L. L. Gant (ed).

¹ See: 2006. évi VI. törvény indokolása a csődeljárásról, a felszámolási eljárásról és a végelszámolásról szóló 1991. Évi XLIX. törvény módosításáról [Explanatory note on the Act VI of 2006 amending of the Hungarian Insolvency Act].

² Zoltan Fabok: “Wrongful Trading” in England and Hungary: A Comparative Study, p. 90.

³ “Legal transfer” or “legal transplant” means unilateral adoption of legal norms from other jurisdictions. See N. Garoupa and A. Ogus, “A Strategic Interpretation of Legal Transplants”, (2006) 35 Journal of Legal Studies, p. 341.

⁴ § 3(1)(d), Act XLIX of 1991 on Reorganisation Proceedings and Liquidation Proceedings (“HIA”).

Zoltan Fabok: “Wrongful Trading” in England and Hungary: A Comparative Study, p. 89.

⁵ cf. A Kúria Polgári Kollégiuma Joggyakorlat-elemző Csoport [Civil Department of the Curia, Expert Group Analysing the Case Law], “A vezető tisztségviselők hitelezőkkel szembeni felelőssége» tárgykörben felállított joggyakorlat-elemző csoport összefoglaló véleménye (A Kúria Polgári Kollégiuma által 2017. február 6-án elfogadott összefoglaló vélemény) [“Summary Opinion of the Expert Group on the Subject of the Liability of the Executives vis-à-vis the Creditors” (Summary Opinion approved by the Civil Department of the Curia on 6 February 2017) [2016.El.II.JGY.G.2.] (the “Summary Opinion”), available at http://lb.hu/sites/default/files/joggyak/osszefoglalo_velemenyn_6.pdf (last viewed 24 March 2019), p. 12.

influence on the decision-making mechanisms of the debtor company shall also be considered a director for the purposes of liability for wrongful trading. This category is generally described as “shadow directors” in judgments and the literature but the definition appears to cover both shadow and *de facto* directors.⁶ In the jurisprudence, the *de facto* director is a person who assumes to act as a director.

- 1.2.1.3 Depending on the circumstances, a shadow director might be, for instance, the company’s majority (or even minority) shareholder or, in theory, also a financial institution or a legal / financial advisor of the company.⁷

1.2.2 *Persons liable for criminal offences during the twilight period*

- 1.2.2.1 According to the Hungarian Criminal Code,⁸ criminal offences during the twilight period may be committed by anyone who is entitled to control the assets (in whole or in part) of the debtor company, or has the opportunity to do so, notwithstanding that the contract for the given transaction may subsequently be found to be invalid.⁹
- 1.2.2.2 Those persons who have control over the company’s assets, are determined in the company’s instrument of incorporation.¹⁰ It is to be noted that once liquidation proceedings have been formally opened, only the liquidator may dispose of the company’s assets.

1.3 *Twilight period*

1.3.1 *Twilight period - wrongful trading*

- 1.3.1.1 The period during which the director might incur personal liability for wrongful trading (the twilight period) is not pre-determined and differs from case to case. It begins with the occurrence of the debtor company’s imminent insolvency. Pursuant to the legal definition, imminent insolvency occurs when the directors were or should have been reasonably able to foresee that the company would not be able to satisfy its liabilities when due (cash-flow test). In other words, when the director knows or should foresee that the company is cash-flow insolvent he or she is exposed to liability for wrongful trading if further elements of the liability are present. When applying the rather rigid cash-flow test, it appears that the hope of realising some uncertain income in the future is insufficient to be shielded from imminent insolvency.¹¹
- 1.3.1.2 In several cases, the Hungarian courts have applied the ‘current ratio test’ or the ‘quick ratio test’ to determine the cash-flow situation of the company. The current ratio is a basic indicator calculated by dividing total current assets by total current liabilities; the quick ratio, by contrast, takes into account the most liquid current assets: it is calculated by adding cash and equivalents, marketable investments, and accounts receivables, and dividing that sum by current liabilities.¹²

1.3.2 *Twilight period – criminal offences*

- 1.3.2.1 Certain of the so-called “bankruptcy offences”, which include several different criminal offences specified under section 2.3.1.1 below, may be committed during the twilight period. The twilight period for determining these offences commences at the same time as it would under the wrongful trading rules.

1.4 *The ‘look back’ periods for avoidance actions*

- 1.4.1 Aside from the twilight period relating to the liability of directors and other persons in the case of wrongful trading and bankruptcy offences, there are other periods relating to the transactions entered

⁶ Zoltan Fabok: “Wrongful Trading” in *England and Hungary: A Comparative Study*, p. 90.

⁷ Summary Opinion, pp.13-14.

⁸ Act C of 2012 on the Criminal Code, § 404.

⁹ I. Hegedűs, Zs. Juhász, K. Karsai, T. Katona, E. Mezölaki, Zs. Szomora, S. Törő, “*Kommentár a Büntető Törvénykönyvről szóló 2012. évi C. törvényhez [Commentary to Act C of 2012 on the Criminal Code]*,” (Online Complex Wolters Kluwer Commentary), at § 404.

¹⁰ Summary Opinion, p. 12.

¹¹ Zoltan Fabok: “Wrongful Trading” in *England and Hungary: A Comparative Study*, pp. 94-95.

¹² Zoltan Fabok: “Wrongful Trading” in *England and Hungary: A Comparative Study*, p. 95.

into by a company prior to insolvency proceedings, that have paramount importance for the insolvent company's creditors.

1.4.2 Within 120 days from the time of gaining knowledge or within a one-year limitation period from the date of publication of the notice of the company's liquidation, the creditors or the liquidator may bring an action to retrospectively challenge the company's transactions concluded prior to the opening of the liquidation proceedings.¹³ These voidable transactions are defined in section 4.1.2 below. The look back periods within which such transactions may be challenged differ according to their nature as follows:

- (i) For fraudulent transactions the look back period (the period calculated retrospectively from the date of filing for liquidation) is 5 years;
- (ii) For transactions at an undervalue, the look back period is 3 years;
- (iii) For preferential transactions, the look back period is 90 days;
- (iv) For misuse of guaranties transactions, the look back period is 3 years (only regarding contracts entered into on or after 1 July 2017); and
- (v) For preferential service, the look back period is 60 days.

2. Actions potentially giving rise to liability for directors

(a) In respect of which acts during the twilight period may a director be held personally liable or which may otherwise have adverse consequences for the director?

(b) In relation to each act identified in (a) above:

- (i) is the director's liability considered to be civil, criminal or both?**
- (ii) can a director be made personally liable for all or part of the company's losses or for all or part of the deficit to creditors?**
- (iii) will liability attach to all the directors or to individual directors in proportion to their specific involvement?**
- (iv) is there a specified period before commencement of a subsequent insolvency procedure within which the relevant act must have been undertaken in order for liability to attach to a director? and**
- (v) what defences, if any, will be available in relation to each offence?**

2.1. Wrongful trading

2.1.1. Actions giving rise to wrongful trading

2.1.1.1 In the case of wrongful trading, the liability is civil by nature and regulated by the Hungarian Insolvency Act.¹⁴

2.1.1.2 Pursuant to the Hungarian insolvency laws, there are several key elements that are required to establish liability for wrongful trading. If any element is missing, the director cannot be held liable.

- (i) The company has to be in a state of imminent insolvency, that is, within the twilight period. Accordingly, the director is not liable for acts performed before the occurrence of the company's imminent insolvency, even if the director's actions had a detrimental effect on the company's assets.¹⁵ However, for acts not falling within the period of imminent insolvency the director can still be held liable by the company under general liability rules.

¹³ § 40, HIA.

¹⁴ § 33/A, HIA.

¹⁵ Summary Opinion, p. 20.

- (ii) Liability can attach only to a director who has been in this position within three years prior to the opening of the liquidation proceedings.
- (iii) Insolvent liquidation proceedings must have been opened against the debtor company. If the debtor is able to avoid opening formal liquidation proceedings, the director will not be liable for wrongful trading. Therefore, the liability for wrongful trading is *per definitionem* retrospective.¹⁶
- (iv) The director knew or should have concluded before the opening of the formal insolvency proceedings that the company was in a state of imminent insolvency.
- (v) The person affected had to be, in a wide sense, a director of the company during the critical period.¹⁷ For the definition of “directors” for the purposes of wrongful trading, please refer to section 1.2.1 above.
- (vi) The director fails to prove that he or she took every step he or she ought to have taken to minimise the loss to the company’s creditors. Should the director as defendant in the wrongful trading litigation be able to prove that he or she took every step with a view to minimising the potential loss to creditors that is to be expected from a person in such a position, then no liability is incurred. Hence, the proof thereof is an effective defence against wrongful trading liability.¹⁸
- (vii) A loss is required to activate the director’s wrongful trading liability: either the debtor’s assets have diminished; or the director obstructed full satisfaction of the creditors’ claims; or has neglected to carry out the cleaning up of environmental damages. However, in order to trigger liability for wrongful trading the director must have disregarded the creditors’ interests and as a result of which the losses occurred. In other words, even if the asset pool diminishes during the critical period, this does not automatically result in the liability of the director. Some additional element, typically a fraudulent or grossly negligent act of the director, is required.¹⁹ Note that case law appears to be divided as to whether payments to selected (but non-related) creditors diminishing both the asset pool of the company and the funds to be distributed to the remaining creditors is contrary to the prohibition of wrongful trading.²⁰

2.1.1.3 The violation of the interests of the creditors is presumed if the director, failing to comply with the law, did not deposit and publish the debtor’s annual accounts prior to the opening of liquidation proceedings and / or breached his or her obligation to cooperate with the liquidator by providing him or her with relevant information and documentation.²¹ Some questions have been raised, however, regarding the interpretation of this provision.

- (i) First, the rule apparently fails to determine the length of the period during which, before the opening of the liquidation proceedings, the failure to deposit and publish the annual accounts is taken into consideration.²²
- (ii) Second,²³ and more importantly, there is some uncertainty in the case law regarding the scope of the presumption. The position of the Curia (the Highest Court in Hungary) is that, if the claimant proves the timing of the occurrence and the beginning of the imminent insolvency, and the increase of the net deficiency in the critical period then, the statutory presumption should be applied. It is presumed that the director neglected the interests of the creditors and

¹⁶ Zoltan Fabok: “Wrongful Trading” in *England and Hungary: A Comparative Study*, p. 89.

¹⁷ Ibid. p. 89.

¹⁸ Ibid. p. 90.

¹⁹ Ibid. p. 92 and BDT2016 3499 (*Debreceni Ítéltábla* Gf. IV. 30 369/2015/6).

²⁰ Ibid. p. 102.

²¹ Ibid. p. 109.

E.g. BH2012. 101 (*Legf. Bír. Gfv. X. 30.361/2010*); Kúria Gfv.VII.30.059/2015/5; Kúria Gfv.VII.30.024/2015/4; ÍH 2013.37 (*Szegedi Ítéltábla* Gf. I. 30.344/2011); ÍH 2013.76 (*Fővárosi Ítéltábla* 13. Gf. 40.002/2012/15); BDT2012. 2619. (*Szegedi Ítéltábla* Pf. I. 20.498/2010); *Fővárosi Ítéltábla* 12.Gf.40.013/2015/6-II; *Fővárosi Ítéltábla* 15.Gf.40.043/2015/5/II. In around 36% of the cases the statutory presumption applies, see P. Lakatos, “A vezető tisztségviselő felelőssége vélelmének fennállásával kapcsolatos kérdések [Questions regarding the Statutory Presumption of the Liability of the Executives]” (undated) (Annex No 5 to the Summary Opinion), p. 82.

²² Zoltan Fabok: “Wrongful Trading” in *England and Hungary: A Comparative Study*, p. 97.

²³ Ibid. p. 97.

this is causal in relation with the losses to the creditors.²⁴ However, other views appear in the case law.²⁵ Notably, the statutory presumption does not operate with regard to shadow directors.²⁶

- 2.1.1.4 Whatever action taken by the director that meets the aforementioned conditions, establishes his or her liability for wrongful trading. Although the potential wrongful acts cannot be exhaustively enumerated, certain scenarios have been identified according to a report issued by the Curia.²⁷
- 2.1.1.5 These scenarios include: if a creditor suffers loss because the director took extraordinarily unreasonable risks; or if the director caused the company to enter in to a loan even though the director should have known that the loan would not be paid back, it is likely that such action would establish the director's wrongful trading liability. Another typical example of wrongful trading is when the director approves the payment of dividends to the members of the company despite the company's imminent insolvency and without raising any objections to such payment at the company's general meeting.²⁸
- 2.1.1.6 Looking at the substance of the cases, it can be observed that most (if not all) of the cases where the courts have established personal liability for wrongful trading, involved an element of fraud by the director. However, this element of fraud is to be understood widely: cases in which the defendant prioritised affiliated entities or shareholders over non-connected creditors seem to suffice to trigger liability for wrongful trading, assuming the further elements are also present.²⁹

2.1.2 The extent of the director's liability

- 2.1.2.1 In the case of wrongful trading, creditors cannot hold the director liable for all their losses vis-à-vis the company. The upper limit of the liability for wrongful trading is the amount by which the assets of the company have diminished during the critical period, as long as it is attributable to the director. Naturally, the director is not liable for losses that are covered by the assets of the company.³⁰
- 2.1.2.2 In the second stage of the litigation process (for details of the two-stages of litigation please refer to section 5.1 below), if the claimant creditor/s establishes the liability of the director in the first litigation proceeding and the amount by which the director diminished the company's assets – the court may order the director to compensate those creditors on *pro rata* basis who initiated the second litigation.
- 2.1.2.3 If more than one director causes damage, they are jointly and severally liable towards the creditors. If the liability of a shadow director is established, this also implies the liability of the *de jure* director.³¹

2.1.3 Defences

- 2.1.3.1 If the director does not meet all of the preconditions listed in section 2.1.1 *supra*, then liability is not incurred. However, the most common defence is pleaded in connection with the director's conduct in respect of the creditors' interests. Thus, should the director as a defendant in the wrongful trading litigation be able to prove that he or she took every step with a view to minimising the potential loss to creditors that is to be expected from a person in such a position, then no liability is incurred. In this case, the burden of proof, falls principally on the director.

²⁴ Kúria Gfv.VII.30.024/2015/4; Kúria Gfv.VII.30.059/2015/5.

²⁵ M. Dzsula, "A vezető tisztségviselő felelősségével kapcsolatos jogalkalmazási problémák II. [Issues regarding application of law relating to the liability of executives II.]" (2013) 23(7) Céghírnök, p. 9.

²⁶ IH 2012.91. (Fővárosi Ítéletábla 14.Gf.40.493/2011/4).

²⁷ Summary Opinion.

²⁸ Ibid. p. 22.

²⁹ Zoltan Fabok: "Wrongful Trading" in England and Hungary: A Comparative Study", p. 109.

³⁰ Legfelsőbb Bíróság Gfv.X.30.047/2011/3.; Debreceni Ítéletábla Gf.III.30.387/2012/5.; Summary Opinion, p. 23.

³¹ Legfelsőbb Bíróság Gfv.IX.30.249/2010/4., Zoltan Fabok: "Wrongful Trading" in England and Hungary: A Comparative Study, p. 93.

- 2.1.3.2 The director may also avoid liability if he or she convenes a general meeting of the company in the wake of the company's imminent insolvency and the director makes a proposal for the resolution of the situation, and the shareholders rejected this proposal.³²
- 2.1.3.3 In addition to these aforementioned examples, according to the Curia's opinion³³ a director does not incur liability if, for instance, he or she voted against the company's action or inaction as a result of which the director becomes liable. The Curia has also pointed out that a director, who does not have the necessary expertise for the role or does not instruct an administrative body to appropriately inform him or her of the financial situation of the company (for example, accountants or other experts), is not exempt from liability.³⁴
- 2.1.3.4 As regards the burden of proof, there appears to be some ambiguity. On the one hand, the wording of the Hungarian Insolvency Act suggests that the claimant is expected to prove that the director, when continuing to trade, disregarded the interests of the creditors.³⁵ On the other hand, the statute provides that the director as defendant, who is able to prove to that he or she has taken all reasonable measures expected from a person in such a position, upon the occurrence of the imminent insolvency so as to prevent and mitigate the losses of creditors, and to prompt the supreme body of the debtor's economic operator to take action, shall not be held responsible. Thus, it is not completely clear on the basis of the wording of the statute, which party is expected to establish that the director reasonably tried to protect the interests of the creditors. The position taken by the Curia is not clear either. In one judgment, the judicial body ruled that the occurrence and the date of the imminent insolvency; the fact and the extent of the increase of the net deficiency; and the causal relation between the behaviour of the director and the increase of the net deficiency were to be proved by the claimant. On the other hand, the defendant director needs to prove that he or she has taken all reasonable measures expected from a person in such a position to prevent and mitigate the losses of creditors.³⁶ However, another judgment suggests that the claimant is also required to establish that the director acted in a way contrary to the interests of the creditors during the critical period.³⁷

2.2 Liability of directors in the case of the company's forced deregistration

- 2.2.1 For the sake of completeness, the director's liability in the case of the company's forced deregistration is also briefly discussed here.³⁸ Forced deregistration proceedings are separate to liquidation proceedings and are governed by a separate statute. In case of deregistration the ultimate dissolution of the company occurs not because of insolvency, but due to other circumstances.
- 2.2.2 By the company's forced de-registration, the company is irrevocably dissolved and removed from the Companies' Register. In practice, the companies that are the subject of forced deregistration proceedings, have no assets and are insolvent. However, in the event that a debtor company has some assets, the court turns the forced deregistration proceedings into insolvent liquidation proceedings.
- 2.2.3 Forced deregistration proceedings aim to remove from the Companies' Register those companies that have seriously violated the statutory law. Among others the following circumstances may result in the forced deregistration of the company (the deregistration is normally applied as an ultimate sanction):

³² *Kúria Gfv.VII.30.081/2013/6.*

The civil code provides that shareholders are required to adopt decisions concerning the subscription of supplementary capital contributions or on securing the initial capital in other ways, on any reduction of the initial capital, or in the absence of all these, on the company's transformation, merger, division or dissolution without succession.

³³ Summary Opinion, p. 26.

³⁴ *Ibid.*

³⁵ For the purpose of establishing the disregard of the creditors' interests by a director, prior to 15 March 2014 the Insolvency Act provided that it must be established that the director failed to act on the basis of the priority of the creditors' interests. The amendment to the Insolvency Act, which entered into effect on 15 March 2014, however provides that the directors are expected to 'take into consideration' the interests of the creditors, rather than prioritise them. However, the changing in the wording of the statute may have no effect on the case law, see A. Csöke, "A vezető tisztviselő felelőssége fizetéseképtelenség és felszámolás esetén [Liability of executives in the context of insolvency and liquidation]", in Z. Csehi and M. Szabó (eds), *A vezető tisztviselő felelőssége [Liability of the executives]* (2015, Wolters Kluwer, Budapest) p. 142.

³⁶ *Legfelsőbb Bíróság Gfv.X.30.047/2011/3.* cf. Summary Opinion.

The Summary Opinion appears to share this view, pp. 25-27, 31-32.

³⁷ This section is from: Zoltan Fabok: "Wrongful Trading" in *England and Hungary: A Comparative Study*, p. 91.

³⁸ § 116, Act V of 2006 on public company information, company registration and winding-up proceedings.

- (i) the company court concludes that the company's lawful operation cannot be restored;
- (ii) the company has not submitted its balance sheet;
- (iii) neither the company nor its directors are available;
- (iv) the Tax Authority withdrew the tax number of the company; or
- (v) the solvent liquidation of the company is not completed within 3 years.

2.2.4 If the company is deregistered on one of the stated grounds, the directors may be liable for the company's debts. The rules that are applicable for the director's liability in this case are almost identical to the rules to be applied to liability for wrongful trading.³⁹ Thus, the director is liable for the outstanding claims of the company's creditors to the extent of his or her contribution to the diminution of the company's assets, if the director failed to properly carry out his or her responsibilities with a view to the interests of the creditors subsequent to the occurrence of the company's imminent insolvency, in consequence of which the company's assets have diminished or the full satisfaction for the creditors' claims was frustrated.

2.2.5 As with the wrongful trading rules, those persons are also considered to be directors who exercised dominant influence on the decision-making mechanisms of the company (i.e. shadow directors).

2.2.6 The meaning of the term 'imminent insolvency' mentioned in section 2.1.1.2, is identical to the 'imminent insolvency' term used for the purposes of wrongful trading liability.

2.2.7 Should the company have more than one director, their liability shall be joint and several.

2.2.8 There are two important differences to the wrongful trading rules as follows:

- (i) First, there is no period within which the director has to be in such position prior to the opening of the 'forced deregistration proceedings' so as to be able to incur liability (as opposed to wrongful trading liability, where this period is three years).
- (ii) Second, contrary to the wrongful trading rules, there is no two-stage litigation process. The creditors may ask for the establishment of the director's liability and for the determination of the compensation payable by the director in the same hearing.

2.2.9 The creditors may bring action against the director – provided that the creditors registered their claims during the forced de-registration proceedings – within 90 days from the publication of the company's termination in the Companies Bulletin.

2.2.10 There are two grounds for a director's exemption from liability. First, directors cannot be held liable, if they are able to prove that the imminent insolvency occurred at a time when they were not a director, or if the imminent insolvency occurred for reasons other than their actions as directors. Notably, directors cannot exempt themselves on this ground under the wrongful trading rules. Second, directors are not liable, if they have taken all reasonable measures expected from persons in such a position, upon the occurrence of a situation carrying the potential threat of insolvency, so as to prevent and mitigate the losses of creditors and to convene the supreme body of the company to take action.

2.3 Criminal offences

2.3.1 Actions giving rise to criminal liability in connection with the twilight period

2.3.1.1 The Hungarian Criminal Code defines four main actions that give rise to the criminal liability of those persons who have control over the company's assets (hereinafter: directors).

- (i) *Culpable management*

The director commits culpable management by, in fact or ostensibly, diminishing the

³⁹ § 118/A, Act V of 2006 on public company information, company registration and winding-up proceedings.

company's assets and therefore preventing the satisfaction of the creditor or creditors in part or in whole. There are some typical acts by which this result can be achieved, however, all must be performed while the company is in the state of imminent insolvency. First, by concealing, disguising, damaging, deteriorating or destroying, or by making unusable the company's assets or any part thereof. Second, by concluding a sham contract, or recognising a doubtful claim. (A sham contract is as defined in the Hungarian Civil Code: if the contract is intended to disguise another contract, the rights and obligations of the parties are to be adjudged on the basis of the disguised contract). However, the list is not exhaustive, and the offence can be committed by other acts as well, if such an act has one of the aforementioned results and is in contradiction to the requirements of the prudent management of the company.⁴⁰

(ii) *Fraudulent failure*

The director commits fraudulent failure, if he or she engages in conduct constituting culpable management in order to artificially cause the company's insolvency, or to cause the appearance of insolvency. In this context, insolvency means 'economic' insolvency, that is, if the company is unable to satisfy its financial obligations as they become due.⁴¹

(iii) *Fraudulent conveyance*

The director is liable for the offence of fraudulent conveyance, if he or she engages in conduct which constitutes culpable management, provided that the company is already insolvent (as opposed to the state of imminent insolvency required for the offence of culpable management referred to above).⁴²

(iv) *Fraudulent preferential treatment of a creditor*

This offence is committed, if the director, as defined in section 1.2.2, provides preferential treatment to any creditor in violation of the priorities of satisfaction specified in the Hungarian Insolvency Act following the opening of the liquidation proceedings.⁴³

2.3.2 Defences

2.3.2.1 These offences may only be committed intentionally. Therefore, it is a defence that the director was not aware of the company's state of imminent insolvency or that the director has not intentionally caused, or acquiesced to, the diminution, or the appearance of the diminution, of the company's assets. It is also a defence that the director has not intentionally caused, or acquiesced to, the failure to satisfy the creditors' claims.⁴⁴

2.3.2.2 In addition, certain defences may also be applicable. Among them, the following:

- (i) being insane at the time of committing the offence;
- (ii) being under coercion or threat;
- (iii) being unaware of the circumstances that made the act an offence (depending on the circumstances, this may be either a complete defence or only a mitigating factor); or
- (iv) having the mistaken assumption that the offence at hand was not harmful to society and having reasonable grounds for this presumption (depending on the circumstances, this may be either a complete defence or only a mitigating factor).

⁴⁰ I. Hegedűs, Zs. Juhász, K. Karsai, T. Katona, E. Mezölaki, Zs. Szomora, S. Törő, "Kommentár a Büntető Törvénykönyvről szóló 2012. évi C. törvényhez" [Commentary to Act C of 2012 on the Criminal Code], (Online Complex Wolters Kluwer Commentary), at § 404.

⁴¹ Ibid.

⁴² Ibid.

⁴³ Ibid.

⁴⁴ Ibid.

3. **Other persons involved with the company's affairs who may be liable in relation to their actions during the twilight period**
 - (a) **In addition to those persons referred to in 1(a) above, can others be held liable in respect of the company's activities during the twilight period?**
 - (b) **In respect of which acts may other persons be held liable and to what extent does the liability of those other persons differ from that for directors identified in Question 1(a) above?**
 - (c) **Can those other persons be made personally liable for all or part of the company's losses or for all or part of the deficit to creditors?**

3.1 **Other persons – wrongful trading**

- 3.1.1 The widely drafted definition⁴⁵ of a shadow director may, in theory, include those who advised the debtor company in a professional capacity (for example, a solicitor or accountant). However, there are no reported cases in which the Hungarian courts established the liability of a professional adviser as a shadow director.⁴⁶
- 3.1.2 Those who fall within the category of a shadow director, can incur the same liability under the same conditions as a *de jure* director: they can be held liable for the same acts and they can be made personally liable for the loss they caused to the company.
- 3.1.3 The extent to which these other persons can be held liable is identical to the extent to which directors may be held liable. Thus, the upper limit of liability for wrongful trading is the amount by which the assets of the company have diminished during the critical period, as long as it is attributable to such other person.
- 3.1.4 One of the peculiar characteristics of the Hungarian legislation is that, in an indirect but unambiguous way, it puts the majority shareholder of the debtor company in the position of a “statutory surety” (guarantor) of the director regarding his or her liability for wrongful trading even if the majority shareholder does not fall within the category of shadow director. The essence of the provision⁴⁷ is that the claimants of the declaratory action, at the first stage of the litigation process, may request the court to order the director as defendant to provide financial security for the case if – typically later, in the second stage (action for performance) – the court finds the director liable for wrongful trading and obliges him or her to pay compensation to the creditors on pro rata basis. Should the judgment ordering the former director to pay compensation to the creditors turn out to be unenforceable, for example because the director is impecunious, then the creditors as claimants will be able to recover their claims approved by the court from the financial security. The peculiar feature of the legislation is that the majority shareholder of the debtor company shall be deemed, by force of law, as a guarantor regarding the financial security if the latter cannot be recovered from the director. By enacting this provision, the legislator expanded the liability for wrongful trading, originally targeting the managers of the company, to include the majority shareholders. Thereby, beyond providing an apparent benefit to the creditors, the legislator virtually eliminated the, otherwise very real, conflict of interest between directors and the majority shareholders arising from the threat of liability for wrongful trading.⁴⁸

3.2 **Other persons – criminal offences**

- 3.2.1 In the case of bankruptcy offences, whoever is entitled to control the assets of the debtor company, or has the opportunity to do so, may commit an offence. Typically, this person is the director, however, the articles of association of the company or other ad hoc authorisations can also give control to other persons. According to legal literature,⁴⁹ the liability can be established with respect to an individual based on his or her personal statements as well, even if it was the company's corporate body who was entitled to dispose of the company's assets ultimately.

⁴⁵ § 33/A(2), HIA.

⁴⁶ Zoltan Fabok: “*Wrongful Trading*” in *England and Hungary: A Comparative Study*, p. 99.

⁴⁷ § 33/A(9), HIA.

⁴⁸ This section is from: Zoltan Fabok: “*Wrongful Trading*” in *England and Hungary: A Comparative Study*, pp. 98-99

⁴⁹ I. Hegedűs, Zs. Juhász, K. Karsai, T. Katona, E. Mezőlaki, Zs. Szomora, S. Törő, “*Kommentár a Büntető Törvénykönyvről szóló 2012. évi C. törvényhez*” [*Commentary to Act C of 2012 on the Criminal Code*], (Online Complex Wolters Kluwer Commentary), at § 404.

3.2.2 Under the criminal rules, the person who committed the offence is not liable for the company's or the creditors' losses. Such a liability attaches to the director only on the basis of the wrongful trading rules.

4. Transactions during the twilight period

(a) On what basis may transactions with the company in the twilight period be set aside?

(b) What defences, if any, are available to a party seeking to protect such a transaction from being attacked?

(c) On what basis may directors and other persons involved with the company's affairs properly incur further credit during the twilight period?

4.1 Voidable transactions

4.1.1 Establishing the liability of the directors under the wrongful trading rules does not necessarily mean that any or all underlying transactions are avoided.

4.1.2 As referred to in section 1.4.2. *supra*, certain transactions can be challenged by the creditors or the liquidator retrospectively, after the opening of formal insolvency proceedings. These transactions are as follows:⁵⁰

(i) Fraudulent transactions

Transactions resulting in the diminution of the debtor's assets provided that the debtor's intention was to defraud the creditors, and the other party to the detrimental contract had or should have had knowledge of such intent. Those transactions that were entered in to within five years of the date of the filing for liquidation against the debtor company can be challenged.

(ii) Transactions at an undervalue

Transactions aiming at the transfer of, or undertaking any commitment for the encumbrance of, the debtor's assets without any consideration, or other transactions with third parties if the stipulated consideration constitutes unreasonable and extensive benefits to a third party. Those transactions that were entered in to within three years prior to the date of the filing for insolvency against the debtor company can be challenged.

(iii) Misuse of guaranties

Transactions aiming at the transfer of ownership by way of guarantee, or assignment of a right or claim by way of a guarantee or exercising a collateralised option to buy, where the beneficiary exercised his or her rights in a way detrimental to the debtor. Those transactions that have been entered in to within three years prior to the date of the filing for insolvency against the debtor company can be challenged.

(iv) Preferential transactions

Transactions giving preference and privileges to any one creditor, such as among others amending an existing contract to the benefit of a creditor, or to providing security to an unsecured creditor. Those transactions that have been entered in to within 90 days prior to the date of the filing for insolvency against the debtor company can be challenged.

4.1.3 In addition to the aforementioned voidable transactions, the liquidator is entitled to reclaim any service the debtor has provided if it resulted in giving preference to any one creditor and if such service is not usually provided under normal circumstances. The prepayment of a debt during the look back period is considered to be such a preference. The look back period for preferential services is 60 days prior to the date of the filing for insolvency against the debtor.

4.1.4 Bad faith and / or gratuitous promise is presumed if the debtor enters into an agreement with

⁵⁰ § 40, HIA.

- (i) a company that is under its (direct or indirect) majority control;
- (ii) a shareholder or director of the debtor (including their relatives); or
- (iii) if a contract is concluded between companies that are not directly or indirectly connected by way of affiliation, but are controlled by the same person or the same company.

4.2 Defences

4.2.1 The transactions referred to in section 4.1.2 can be challenged by either the creditors or the liquidator in the form of submitting a statement of claim to the competent court. In the litigation, the defendants (namely the parties that concluded the challenged transaction) can submit all relevant defences in support of the fact that the transaction at hand does not fall within the aforementioned categories.

4.2.2 In the case of a fraudulent transaction, the burden of proving the bad faith of the transacting parties, the defrauding intention of the company and the *mens rea* of the other party is on the party trying to avoid the transaction.⁵¹ In contrast to the fraudulent transaction, however, for transactions at an undervalue, preferential transactions and misuse of guaranties the *mens rea* of the acting party does not matter: the liability can be established on purely objective grounds.⁵²

4.3 Further transactions during the twilight period

4.3.1 *Incurring further credit in the critical period*

4.3.1.1 The director is free to incur further credit on behalf of the company, even if the company is on the verge of insolvency. During the twilight period, the director, acting in the interests of the company, may want to trade the company out from the difficult situation, but in order to do so is likely to need time and additional credit facilities. In principle, this is not contrary to the obligation of the director to take every step with a view to minimising the potential loss to the company's creditors in the critical period. After all, if the trade out is successful and the company regains its solvency then the creditors' claims will be paid in full and no insolvency proceedings will be opened against the company.

4.3.1.2 It is to be mentioned, that when a company operates on the verge of insolvency and it incurs further credit from 'new' creditors, the position of these new creditors give rise to certain, partially ethical, questions. The new creditors may find that some or all of the 'old' creditors (i.e. those whose claims arose prior to the critical period) were simply paid off from the money coming from the new creditors.⁵³ However, the Hungarian wrongful trading rules, in their current form, do not efficiently protect "new" creditors in such situations.⁵⁴

4.3.2 *Paying off creditors in the critical period*

4.3.2.1 Apart from incurring further credit, the issue of paying off selected creditors in the twilight period also arises. There is a degree of uncertainty as to what constitutes the diminution of assets and which payments by the company, diminishing the asset pool, are deemed lawful.

4.3.2.2 The majority opinion, confirmed by the Curia,⁵⁵ suggests that if the asset pool diminishes in the critical period, even if through paying off some legitimate debts to the creditors, this amounts to the diminution of assets for the purposes of the wrongful trading provisions. A minority of the decisions have concluded that in the event both the assets and the liabilities of the company decrease, for example, by paying off one or more legitimate creditors with due claims, this is not a diminution of assets for the purposes of wrongful trading.⁵⁶

⁵¹ A. Csöke, "Nagykommentár a csődeljárásról és a felszámolási eljárásról szóló 1991. évi XLIX. törvényhez [Commentary to Act XLIX of 1991 on the Hungarian Bankruptcy and Liquidation Proceedings]" (Online Wolters Kluwer Commentary), at § 40.

⁵² Ibid.

⁵³ Zoltan Fabok: "Wrongful Trading" in *England and Hungary: A Comparative Study*, pp. 99-100.

⁵⁴ Ibid. p. 101.

⁵⁵ *Kúria Gfv.VII.30.024/2015/4., BH2016. 179.*

⁵⁶ *E.g. Debreceni Ítéltábla Gf.III.30.387/2012/5, Szegedi Ítéltábla Gf.IV.30.105/2013/5.*

This section is from: Zoltan Fabok: "Wrongful Trading" in *England and Hungary: A Comparative Study*, p. 102.

- 4.3.2.3 As to the question asking which creditors may lawfully be paid off in the critical period, even if at the price of diminishing the asset pool, diverging answers can be found in the case law. At the one end of the scale there are a few judgments concluding that no payment is allowed which diminishes the assets of the debtor company.⁵⁷ At the other end of the scale are those decisions ruling that payments to legitimate creditors, including shareholders, do not violate the prohibition against wrongful trading,⁵⁸ as long as both the assets and liabilities diminish in equivalent proportions.⁵⁹
- 4.3.2.4 What appears to be the majority opinion is that payments to related persons (first of all to the shareholders of the debtor company) are not acceptable.⁶⁰ A number of judgments agree that from the point of view of the liability for wrongful trading a distinction must be made between non-connected creditors on the one hand and the shareholders of the company on the other. The repayment of the shareholder's loan may not frustrate the settlement of claims belonging to non-connected third-party creditors. Some judgments and authors have emphasised that a director, when deciding about payments to be performed during the critical period, should ensure that the specific payment serves to restore the solvency of the company by enabling the continued operation of the business, thus is in the interests of the general body of the creditors.⁶¹
- 4.3.2.5 Hungarian courts appear to accept that payments to those secured creditors whose claim would be covered by the assets anyway, in a hypothetical insolvent liquidation scenario, does not trigger liability for wrongful trading.⁶²
- 4.3.3 Finally, once liquidation proceedings are formally opened against a company, it is only the liquidator who is entitled to accept post-commencement finance and dispose of the company's assets.

5 Enforcement

By whom may action be brought against directors and other persons identified in Question 3 above?

5.1 Wrongful trading - enforcement

- 5.1.1 With respect to the director's liability for wrongful trading, as referred to above, a two-stage litigation process has been introduced in Hungary. During the first stage, after the opening but before the closing of the insolvency proceedings, a declaratory action should be brought against the former director. This claim may be made by either the liquidator or any creditor or creditors. The litigation is declaratory in nature. It is aimed at establishing the liability and the amount of the diminution of assets caused by the continuation of the business activity during the critical period of imminent insolvency.⁶³ No compensation may be sought at this stage of the process. In reality, a significant percentage of reported cases are commenced by creditors, not infrequently by the tax authority.⁶⁴
- 5.1.2 As regards the financial security that may be requested from the director in this first litigation, please refer to section 3.1.4. above.
- 5.1.3 In the second stage of the litigation process, within 90 days from the official publication of the closing

⁵⁷ *Kúria Gfv.VII.30.265/2015/4; Legfelsőbb Bíróság Gfv.IX.30.432/2010/4.*

⁵⁸ But it may well be incompatible with the rules on preferences, see § 40, HIA.

⁵⁹ *Fővárosi Ítéltábla 12.Gf.40.469/2013/5; Pécsi Ítéltábla Gf.IV.30.117/2013/8; Pécsi Ítéltábla, Gf.IV.40.022/2015/4.*

This section is from: Zoltan Fabok: "Wrongful Trading" in *England and Hungary: A Comparative Study*, p. 103.

⁶⁰ *Kúria Gfv.VII.30.193/2013/8; Debreceni Ítéltábla Gf.IV.30.008/2015/5; Szegedi Ítéltábla Gf.III.30.401/2014/2;*

BDT2014. 3241 (Szegedi Ítéltábla Gf. I. 30 509/2012); Győri Ítéltábla Gf.II.20.117/2015/3; BDT2013. 2881

(Szegedi Ítéltábla Gf. I. 30 276/2011.). Similarly, A. Csőke, "A vezető tisztviselő felelőssége fizetési képtelenség és felszámolás esetén [Liability of executives in the context of insolvency and liquidation]", in Z. Csehi and M. Szabó (eds), *A vezető tisztviselő felelőssége [Liability of the executives]* (2015, Wolters Kluwer, Budapest) p. 132.

⁶¹ *BDT2014. 3241 (Szegedi Ítéltábla Gf. I. 30 509/2012); Győri Ítéltábla Gf.II.20.117/2015/3; Debreceni.*

Ítéltábla Gf.IV.30.008/2015/5. Similarly, A. Csőke, "A vezető tisztviselő felelőssége fizetési képtelenség és felszámolás esetén [Liability of executives in the context of insolvency and liquidation]", in Z. Csehi and M. Szabó (eds), *A vezető tisztviselő felelőssége [Liability of the executives]* (2015, Wolters Kluwer, Budapest) p. 132.

This section is from: Zoltan Fabok: "Wrongful Trading" in *England and Hungary: A Comparative Study*, p. 103.

⁶² *Kúria Gfv.VII.30.040/2012/3; ÍH 2013.37. (Szegedi Ítéltábla Gf. I. 30.344/2011).*

This section is from: Zoltan Fabok: "Wrongful Trading" in *England and Hungary: A Comparative Study*, p. 103.

⁶³ 1/2013. (II. 28.) Polgári jogegységi határozat. See A. Csőke, "A vezető tisztviselő felelőssége [Liability of the executive]", in A. Csőke, E. Lettner and Cs. Juhász, *Nagykommentár a csődeljárásról és a felszámolási eljárásról szóló 1991. évi XLIX. törvényhez [Comprehensive Commentary on the Insolvency Act]* (2015, Wolters Kluwer, Budapest) [electronic edition], at § 33/A.

⁶⁴ This section is from: Zoltan Fabok: "Wrongful Trading" in *England and Hungary: A Comparative Study*, p. 96.

of the insolvency proceedings in the Companies Bulletin, assuming that the assets of the debtor do not or only partly cover the creditors' claims (so in virtually all cases), the creditors, but no longer the liquidator may bring an action for compensation. In this second phase of the litigation the court, if it approves the claim, orders the former director to compensate those creditors on *pro rata* basis who initiated this second litigation.

5.1.4 The maximum compensation to be shared among those creditors bringing the claim amounts to the net deficiency accumulated during the critical period as established by the court in the first phase of the litigation.

5.1.5 One of the inexplicable peculiarities of the rules is that the second stage of the litigation process may only be initiated by a creditor or creditors, this may, however, include creditors who did not participate in the first litigation stage. The root of the problem is that – for an unknown reason – the statute does not require the defendant director to contribute to the assets of the debtor company.⁶⁵ Instead, the claimants are free to enforce their claims on a quasi-individual basis in this second stage of proceedings. This appears to contradict the principle of collective insolvency proceedings.⁶⁶

5.2 Voidable transactions - enforcement

5.2.1 With regard to the voidable transactions referred to in detail in section 4.1.2. above, the creditors or the liquidator (in the name of the company) may bring an action within 120 days from the time of gaining knowledge or within a one-year limitation period from the date of publication of the notice of liquidation. If the creditors initiate the litigation, the company will be a defendant to the litigation.⁶⁷

5.2.2 In these cases, the claimants are not aiming at establishing the director's liability, but only to avoid a particular transaction and thus recover the asset subject to the transaction to the company's asset pool.

6 Remedies available

In respect of the acts identified in Questions 2, 3 and 4 above, what remedies are available?

6.1 Remedies for wrongful trading

6.1.1 First, if a director commits wrongful trading, he or she can be held personally liable for the loss that the creditors suffered during the twilight period. As mentioned before, the monetary limit of the director's liability is the decrease of the asset pool of the debtor company in the period which begins with the occurrence of the debtor company's imminent insolvency and ends with the debtor company entering in to liquidation proceedings.

6.1.2 Second, if the court establishes the director's liability for wrongful trading (in the first litigation) and the director fails to compensate the creditors (after the second litigation), then the director will be disqualified for five years by the competent court. The disqualification means that for five years the director cannot acquire majority control in any company; cannot be a shareholder with unlimited liability in any company or of a sole proprietorship; and, most importantly cannot be the director (or representative) of any company.⁶⁸

6.2 Remedies for voidable transactions

6.2.1 If the litigation is successful, the transactions will be declared void. As a result, typically the party contracting with the debtor is required to return the asset to the insolvency estate. The contracting party may lodge a claim against the debtor to the liquidator and if accepted may expect a *pro rata* distribution (if any) according to the hierarchy of the creditors' claims.

⁶⁵ e A. Csőke, "A vezető tisztségviselő felelőssége [Liability of the executive]", in A. Csőke, E. Lettner and Cs. Juhász, *Nagykommentár a csődeljárásról és a felszámolási eljárásról szóló 1991. évi XLIX. törvényhez [Comprehensive Commentary on the Insolvency Act]* (2015, Wolters Kluwer, Budapest) [electronic edition], at § 33/A.

⁶⁶ This section is from: Zoltan Fabok: "Wrongful Trading" in England and Hungary: A Comparative Study, p. 97.

⁶⁷ J. Gál, L. Juhász, Á. Mika: "Társasági jogi perek [Company law litigations]" (2018, HVG-ORAC Lap és Könyvkiadó Kft., Budapest), p. 363.

⁶⁸ § 9/B, Act V of 2006 on public company information, company registration and winding-up proceedings.

6.3 Remedies for acts identified in section 2.3.1.1. (criminal offences)

Act	Remedy
Culpable management	Felony, punishable with imprisonment between 1 to 5 years.
Fraudulent failure	Felony, punishable with imprisonment between 1 to 5 years.
Fraudulent conveyance	Felony, punishable with imprisonment between 1 to 5 years.
If the abovementioned offences are committed with respect to a company of strategic importance, or if the diminution of the assets, actually or fictitiously, exceeds HUF 500,000.	Felony, punishable with imprisonment between 2 to 8 years.
Fraudulent preferential treatment of a creditor	Misdemeanor, punishable by imprisonment not exceeding two years.

7. Duty to co-operate

- (a) **To what extent are directors and other persons identified in Question 3 above obliged to co-operate with the insolvency office-holder's investigation into the company's affairs?**
- (b) **Is this obligation modified by any rules in relation to the defence against self-incrimination? Are any human rights laws applicable to such obligations?**

7.1 Duty to co-operate with the liquidator

7.1.1 The Hungarian Insolvency Act enumerates the obligations of the director to co-operate with the liquidator. The main obligations of the directors are as follows:⁶⁹

(i) **Duty to provide information**

It is a general obligation of the director to assist the liquidator during the liquidation proceedings and to provide information at the liquidator's request concerning the company's activities in particular with respect to the whereabouts of the company's assets.

The director must also inform the liquidator of any transactions identified in section 4.1.2 (the voidable transactions).

(ii) **Assets and documents**

The director must hand over the company's assets and documents to the liquidator. In connection with this obligation, the director is required to provide access to the company's closed and sealed properties. The director must prepare a list of the documents that may not be discarded, and deliver such documents, as well as archive materials to the liquidator. The director must also hand over to the liquidator any assets that do not belong to the company.

(iii) **Financial statements and inventories**

The director has to prepare the applicable financial statements (a closing inventory, the annual accounts or simplified annual accounts, a closing balance sheet and a tax return) of the company and give them to the liquidator (and the tax authority). In connection with these financial statements, the director is obliged to provide a statement confirming that the financial statements provide a true and fair view of the debtor company's financial situation.

7.1.2 If the director does not comply with the statutory obligations, the court can order that the cost of obtaining the required information by other means is borne by the director who is in breach of his or her obligations.

⁶⁹ § 31, HIA.

- 7.1.3** In addition, the director faces a civil fine if he or she fails to meet their obligations or to co-operate with the liquidator. The maximum of the fine is 50% of the director's income received from the company in the year prior to the opening of the liquidation proceedings. If the income cannot be established, it might be up to HUF 2 million.⁷⁰ Notably, former directors of the company may also be fined, if it can be established that the former directors failed to comply with one of their obligations and did not co-operate with the liquidator, despite the liquidator's explicit request.⁷¹
- 7.1.4** Prior to 2012, the criminal law imposed sanctions on directors in connection with their failure to comply with their duty to co-operate with the liquidator. However, the legislator abolished the administrative bankruptcy offence in 2012 (see further below) and there are no criminal sanctions against such non-cooperation.
- 7.1.5** The liquidator may also enter any of the debtor company's premises and search and inspect any of the debtor's assets.
- 7.1.6** It is a common problem that a director resigns from a company before his or her cooperation duties are triggered. The Civil Code tries to redress this situation by providing that if the company's operation requires so, the resignation of the director becomes effective only with the appointment of a new director, or, failing that, with the expiration of 60 days from the date of resignation.⁷²
- 7.2 Self-incrimination and human rights**
- 7.2.1** In line with Article 6 of the European Convention of Human Rights (ECHR), the defence against self-incrimination is a well-established principle enshrined in the Hungarian criminal procedure.
- 7.2.2** Moreover, since Hungary is party to the ECHR, those persons who fear of self-incrimination, may rely on the provisions of the ECHR before Hungarian Courts.
- 7.2.3** The potential for self-incrimination by a director may occur in particular in relation to the director's duty to provide the liquidator with information regarding any potential voidable transactions of the company. If the director disclosed to the liquidator that he or she had committed a fraudulent transaction whilst acting as a director of the company, that might very well have established the criminal offence of culpable management. This is exacerbated by the fact that the liquidator is obliged to report any potential criminal offence that he or she has discovered in connection with the company's liquidation.⁷³
- 7.2.4** Prior to 2012, there was a potential for self-incrimination (in theory at least) because the criminal law sanctioned the director's failure to co-operate with the liquidator (by the so-called administrative bankruptcy offence).⁷⁴ However, the legislator abolished the administrative bankruptcy offence in 2012, and thus there are no longer criminal sanctions for the director's non-cooperation. Hence, in the field of criminal law at least, the danger of self-incrimination ceased to exist.

8. Appeals and limitation periods

- (a) What limitation period, if any, applies to the actions referred to above?**
- (b) What rights of appeal are available from the decisions of the lower courts?**

8.1 Limitation periods

8.1.1 Limitation periods for wrongful trading

- 8.1.1.1** The first litigation, establishing the director's liability for wrongful trading, may be initiated after the opening but before the closing of the liquidation proceedings.
- 8.1.1.2** The second litigation, for determining the compensation to be paid by the director, may be initiated

⁷⁰ § 33(1), HIA.

⁷¹ BDT 2016.3435.

⁷² § 3:25(4), Act V of 2013 on the Civil Code.

⁷³ § 404/A, Act C of 2012 on the Criminal Code.

⁷⁴ See: G. Kertész, "Az adminisztratív csődbüntetés és a kisvállalkozások [Administrative bankruptcy crime and the small enterprises]" (2006, Tudományos Közlemények 14-15.) p. 156.

within 90 days from the official publication of the closing of the liquidation proceedings in the Companies Bulletin.

8.1.2 Limitation periods for voidable transactions

- 8.1.2.1 The avoidance claim will lapse unless the claimant starts the litigation within 120 days from the time of gaining knowledge but within one year after the opening the insolvency proceedings at the latest.

8.1.3 Limitation periods for criminal offences in connection with the twilight period

- 8.1.3.1 The prosecution of culpable management, fraudulent failure and fraudulent conveyance, will be time-barred after five years from the commitment of the offence.
- 8.1.3.2 If, however, the offences were committed in respect of a company with strategic importance, or the diminution of the assets, actually or fictitiously, is particularly substantial (exceeds HUF 500,000) the limitation period for prosecution is 8 years from the date of the offence.
- 8.1.3.3 In case of the preferential treatment of a creditor, the limitation period for prosecution is 2 years from the date of the offence.

8.2 Appeals

- 8.2.1 Court judgments in relation to wrongful trading or voidable transactions must be appealed within 15 days from the time of the delivery of the first instance judgment. As a general rule, the appeal stays the enforcement of the judgment.
- 8.2.2 The appellate court reviews the judgment of the lower court within the scope of the appeal. Moreover, with certain exceptions, new evidence cannot be offered to the appellate court.
- 8.2.3 If, in the first phase of the wrongful trading litigation, the court orders the defendant to provide the financial security specified in section 3.1.4. above, the defendant may appeal against this decision, such an appeal application must be decided by the second instance court within 15 days of the appeal.
- 8.2.4 After the hearing of the appeal application by the second instance court, the losing party may submit a petition for judicial review to the Curia within 45 days from the delivery of the judgment, with a claim that the second instance court's judgment breached the law. The petition for judicial review is essentially a second, though limited, appeal.
- 8.2.5 A party's right to appeal to the Curia is not automatic but is subject to certain conditions and / or the discretion of the Curia. A party may not have recourse to the Curia with a petition for judicial review, if, among others, (i) the party did not exercise his or her right to appeal against the first instance judgment and the second instance court upheld the first instance judgment under the appeal by the other party, or, (ii) if the claimed amount does not exceed HUF 5 million. In the latter instance, the Curia may accept the petition under some extraordinary circumstances.
- 8.2.6 An appeal may be made against a judgment for one of the criminal offences referred to in section 2.3.1.1 above. If the judgment of the second instance court on appeal is contrary to the first instance judgment, the losing party may appeal to the third instance court. Under certain circumstances, it is possible to file a petition for judicial review against either the first or the second instance court judgments. However, a petition for judicial review may not be made against a judgment of the third instance court on the basis of infringement of the law

9. Foreign corporations

Do the provisions outlined above apply to both domestic and foreign corporations?

9.1 Companies within the European Union

9.1.1 Regulation No. 2015/848 of 20 May 2015, which came into force in European Union Member States (except Denmark) on 26 June 2017 (Recast Insolvency Regulation) lays down procedural rules applicable to European cross-border insolvency cases. The purpose of the Recast Regulation is to address the situation of the debtor having creditors or assets in more than one Member State of the EU. The Recast Regulation classifies insolvency proceedings either as main or territorial / secondary liquidation proceedings. The courts of the Member State within the territory of which the centre of the debtor's main interests (COMI) is situated shall have jurisdiction to open main insolvency proceedings.⁷⁵ The COMI is the place where the debtor conducts the administration of its interests on a regular basis and which is ascertainable by third parties. In the case of a company or legal person, the place of the registered office shall be presumed to be the centre of its main interests in the absence of proof to the contrary.

9.1.2 Similarly, as to companies whose COMI is within European Union the laws of the Member State in which the main insolvency proceedings have been opened determines, as a general rule, the applicable laws regarding the insolvency proceedings.

9.1.3 The company's COMI also determines the applicable law as to the liability of the directors.⁷⁶ Even if, a company is registered in Germany, but the main insolvency proceedings are opened in Hungary (because the company's COMI is situated in Hungary), the Hungarian wrongful trading rules specified above shall apply to the director's liability.

9.1.4 Secondary insolvency proceedings may be opened in a Member State in which the company's establishment⁷⁷ is situated (provided that the company's COMI is within the EU). The law applicable to these proceedings shall be that of the Member State in which the secondary insolvency proceedings is opened. For instance, if a French company has an establishment in Hungary, then, assuming that secondary insolvency proceedings have been opened, the Hungarian insolvency rules (including the wrongful trading rules) shall apply to the Hungarian secondary insolvency proceedings.

9.2 Companies outside the European Union

9.2.1 As to companies, whose COMI is outside the European Union, the Hungarian courts have jurisdiction for the insolvency proceedings if the company's seat is in Hungary or has a place of business (branch office or other establishment) in Hungary, where it carries out a non-temporary economic activity.⁷⁸ If Hungarian courts have jurisdiction, then, according to the Hungarian Act on Private International Law,⁷⁹ as a general rule, Hungarian insolvency laws apply to the proceedings.

10. Insurance

Is directors' and officers' insurance available in your jurisdiction? If so, to what extent will the availability of such insurance provide effective protection to directors against personal liability which may arise in connection with the issues raised in Questions 1-9 above?

10.1 Directors' insurance is available and widely used in Hungary.⁸⁰

10.2 The insurance covers a director's civil law liabilities incurred in connection with this position. Sometimes, the insurance covers legal costs as well.

⁷⁵ Art. 3 of Regulation (EU) 2015/848 (Recast Regulation): The centre of main interests shall be the place where the debtor conducts the administration of its interests on a regular basis and which is ascertainable by third parties.

⁷⁶ cf. *Case C-594/14 Kornhaas v Dietmar*.

⁷⁷ According to the Regulation (EU) 2015/848 (Recast Regulation), 'establishment' means any place of operations where a debtor carries out or has carried out in the 3-month period prior to the request to open main insolvency proceedings a non-transitory economic activity with human means and assets.

⁷⁸ § 100, Act XXVIII of 2017 on Private International Law.

⁷⁹ § 66-67, Act XXVIII of 2017 on Private International Law.

⁸⁰ The information in this section 10 is based on the following article: T. Bögös, "A vezető tisztségviselők felelőssége – 3 rész: Vezető tisztségviselők felelősségbiztosítása [The liability of the director – 3rd part: the liability insurance of the director]; available at: <https://advocatus.dlapiper.hu/?p=2158>

- 10.3** In addition to directors, additional persons of company may be also insured by the same insurance. For instance, it is possible to insure officers, members of the supervisory board or leading employees of the company.
- 10.4** Although not prescribed by any law, the insurance contract is usually concluded by the company for the benefit of its director.
- 10.5** In practice, there are two main types of directors' insurance. The first one covers damages incurred whilst the insurance is in place, whereas the second one covers damages that are claimed whilst the insurance is in effect. Naturally, these two main types can be combined as well.



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