

NEW TAKE-OVER RULES IN HUNGARY

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The recent transactions (early 2001) on the Hungarian stock market (mostly in the field of chemical industry) showed some "gaps" in Hungary's take-over rules, which rules had been in effect since June 18, 1998. In addition, the Budapest Stock Exchange (the "BSE") noted that pursuant to their experience, public companies could be controlled via holdings of less than 33% of the voting interest (which was originally the threshold above which the take-over rules were applicable).

When the previous take-over rules were initially enacted, the experience of the Hungarian Financial Supervisory Authority (the "PSZÁF") was limited to foreign examples, although it had to in practice examine how to ensure the utmost of transparency on the Hungarian capital markets. Consequently, the past three years' experience showed that the take-over rules required revision to ensure the due functioning of the take-over rules, namely that the interests and rights of minority shareholders were actually protected. The BSE's and the PSZÁF's accumulated experience also motivated the introduction of a new reporting obligation to maintain an up-to-date public record of those shareholders who exert influence over public companies.

For example, while the previous take-over rules required that any shareholder (whether *indirectly* or *directly*) who held over 33 percent of a public company's voting shares and who wanted to increase this shareholding through the acquisition of additional shares via a share transfer was obliged to commence a public offer for at least an additional 50 percent of the shares. However, the main problem was how to guarantee the above protections in cases in which the take-over of voting rights was carried out *indirectly* and without the actual transfer of any shares, which procedure was not specifically addressed in the previous take-over rules. Therefore, it was rather easy to bypass the legal requirement by acquiring of voting rights in the target company, e.g., via the establishment of a contractual relationship between the acquirer and the holder of voting shares. Under the previous provisions, a mandatory public offer was also not required if the acquisition of influence (i.e., more than 33% of the voting rights) was effectuated through the subscription of new shares or by decreasing the company's share capital since only acquisition involving a transfer of shares triggered the mandatory take-over bid.

In response, new take-over rules were passed by the Hungarian Parliament pursuant to Act L of 2001 on the Amendment of Financial Regulations, which also modified the Securities Act (Act CXI of 1996) in which the take-over rules are actually incorporated. These new regulations came into effect on July 18, 2001 (the "**New Take-over Rules**") and they are applicable to any activities resulting in gaining of influence after this date. If the statutes (bylaws) of a public company contain any provision which is different from the mandatory rules, the statutes (bylaws) shall be amended accordingly at the next general meeting to take place after July 18, 2001; however, the provisions

on the thresholds for mandatory public offers and public offer prices must be amended until June 30, 2004.

The commentary and analysis herein will only generally address the main considerations and modifications brought about by the New Take-over Rules.

(1) CLARIFICATION OF DEFINITIONS (GAINING INFLUENCE, INDIRECT INFLUENCE)

- 1.1 The scope of the Securities Act has been modified in the sense that the Securities Act clearly now extends to certain rules concerning the gaining of influence with respect to a public company limited by shares ("**Public Company**"). Additionally, the powers of the supervision authority, the PSZÁF have been explicitly specified in connection with the activities concerning the supervision related to the gaining of influence in a Public Company.
- 1.2 The Securities Act, for the sake of clarity, now defines the phrase "**gaining of influence**". Pursuant to the modified Section 94 of the Securities Act, "gaining of influence" means:
 - (a) the acquisition of voting rights exercisable at a shareholders' meeting of a Public Company ("**voting interest**"), including:
 - (i) the acquisition of the voting interest by exercising of an option right, or repurchase right granted for the acquisition of a voting interest,
 - (ii) performance of a futures contract with respect to the acquisition of a voting interest,
 - (iii) the exercising of voting rights on the basis of a use or usufructuary agreement,
 - (iv) other circumstances not directly aiming at the gaining of influence, especially, inheritance, legal succession, or agreement among the shareholders of the Public Company effecting a change in the proportion of voting rights belonging to shareholders holding such voting interests;
 - (b) an agreement between a shareholder of a Public Company and other shareholders pursuant to which (i) the shareholder shall be entitled to appoint and replace the majority of the officers/directors and supervisory boards members, or (ii) the parties to such agreement shall control the Public Company pursuant to so-called "consented principles" (e.g., formal understandings or mutually agreed to guidelines).
 - (c) the harmonized conduct of independent persons having voting interests.
- 1.3 On assessing the facts and the extent of any acquisition of influence, the direct and indirect acquisition of influence and the extent of influence exercised by close relatives shall also be taken into account. For the purposes of the Securities Act, indirect proprietary interest and indirect influence mean exercising voting rights and those proprietary interests - including cases referred to in (b) above - in an undertaking through the proprietary interests in or voting interests held in of another undertaking ("intermediary undertaking"). On assessing the extent of such indirect property and indirect influence, the voting rights or proprietary

interests of the undertaking having an indirect proprietary interest or indirect influence held in the intermediary undertaking shall be multiplied by the voting rights or proprietary interest of the intermediary undertaking held in the target undertaking, depending on which number is higher - leading to a rather complicated calculation. Should the voting rights or proprietary interest held in the intermediary undertaking exceed 50%, it shall be calculated as 100%.

- 1.4 It should be noted that shareholder representatives (e.g., banks acting as GDR depositaries) who represent ultimate beneficial owners of any particular shares in a Public Company must be registered in the respective company's Shareholder Register (which is the statutory requirement for the exercising of voting rights over said shares) - along with the actual owner of the particular shares. Otherwise, the shareholders' representatives will be deemed to be the "actual" shareholder if they have only registered themselves. In the latter case, the rules applicable to the gaining of influence shall directly apply to such shareholders' representative.

(2) REPORTING AND PUBLICATION OF GAINING INFLUENCE

- 2.1 Similarly to the international practice on point, for the purposes of protecting shareholders' interests against so-called hostile take-overs, in the statutes (by-laws) of many Hungarian Public Companies, an acquisition of over 5 or 10% of the voting shares (whether directly or indirectly) must be reported to the Board of Directors before the acquirer would have the right to exercise the attaching voting rights. In lack of such reporting, the exercising of voting rights in excess of the interest reported shall not be effective vis-a-vis the company, i.e. the shareholders may only exercise their voting rights up to 5% or 10%, depending on the particular statutes (by-laws).
- 2.2 The New Take-over Rules introduced similar requirements so that in addition to the Board of Directors, the PSZÁF would also be notified to ensure that it will have an accurate and more up-to-date information on the relevant ownership structure, which would enable it to supervise the due compliance with the take-over rules. Previously, Public Companies only had to annually report such information pursuant to the annual reporting obligations under the Securities Act on any changes which occurred to their ownership structure with respect to shareholders owning at least a 5% interest.

In compliance with the provisions of Council Directive 88/627/EEC on the information to be published when a major holding in a listed company is acquired or disposed of, pursuant to the newly introduced rules, the gaining or termination of influence representing 5, 10, 15, 20, 25, 30, 35, 40, 45, 50, 75, 90 percent must be reported to the PSZÁF (and the Board of Directors) within 2 days of its occurrence and an announcement must be made - *in the Official Gazette of the Budapest Stock Exchange/Magyar Tőkepiac* and in the publication in which the Public Company generally publishes its statutory announcements as well as the BSE's website without delay.

The statutes (bylaws) of the Public Company may also stipulate, that the reporting and announcement obligations set forth above shall also apply if an increase or decrease in the acquisition of influence reaches two percent.

- 2.3 In lack of compliance, the shareholders' rights may not be exercised until due compliance with same. Whereas previously, the fines which could have been imposed by the PSZÁF for breaching reporting rules were between HUF 10,000 - 500,000, pursuant to the new regulations the fine may be between HUF 500,000 - 100,000,000 (appr. USD 1,500 - USD 350,000).

(3) MANDATORY PUBLIC OFFER - APPLICABLE THRESHOLDS

- 3.1 Whereas the previous take-over rules required that for the acquisition of voting shares via share transfers representing more than 33 percent of the voting shares in a Public Company, an offer for at least an additional 50 percent of the voting shares be made, the New Take-over Rules now require a public offer for *all the remaining (outstanding) voting shares and with respect to all shareholders holding voting shares*.

The New Take-over Rules further qualify the above new requirement by stipulating that in the event that no other shareholder holds more than 10 percent of the voting shares, then such mandatory public offer shall kick in once a potential shareholder wishes to acquire more than a 25 percent voting interest. The main reason for the introduction of the 25 percent threshold requirement (in the interest of protecting minority shareholders' rights) was based on the above described experience of the BSE and PSZÁF, mainly that a control position may be achieved by far less than a 33 percent voting interest.

If the statutes (bylaws) of a Public Company contain any provision on the threshold for takeover bids which is contrary to the above, the statutes (bylaws) shall be amended accordingly at the latest until June 30, 2004.

It shall be noted that if an undertaking has an influence of more than 25% or 33% and such influence was not acquired through a public offer under the previous rules, the influence in the undertaking may be increased only in compliance with the New Take-over Rules.

- 3.2 As a main principle, the public offer must be made in advance with respect to the contemplated gaining of influence exceeding the 33 % or 25% thresholds (as the case may be). In certain cases, however, if the gain of influence occurs via the methods specified in Section 1.2 (a) (i) - (iv) and (b) above, and if the transaction is carried out pursuant to a procedure regulated by law with the participation of the state property management agency (the APV Rt.), the public offer may be made within 15 days of the reporting of the gaining of influence exceeding the threshold.

- 3.3 The legal consequence of breaching the mandatory rules concerning the obligation to make a public offer previously was that the share transfer agreement which was concluded without carrying out a public offer was deemed null and void. Pursuant to the New Take-over Rules,

if the gaining of influence is not carried out in compliance with the mandatory regulations, the shareholders' rights may not be exercised and the voting interest exceeding 33% or as the case may be 25% must be sold within 60 days of the resolution of the PSZAF establishing the breach. Additionally, the New Take-over Rules introduced a rather effective additional sanction by establishing that until the sale of such “illegally obtained” shares, the shareholder may not exercise any shareholders’ rights with respect to those shares already held by the shareholder but are nonetheless below the threshold.

(4) MANDATORY ELEMENTS OF A PUBLIC OFFER

4.1 It should be noted that pursuant to the New Take-over Rules, the person(s) making the public offer must evidence the financial resources to support the offer when the terms of the public offer are submitted for approval to the PSZAF pursuant to the applicable prospectus.

4.2 Additionally, the new provisions of the Securities Act stipulate that the person(s) making the public offer may only reserve the right to waive the offer if pursuant to the acceptance declarations the person(s) making the offer may not gain an influence over 50% of the voting shares, whereas pursuant to the former rules the offeror was permitted to waive the offer if the acceptance declarations did not reach the statutory offer minimum (i.e., minimum of 83%) and the offeror could have excluded the fulfillment of the acceptance declarations which exceeded the offer.

(5) PUBLIC OFFER PRICE

5.1 Previously, the Securities Act differentiated between three cases in connection with the establishment of the minimum public offer price, which structure has been retained by the New Take-over Rules.

(a) Minimum public offer price in the case of shares introduced on the stock exchange

Whereas the former rules required that the price be a minimum of the weighed average stock price during the 90-day-period preceding the public offer, the new rules set forth that the minimum price shall be the highest among three possible prices: (i) the weighed average stock price calculated on the basis of the trade volume during the 180-day period preceding the submission of the draft offer for approval to PSZAF, or (ii) the highest share transfer price between the offeror and related parties during the prior 180 days, or (iii) in the case of exercising an option or repurchase right, the aggregate of the option fee and price.

(b) Minimum public offer price in the case of shares not introduced on the stock exchange

The former rules required that the price be a minimum of the weighed average price published during the 180 days preceding the public offer (such publication usually occurred in a manner that brokers published in certain newspapers the sale and

purchase offers for shares traded on the OTC market.) The New Take-over Rules set forth that the minimum price shall be the highest among three possible prices: (i) the weighed average published price calculated on the basis of the trade volume during 180 days preceding the submission of the draft offer for approval to PSZAF, or (ii) the highest share transfer price between the offer and related parties during the past 180 days, or (iii) in the case of the exercising an option or repurchase right, the aggregate of the option fee and price.

The New Take-over Rules established a minimum price requirement more beneficial to minority shareholders on the basis of the PSZÁF's practice dating back to 1998. In many instances, stock prices are far below the "secondary market price" of Public Companies for which a 25% or 33% voting interest is sold to an offeror by current shareholders. The newly introduced rules intend to establish that minority shareholders shall also benefit from such a more favorable secondary market price.

- (c) Minimum public offer price in the case of shares not introduced on the stock exchange, provided that there is no published market price

The PSZÁF shall assess in the course of the prospectus' approval as to whether the price offered by the offeror is acceptable.

- 5.2 If the statutes (bylaws) of a Public Company contain any provision on the public offer price which is different from the above, the statutes (bylaws) shall be amended accordingly at latest until June 30, 2004.
- 5.3 The New Take-over Rules also shortened the maximum term of the offer period from 60 to 45 days. (Therefore, the deadline for accepting a public offer shall be no less than 30 days and no more than 45 days.) Before the expiration of the deadline, the offeror may amend the public offer with respect to the purchase price, provided that the amended purchase price - calculated in HUF - exceeds that of the original offer. In such a case, the increased purchase price is applicable even to the acceptance declarations made before the publication of the amendment and increased offer price.
- 5.4 Counter-offers may still be made, if the HUF equivalent of the offered price is higher by at least 5% of the originally offered price. The new element is that the calculation base must be HUF. Additionally, the counter-offer must be submitted at the latest 15 days prior to the expiration of the offer, which now provides essentially only 30 days to a potential counter-offeror (previously, up to 50 days was provided).

(6) OBLIGATIONS OF THE BOARD OF THE OFFEREE COMPANY

- 6.1 The Board of Directors of a Public Company, from the time of the receipt of the public offer within the deadline available for the acceptance of the public offer, may not pass any resolution that might interfere with the proceedings, such as increasing the registered capital

of such Public Company or acquiring the Public Company's own shares. The New Take-over Rules further clarifies that if the Board obtains knowledge of the purchase intention before the official receipt of the public offer, the obligation to abstain from actions as set forth above is applicable

6.2 The New Take-over Rules introduced that the Board of the offeree company shall draw up and make public its opinion on the public offer before the first date for the acceptance of the public offer.

(7) VOLUNTARY PUBLIC OFFER

The possibility to commence a so-called voluntary public offer is also regulated by the New Take-over Rules. A public offer shall be deemed as voluntary if the offeror does not wish to gain influence beyond the previously-mentioned thresholds. To make a voluntary public offer, the rules applicable to mandatory public offers shall apply, provided, however that the requirement concerning the minimum extent of the offer (i.e., for 100% of outstanding shares) in such a case would obviously not apply. In addition, the rules concerning the obligation of the Board to comment on the terms of the public offer and the right of the Board to obtain the services of an independent financial expert to evaluate the offer is not applicable, and counter-offers may not be made. If the acceptance declarations exceed the offer, the transfer of the shares to the offeror may be carried out proportionately.

A voluntary public offer may not be made at all during the term when there is a pending mandatory public offer. This rule essentially prevents minority shareholders from making a voluntary offer for e.g. 25% + 1 of the voting shares during a pending mandatory offer (with the aim of such voluntary offer being that in the case when the minority shareholders know that the offeror desires to acquire a 75% + 1 voting interest and the minority shareholders find the offer price insufficient, then if they together would be able to gain a 25% + 1 voting influence, they would then perhaps be able to force the person(s) making the mandatory offer to purchase their combined 25% + 1 share at a greater more premium).

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