THE EUROPEAN UNION GOES EAST
CAPITAL MARKETS

(CAPITAL MARKETS AND CORPORATE TAKEOVER LEGISLATION IN HUNGARY)

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Author: Dr. András Szecskay

PART I

HUNGARIAN CAPITAL MARKETS

1. GENERAL LEGAL OVERVIEW ON THE CAPITAL MARKETS IN HUNGARY

1.1 Underlining Regulations on the Participants, Market Instruments, Securities Trading and Supervision

Between 1988 and 1991, legislation covering company law, securities trading, investment funds, banking activities and bankruptcy established within Hungary the regulatory framework of capital markets (i.e., the issuance of securities, terms of operation of issuers and professional investment services companies, tasks and scope of authority of governmental supervisory authorities and the terms of establishment and operation of a stock exchange).

Over the last ten years, it has become clear that in the course of Hungary's transition to a market economy, one of the major driving forces fuelling economic development is the level of maturity of the capital markets, and in particular, the ability of the market, on the one hand, to finance market participants, and on the other one hand, to regulate and supervise these participants to prevent unauthorized financial activities in the interest of investors and creditors.

The first wave of development of the Hungarian capital markets regime coincided with the second phase of the privatization process, when the state holding company offered its shares in partially privatized companies to the public and foreign investors responded favorably to this emerging Hungarian market. In the past two years, however, for a relatively large number of small and medium-sized investors, capital market investments have become a "habit", a trend which continues to develop.

The recent improvement (strengthening) of the capital markets in Hungary can be seen not only with reference to the rise in the levels of large investor participation, but also with regard to the increasingly sophisticated expectations from different categories of investors in respect of market instruments, i.e., the forms and methods of investment. At the same time, foreign investors wish to see similarities in the regulation and operation of the capital markets which coincide with Hungary's goal to join the European Union and the harmonization of its laws with EU regulations.

These motivations encouraged the revision of the Act on the Offering of Securities, Investment Services and on the Stock Exchange (revised by Act CXI of 1996, hereinafter the "Securities

Act"), the Act on Credit Institutions and Financial Enterprises (revised by Act CXII of 1996, hereinafter the "Financial Institutions Act"), the Act on Business Associations (revised by Act CXLIV of 1997, hereinafter the "Company Act"[1]), the Act on the Prohibition of Unfair Market Practices (revised by Act LVII of 1996, hereinafter the "Competition Act") and the passing of new laws, i.e., on Risk Capital Companies and Funds, as well as Loan Mortgage Companies, etc., in order to ensure the same level of services and protection provided on the European capital markets.

1.2 The Securities Act

In the course of the recent revision of the Securities Act originally adopted in 1990, a number of EU Directives have been taken into consideration.[2]

(A) Financial Services

The Securities Act defines the activities which are considered to constitute financial services in Hungary (e.g., agency, commission agency, trading, portfolio management and underwriting, as well as other supplementary activities - securities custody and connecting services, safekeeping of securities, rendering of consultation services concerning the reorganization of the capital structure of corporations, organization of the offering of securities and of the takeover of a company limited by shares [discussed in detail in Part II, below], investment consultancy, provision of development loans for securities trading transactions, keeping of securities accounts and client's accounts, etc.). The terminology of the Securities Act follows EU principles, although the classification of the activities defers slightly from the corresponding EU terms.

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1 Act CXLIV of 1997, which entered in force on June 16, 1998, substantially overhauled the company law regime in Hungary and, as a result, it is often referred to as the "new" Company Act. The prior Company Act was in force from January 1989 to June 15, 1998.

2 Such directives include:

(a) No. 79/279/EGK of the Council on coordination of requirements concerning the authorization of listing of securities on the stock exchange;

(b) No. 80/390/EGK of the Council on coordination of terms - for submission to preliminary authority approval - of the drafting, control and availability of a prospectus to be published for the introduction of securities on the stock exchange;

(c) No. 82/121/EGK of the Council on regular information to be published by companies limited by shares which have their shares listed on the stock exchange;

(c) No. 89/298/EGK of the Council on coordination of terms of the contents, control and publication of the prospectus to be published in the course of the public offering of transferrable (negotiable) securities;

(d) No. 89/592/EGK of the Council on coordination of regulations relating to insider trading;

(e) No. 93/6/EGK of the Council on compliance of investment companies and credit institutions with capital requirements; and

(f) No. 93/22/EGK of the Council on investment services in respect of securities.

(B) Financial Services Providers

With respect to the conduct of financial services providers (befektetési vállakozás as defined in the Securities Act), which may operate only as companies limited by shares and may only issue registered securities, the Securities Act specifies three different categories of providers, classified on the basis of their licenced activities. As a result, financial services may be provided through a stockbroker (e.g., agency and consignee's activities - established with HUF 20 million of initial capital), a securities dealer (e.g., securities trading on own account, agency activities, consignee's activities, commercial activities, and portfolio management - established with HUF 100 million of initial capital), and as a so-called investment company (e.g., a company having the ability to engage in full scale financial activities, including providing underwriting guarantees and the extension of development loans - established with HUF 1 billion, with such capital and any capital increases to be made available solely in cash).

For purposes of becoming a financial services provider, an operation license must be obtained from the State Money and Capital Market Supervision (Állami Pénz és Tőkepiaci Felügyelet - "ÁPTF"). The ÁPTF is a governmental agency authorized to control financial services providers, corporations in the course of issuing marketable (transferrable) securities via both public offerings and private placements, the stock exchange, the central clearing house and the investment securities deposit organization clearing house. It also may issue licences and impose sanctions on market participants if they do not operate in compliance with applicable laws, or if they operate without statutory licences or not in compliance with such licences.

With respect to Hungary's international agreement upon joining the OECD, and subject to its obligations, Hungary enacted an act (Act CXXXII of 1997) on the registration of **branches** of corporations having their corporate seat outside of Hungary. Thus, as of January 1, 1998, branches of foreign financial services provider companies, as well as banks, may be registered in Hungary as a branch of a foreign corporation, provided they comply with the licensing requirements applicable to corporations established in Hungary.

Under the former Hungarian legislative scheme, the separation between financial services and bank services was extremely strict, e.g., banks could not carry out financial services. This strict separation requirement, however, has been relaxed somewhat by virtue of modifications in 1997 to both the Securities Act and the Financial Institutions Act which permit a "break through" leading toward the establishment of **universal banking.** While the limitations on performing activities other than the banking services, on the one hand, and financial services, on the other hand, are still strict, as of January 1, 1999, banks may now obtain a license for the rendering of full scale financial services. The primary condition for such a license is that within the bank, a "Chinese" wall between the banking and investment services departments is properly erected and developed, and that the management of risks, via the Commercial Book (Kereskedési Könyv), is properly set up.

It also should be noted that, for purposes of having a clear ownership structure for financial services providers, the Securities Act prohibits a financial services provider

from having direct ownership or indirect ownership, exceeding a 10% interest, in another financial services provider. Consequently, the owners of the financial services providers may not have an ownership interest in another financial services company in Hungary which exceeds a 10% interest.

(C) Investor Protection

The Securities Act sets forth strict rules with respect to the continuous reporting obligation of issuers of publicly-traded securities.

In the interest of strengthening the controlled market, as opposed to the OTC market, the Securities Act introduced an obligatory introduction requirement where an offering exceeds a value of HUF 200 million.

Privately-held companies limited by shares also have reporting obligations to the ÁPTF, in order to ensure their mandatory compliance with the rules regarding the issuing of securities. It should be noted that the Securities Act and the Company Act allow companies limited by shares which, at any time became publicly-held, to convert into a privately-held company, provided that at least 75% of their shareholders holding an interest representing not more than 1% of 100% of the shares issued by such company, approve the conversion in advance.

The central clearing house (Központi Elszámolóház és Értéktár - "KELER"), apart from its clearing of the stock exchange transaction activities, is responsible, as of 1996, for keeping record of all securities issued or introduced in Hungary, to ensure formal compliance with the rules covering the issuance and recording of securities, particularly with regard to the control of dematerialized securities. Securities in a dematerialized form may be issued in Hungary as of 1997.

In 1993, Hungary - the first among the former Soviet-bloc countries to do so - established an agency (the National Deposit Insurance Fund / Országos Betétbiztosítási Alap) for the securing and insuring of frozen investments in Hungary, up to a certain limit (HUF 1 million).

The Company Act, as of June 16, 1998, amended the Securities Act by introducing - with reference to EU regulations - strict rules regarding takeovers in the case of publicly-held companies. These rules are discussed in detail in Part II, below.

2. INVESTMENT FUNDS

The importance of investment funds has grown tremendously in Hungary, as a result of the development of private pension funds, as well as the increasing attractiveness of such funds to small investors in view of the decreasing rate of return on discount and other state bonds and the decline in bank deposit interest rates.

An investment fund, as defined in Act LXIII of 1991 on Investment Funds (befektetési alapokról szóló tv. - "BAT") (as amended), is a legal entity:

- established through a company engaged in investment fund management activities ("Fund Manager");

- whose capital is raised through a (i) public issue, or (ii) private placement of its investment units (befektetési jegy), and invested into securities (or real property); and

- managed by the Fund Manager on the basis of the general mandate of the owners of the investment units.

According to the BAT, the investment fund may be an open-end or a closed-end fund, depending on the liquidity of the investment units.

An investment fund may only be established and operated by a Fund Manager.

The Fund Manager must be a Hungarian company limited by shares, having an initial share capital of HUF 20 million, and may only issue registered shares. The Fund Manager must have a fund management operation license from the ÁPTF prior to commencing such activities.

The Fund Manager company, in addition to its investment fund management activities, may only carry out voluntary mutual fund or pension fund asset management activities. (Voluntary mutual fund or pension fund asset management activities are considered a financial service in accordance with the Financial Institutions Act , Act XCVI of 1993 on Voluntary Mutual Insurance Funds and Act LXXXII of 1997 on Private Pension and Private Pension Funds, in connection with which the preparation of a mutual fund and pension fund asset management policy and the extension of the ÁPTF license are required).

To become a Fund Manager, an operations license is required, which is also issued by the ÁPTF.

The initial equity capital of an open-end investment fund (a fund having marketable units, as compared to a closed-end fund, which has units with limited transferability) may be raised by public issue or private placement.

Regarding the public issue of investment units, the issuer must employ one or more managers (brokerage house). Prior to the public issue of investment units, a prospectus must be prepared and approved by the ÁPTF. The prospectus must contain the identification of the Fund Manager and the fund depositor, as well as their current audited financial data, and the specification of the management policy (the "Policy") of the fund (including the name of the fund, the particulars of the face value, type of units, the terms of issue and repurchase of the units, the terms of calculation and distribution of the return on the unit, the terms of calculation of the net asset value, the initial capital, the investment principles, rules of information relating to the investors, the terms of termination of the fund, and the risks in connection with the fund's investments).

Where the initial capital of the fund is raised by private placement, potential investors must make an initial declaration pertaining to the subscription of the investment units and must transfer the initial capital into the account of the fund, established with the fund depositor. Prior to the private placement, the Policy of the fund must be prepared and approved by the ÁPTF.

The fund is considered established if the fund is registered with the ÁPTF. The registration has no retroactive effect. The registration of the fund must be initiated by the Fund Manager. The Fund Manager must certify to the ÁPTF that the initial capital of the fund has been made available in the account of the fund.

If the initial capital, which may not be less than HUF 100 million, is raised via private placement, the units must be registered, and they may only be traded among the subscribers of the units for so long as the units are not offered for sale to the public, i.e., the open-end fund is not converted into a public investment fund. The advantage of establishing the fund by public issue is that a new ÁPTF licensing procedure would not be required for the conversion of the fund into a public open-end investment fund.

According to the BAT, the duty of the Fund Manager is to invest the capital of the fund into securities and thereafter trade (directly or through agents) the securities held by the fund in an effort to attain the highest possible return. The investment decisions are made by the Fund Manager with regard to the principles set forth in the BAT and the Policy.

It should be noted that the Fund Manager must employ an investment fund deposit manager ("Deposit Manager") which may only be a bank (or a specialized credit institution) having an investment fund deposit manager's license from the ÁPTF, allowing it to engage in the following activities:

(i) managing the bank account of the investment fund, including the deposit account to be opened in order to raise the initial capital of the fund;

(ii) maintaining custody of the securities owned by the investment fund and carrying out the related technical assistance in connection with trading such securities; and

(iii) carrying out technical duties with respect to the sale and repurchase of the investment units, payment of their return, and the determination of the net asset value of the units.

The capital of the securities investment fund may only be invested in securities where a suitable calculation of their net value is possible. In accordance with the BAT, such securities are the following:

(a) publicly issued securities issued by Hungarian entities (provided that the securities or similar series of securities of the same issuer are traded on the stock exchange, or there is a publicly announced (OTC) securities' price for at least 7 consecutive days prior to the purchase of the relevant security);

(b) publicly issued or traded securities issued by foreign issuers, provided that the foreign exchange authority approved their trading in Hungary (OECD securities are not subject to such approval) and the securities are quoted on foreign stock exchanges; and

(c) compensation vouchers.

The BAT specifies a number of limitations on the investment policy of a securities investment fund, i.e., it is prohibited from investing more than 5% of the capital of the fund into any one particular type of security offered by an issuer, and is prohibited from purchasing securities exceeding 10% of the fund's total capital volume from any one issuer (except for T-bonds and mortgage papers).

For the liquidity of the open-end investment fund, the Fund Manager must keep at least 15% of the total net value of the fund in cash or in a three-month maximum bearer savings deposit account, or in state guaranteed securities immediately convertible into cash.

3. RISK CAPITAL (VENTURE CAPITAL) FUNDS AND COMPANIES

Another new type of investment vehicle in Hungary is the risk capital (venture capital) fund. The objective of such funds is to provide capital to small and medium-sized companies with growth potential, but which lack the necessary working capital.

A risk capital company is a company established for the exclusive purpose of placing venture capital investments pursuant to Act XXXIV of 1998.

Risk capital funds are funds managed by a Fund Manager through the making of venture capital investments.

The minimum capital requirement of such a company and fund is HUF 500 million. Both the company and the Fund Manager (who has no specific minimum initial capital obligations) must be a company limited by shares issuing exclusively registered shares.

The company and the Fund Manager must obtain an operations license for its activities. The fund must be registered with the ÁPTF.

The company and the fund's capital may be raised via public subscription or private placement, provided, however, that the fund may only be a closed-end fund. The term of operation of both the company and the fund may not be less than 6 years.

The company or the fund, at the time of the initial investment in a company and in an entity controlled by such company, may not exceed 15% of the equity of the company or the fund.

Between the 24th month following the issuance of the company's operation license and the registration of the fund until the 48th month, the value of investments of the company or the fund may not decrease below 30 % of the registered capital of the fund or the company, at any time.

Also, during the first six years of operation of the fund or the company, the average value of the investments must be at least 50% of the equity of the company or the fund, and for at least three of those years, it must average at least 70%.

In the case of both investment funds and risk capital funds and companies, there are strict reporting obligations to the ÁPTF, as well as limitations regarding any transfer of the

investment's management and special bankruptcy rules set forth in the applicable regulations, all of which must be respected by the Fund Managers and the company.

PART II

CORPORATE TAKEOVERS IN HUNGARY: HARMONIZATION OF HUNGARIAN LAW WITH THE EUROPEAN UNION PROPOSAL AND DIRECTIVE

In its Proposal and Directive, the European Council established certain criteria for recommended regulations to be implemented by the Member States regarding takeover bids. Such recommendations are justified by:

- the necessity to coordinate certain safeguards in order to make such safeguards equivalent throughout the EU; and
- the necessity to protect the interests of shareholders of companies,

when these companies are subject to a takeover bid or to a change of control and their securities are admitted to trading on a regulated market within the scope of the Directive.

Under Hungarian law, the issue of a takeover is addressed in three different laws:

- Company Act
- Securities Act
- Competition Act

1. PROTECTION OF MINORITY SHAREHOLDERS

EU Under Article 3 of the Directive, minority shareholders shall enjoy protection where a natural person or a legal entity, as a result of an acquisition, holds securities which when added to any existing holdings, gives him or it a specified percentage of voting rights in a company conferring control of that company. The Directive makes recommendations intended to ensure that rules or other mechanisms and arrangements are in force which either oblige this person to (i) make a bid, or (ii) offer other appropriate -- and at least equivalent -- which afford protection to the minority shareholders of that company.

The percentage of voting rights conferring control for the purposes of paragraph 1 and the method of its calculation shall be determined by the law of the Member State where the supervisory authority is located.

HUN *Company Act: In the case of a company limited by shares, whether publicly or privately held, the Company Act differentiates between the acquisition of (i) a "significant interest", defined as controlling more than 25% of the votes, (ii) a "majority interest", defined as controlling more than 50% of the votes, and (iii) a "controlling interest",*

defined as controlling more than 3/4 of the votes. The acquisition of a significant interest, majority interest or controlling interest, together with an indication of the method and the degree of such influencing interest, shall be reported to the competent court of registration for the registered office of the controlled company by the party holding such interest, within a period of thirty days after the establishment thereof and the fact and degree of the acquisition of such interest shall be published in the official Company Gazette.

In the case of an acquisition of a majority or controlling interest in a company limited by shares, whether publicly or privately-held, the minority shareholders of the acquired company holding 5% or more of the votes, among other things, shall be entitled, at any time, to request that a general meeting be convened and shall have the right to request that the board of directors include an item on the agenda. (Ordinarily, such minority shareholders' rights shall apply only to shareholders holding 10% or more of the votes, unless a lesser amount is specified in the company's deed of foundation.)

Interestingly, the Company Act provides additional protections to minority shareholders, including the right to sell their shares to the acquiring entity at market value, where there has been an acquisition of a majority or controlling interest of a privately-held company limited by shares.

Securities Act: The Securities Act contains mandatory provisions for the contemplated acquisition of 33% or more of a publicly-held company limited by shares. In practice, it appears that in the case of publicly-held companies limited by shares, control may be conferred with 33% of the voting rights. However, the Securities Act does not regulate either privately-held companies limited by shares or limited liability companies[3]. Under the provisions of the Securities Act (Section 94 /1), a public purchase offer shall be announced for the direct or indirect acquisition of shares, by way of transfer, amounting to over 33% of the shares of voting rights of a publicly-held company limited by shares.

The public purchase offer shall be with respect to the share package amounting to over 33% of the shares of the company limited by shares, whereby the public purchase offer of the buyer shall be directed to at least another 50% of the shares constituting voting rights. If the company limited by shares has issued convertible bonds, the obligation of the public purchase offer shall apply to such bonds as well.

The public purchase offer shall be made to each shareholder of the company limited by shares and to holders of convertible bonds.

2. SUPERVISORY AUTHORITY

EU According to Article 4 of the Directive, the Member States shall designate the authority which shall supervise all aspects of the bid. The authority competent for supervising the bid shall be that of the Member State in which the offeree company has its registered office, if the securities of the company are admitted to trading on a regulated market in

[3] A limited liability company (korlátolt felelõsségû társaság or Kft.) is the equivalent of the GmbH., LLC, S.p.A., Sarl., etc.

that Member State. Otherwise, the competent authority shall be that of the Member State on whose regulated market the securities of the company were first admitted to trading and are still traded.

Under their duty of professional secrecy, the competent authorities of the Member States shall cooperate, insofar as is necessary for the performance of their duties and for this purpose shall supply each other with any information that may be necessary.

The supervisory authorities shall have all the powers necessary for the exercise of their functions, which shall include the responsibility for ensuring that the parties to a bid comply with the rules made pursuant to the Directive. In addition, Member States can provide that their supervisory authorities may, on the basis of a reasoned decision, grant variances from the rules drawn up in accordance with the Directive, provided that in granting such variances the supervisory authorities shall respect the principles mentioned in Article 5.

3. GENERAL PRINCIPLES

EU According to Article 5 of the Directive, the Member States shall ensure that the rules or other arrangements made pursuant to the Directive respect the following principles:

(a) all holders of securities of an offeree company that are similarly situated are to be treated equally;

(b) the addressees of a bid are to have sufficient time and information to enable them to reach a properly informed decision on the bid;

(c) the board of an offeree company is to act in the interests of the company as a whole;

(d) false markets must not be created in the securities of the offeree company, of the offeror company, or of any other company connected to the bid;

(e) offeree companies must not be hindered in the conduct of their affairs for longer than is reasonable by a bid for their securities.

4. INFORMATION

EU According to Article 6 of the Directive, the offering company shall ensure that the **decision to make a bid is made public** and that the supervisory authority and the board of the **offeree company are informed** of the bid before the offer is made public.

Thus, the offeror shall draw up and make public in good time an **offer document** containing the information necessary to enable the addressees of the bid to reach a properly informed decision on the bid. Before the offer document is made public, the offeror shall communicate it to the supervisory authority.

HUN *Under Section 94/B of the Securities Act, the potential buyer shall:*

(i) notify the Supervisory Commission of the purchase offer and submit a copy of the purchase offer to the Commission; and

(ii) send the purchase offer to the board of directors of the target company.

The bidder and its advisors shall observe and protect the confidentiality of the information disclosed to it in the course of the bidding procedure.

Under Section 94/C of the Securities Act, the Supervisory Commission may ban the acquisition of shares by public offering within 15 days following receipt of notification, if the contents of the public offer fail to comply with legal regulations. Any such banning order shall be forwarded to the board of directors of the target company. However, if the Supervisory Commission remains silent and does not announce its position within 15 days, such silence shall be regarded as acceptance of the notification. The Securities Act also imposes the obligation on the bidder to have the offer published in the designated newspaper for announcements of the target company and in the publication of the stock exchange within 3 days of receipt of the Supervisory Commission's approval or of the expiration of the deadline granted by the Supervisory Commission.

EU The document shall state at least:

(a) the terms of the bid;

(b) the identity of the offeror or, where the offeror is a company, the type, name and registered office of that company;

(c) the securities or class, or classes of securities for which the bid is made;

(d) the consideration offered for each security or class of securities and the basis of the valuation used in determining it, together with the particulars of the manner in which that consideration is to be given;

(e) the maximum and minimum percentages or quantities of securities which the offeror undertakes to acquire;

(f) details of any existing holdings of the offeror in the offeree company;

(g) all conditions to which the offer is subject;

(h) the offeror's intentions with regard to the future business and undertakings of the offeree company, its employees and its management;

(i) the period for acceptance of the bid, which may not be less than four weeks or more than 10 weeks from the date on which the document is made public; and

(j) where the consideration offered by the offeror includes securities, information about those securities.

HUN *Under Section 94/A of the Securities Act, a public purchase offer shall include at least the following:*

(a) name (company) and domicile (registered office) of the potential buyer;

(b) the quantity and serial numbers of the shares held by the potential buyer in the company limited by shares;

(c) the quantity and serial numbers of the shares intended to be acquired by the potential buyer;

(d) the conditions of acceptance of sales offers in excess of the purchase offer, or notice of the rejection of such offers;

(e) if a sales offer remain below the purchase offer, the right of withdrawal from the purchase offer or the conditions of acceptance of the sales offers;

(f) the price offered for the shares (bonds);

(g) the deadline for acceptance of the public purchase offer;

(h) the place and mode of effecting the sales offer; and

(i) the company name and registered office of the participating investment company.

The potential buyer shall be required to publish its business plans regarding the future operations of the company limited by shares, and, if the buyer is an economic organization, to prepare an information package on its previous business activities.

EU It is also required under Article 6 of the Directive that there must be rules in force specifying that the parties to a bid shall provide the supervisory authority at any time on request with all the information in their possession concerning the bid which the supervisory authority considers necessary for the discharge of its functions.

HUN *The Securities Act provides that the stock exchange may establish additional requirements, in its regulations approved by the Supervisory Commission, regarding the acquisition of shares traded on the stock exchange in respect of a public purchase offer.*

5. DISCLOSURE

EU Under Article 7 of the Directive, it is required that the bid be made public in such a manner as to avoid the creation of false markets in the securities of the offeree company or of the offeror.

It is also required that the disclosure of all required information or documents be made in such a manner as to ensure that they are both readily and promptly available to the addressees of the bid.

HUN *By virtue of Section 94/H of the Securities Act, the stock exchange, during the period commencing between the announcement of the public purchase offer and the publication of the announcement of the results of the offer, is empowered to suspend the trading of the securities on the stock exchange.*

The potential buyer is required to publish its offer in both the designated newspaper for announcements of the target company, as well as in the official publication of the stock exchange, within 3 days of (i) receipt of the Supervisory Commission's approval of the offer, or (ii) the expiration of the 15-day deadline during which the Supervisory Commission may ban the offer.

According to Section 94/A (2) and (3) of the Securities Act, the offeror's business plan for the future operations of the target company, together with the information package on the offeror's previous business activities (where required to be furnished), shall be made available by the investment company at the place of the announcement of the sales offer.

6. OBLIGATIONS OF THE BOARD OF THE OFFEREE COMPANY

EU According to Article 8 of the Directives

(a) after receiving the information concerning the bid and until the bid is made public, the **board of the offeree company should abstain from any action which may result in the frustration of the offer**, and notably from the issuing of shares which may result in a lasting impediment to the offeror for obtaining control over the offeree company, unless it has the prior authorization of the general meeting of the shareholders given for this purpose; and

(b) the board of the offeree company shall **draw up and make public a document setting out its opinion on the bid** together with the reasons on which such opinion is based.

HUN *Under Section 94/B (2) of the Securities Act, the board of directors of the target company, prior to the announcement of the purchase offer and upon request of the bidder, shall disclose the information related to the company limited by shares which is necessary to establish the conditions of the purchase offer.*

Under Section 94/D (3) of the Securities Act, the board of directors of the target company, within the deadline available for the acceptance of the public purchase offer, is prohibited from passing any resolution which may interfere with the proceedings, such as increasing the share capital of the target company or acquiring the target company's own shares.

7. RULES APPLICABLE TO THE MANNER IN WHICH BIDS ARE MADE

EU Under Article 9 of the Directive, it is required that at least the following matters be addressed in the appropriate legislation governing the bids:

(a) withdrawal or nullity of the bid

HUN *Pursuant to Section 94/F (1) of the Securities Act, if the statements of acceptance of the shareholders eligible to accept the offer suggest that the number of shares to be transferred shall remain below the quantity of shares specified in the public offer (i) the bidder shall be entitled to withdraw its purchase offer according to the conditions prescribed in the offer, or (ii) if the bidder's right of withdrawal is not precluded or the conditions therefor are not specified, the transfer of shares shall take place in accordance with the purchase offer and with the statements of acceptance.*

In the event number of statements of acceptance received in respect of the transfer of shares is in excess of the quantity specified in the purchase offer and if the purchase offer does not stipulate the conditions for the acceptance of sales offers in excess of the acquisition quantity proposed in the offer, the transfer of shares shall take place in proportion to the face value of the shares owned by the shareholders submitting the statements of acceptance.

EU (b) revision of bids

EU (c) competing bids

HUN *Up until the tenth day of the expiration of the deadline for the acceptance of a public purchase offer, third parties shall also be entitled to make a public purchase offer (counteroffer or competing bid).*

A competing bid may only be published if it offers better terms to the offeree as compared with the initial offer.

An offer shall be regarded as offering better terms if it proposes to pay a price that is at least 5% greater or offers the same price but for a volume that is 5% higher, or if payment is proposed exclusively in monetary instruments.

If a counteroffer is submitted, the first public offer buyer shall be deemed void; the regulations on public purchase offers shall be applied accordingly in connection with the counteroffer.

EU (d) disclosure of the result of bids.

HUN *Under Section 94/G of the Securities Act, the bidder shall notify the Supervisory Commission regarding the results of the public offer within 3 days following the deadline for the acceptance of the public purchase offer. Furthermore, the successful acquisition, or the failure thereof, shall be published in the newspaper designated by the target company for its public announcements and in the official publication of the stock exchange.*

8. MANDATORY BID

EU Under Article 10 of the Directive, where a Member State provides for a mandatory bid as a means to protect the minority shareholders, this bid shall be launched to all shareholders for all or for a substantial part of their holdings at a price which meets the objective of protecting their interests.

HUN *Under Section 94 (3) of the Securities Act, the public purchase offer shall be made to each shareholder of the company limited by shares and to holders of convertible bonds. Furthermore, all shareholders and holders of convertible bonds shall have an equal right and opportunity to decide whether to accept or reject the purchase offer.*

According to Section 94/D (3) of the Securities Act, it is not permissible to discriminate among the shareholders holding shares belonging to the same series of shares when exercising their right of acceptance of the public offer.

EU If the mandatory bid comprises only a portion of the securities of the offeree company and the shareholders offer to sell to the offeror more shares than the partial offer covers, shareholders should be treated equally by means of a pro-rata treatment of their shareholdings.

HUN *Under Section 94/F (2) of the Securities Act, in the event the statements of acceptance which are received regarding the transfer of shares are in excess of the quantity specified in the purchase offer, and if the purchase offer does not specify the terms and conditions for the acceptance of such sale offers in excess of the offered acquisition, the shares shall be purchased in proportion to the face value of the shares held by the shareholders submitting the statements of acceptance.*

ISSUES ARISING IN THE CONTEXT OF THE TAKEOVER RULES OF THE SECURITIES ACT

1. The takeover rules do not distinguish between transfers effected between independent parties and transfers made within a group of shareholders where the ultimate controlling shareholder remains the same regardless of the share transfer (e.g., as in the case of a restructuring, or allocation of investment risks). Accordingly, it appears that the takeover rules must be followed in respect of so called intra-group transfers, where the parent company transfers shares of over 33% in one of its publicly-held subsidiaries to another of its subsidiaries, even where the subsidiary acquiring the shares is wholly owned by the parent company. Significantly, the transfer of shares by a subsidiary to a parent company is exempted from the mandatory takeover bid rules, since the indirect shareholding of the parent company is taken into consideration. It would appear that the better approach to this situation is to allow all well defined intra-group transfers to be exempted from the takeover bid obligation.

2. A public offer has to be made only when the bidder contemplates exceeding the 33% threshold. Once the bidder exceeds the 33% threshold, it may acquire as much additional interest in the target company as may be available, without being obligated to make a further public offer.

3. According to Section 94/H (4) of the Securities Act, if, as a consequence of the public offer, the bidder acquires a controlling interest of over 90% of the voting rights of the shares issued by the target company, such bidder, within 30 days following the publication of the announcement on the successful result of the offer, shall be eligible to purchase the remaining shares for the price corresponding to the prevailing bid price.

   It would appear that the above-mentioned provision of the Securities Act provides for a call option in favor of the bidder, enabling the bidder to acquire the remaining shares issued by the target company at the stated price. However, as the practice has yet to develop with respect to this provision, the Supervisory Commission was recently asked whether such an interpretation was correct and, if so, in what manner shall it be implemented, e.g., what happens if the holder of certain remaining shares refuses to sell. Surprisingly, the Supervisory Commission took the position is that this provision does not constitute a statutory call option in favour of the bidder. As a result, the manner is which this provision is to take effect remains unclear.

   It would appear that the better practice would allow for the exercise of such rights through a call option, as the alternative at this juncture appears to be no regulation at all. That is, where an offer results in the acquisition by the bidder of more than 90% of the shares of the target company and thus full control of such company, the new controlling shareholder may be free, without regulation, to implement a resolution for the purpose of acquiring the remaining shares of the company.

   Whereas the original purpose of this provision may well have been to create a classic call option exercisable by the bidder acquiring in excess of 90% of the target company's shares, it appears that the major stumbling block to the implementation of such an approach involves the case where all or a portion of the remaining minority shareholding of the target companies are held by the Hungarian State through the State Property Agency. The Supervisory Commission, as a matter of principle, cannot impose a mandatory call option requirement vis-a-vis such shares held by the Hungarian State. In any event, it would appear that the courts ultimately must answer the question as to how this provision shall be implemented.

4. Under section 94 (4) of the Securities Act, a professional investment company shall be commissioned by the bidder to execute and implement the takeover bid for a company limited by shares.

For further information on this topic, please contact Dr. András Szecskay at Szecskay - Attorneys at Law by telephone (+36 (1) 472 3000) or by fax (+36 (1) 472 3001) or by e-mail (info@szecskay.com).