

## REGULATION OF FOREIGN COLLECTIVE INVESTMENT SECURITIES IS RELAXED

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Both, Act XCV of 1995 on Foreign Exchange ("Foreign Exchange Act") and Act CXI of 1996 on the Offering of Securities, Investment Services and on the Stock Exchange ("Securities Act") have changed as of July 1, 2000 with respect to the offering in Hungary of foreign collective investment security (units of investment funds) and their acquisition by (Hungarian) residents.

### I. Foreign exchange Regulations

Prior to June 30, 2000 there was only one exception from the general rules laid down in sections 35 (2) e) and 35 (7) e) of the Foreign Exchange Act, namely both private and public offerings in Hungary and introduction on a recognized domestic securities market of collective investment securities issued by foreign investment funds, as well as the acquisition for consideration of such securities by residents from non-residents abroad or in Hungary, or from residents abroad, require the preliminary approval of the Foreign Exchange Authority.

The exception (in case of collective investment securities until July 1, 2000) was that the abovementioned preliminary approval was not required for the acquisition in Hungary by a resident for payment in Hungarian Forints of collective investment securities issued by foreigners, the private placement or public offering of which in Hungary and introduction on a recognized domestic securities market has previously been authorized by the Foreign Exchange Authority. Prior to July 1, 2000 Section 35/A of the Foreign Exchange Act already provided liberalized regulation on the acquisition, without preliminary approval of the Foreign Exchange Authority, of shares and bonds issued in OECD member countries. With respect to other investment instruments issued in OECD member countries the liberalization kept a reporting obligation on the transaction to the Foreign Exchange Authority. Acquisition of collective investment securities, however, has not fallen under the liberalized rules.

In practice, due to monetary policies, prior to July 1, 2000 no approval have been issued by the Authority for the offering in Hungary of foreign collective investment securities or for their acquisition.

The execution decree of the Foreign Exchange Act was amended at the end of 1999, and the Government - based on its authority laid down in section 89 (2) of the Foreign Exchange Act - eased the restrictions of the Foreign Exchange Act as of July 1, 2000, and extended the *appropriate* application of Section 35/A of the Foreign Exchange Act to foreign collective investment securities.

The appropriate application basically means that no authorization is required, however, reporting is necessary of private placement or public offering and the introduction on a recognized domestic securities market, as well as the acquisition by a Hungarian resident in exchange for consideration from a resident abroad, or from a non-resident abroad or in Hungary of collective investment securities issued by non-resident investment funds - both in HUF or in foreign exchange - provided that the following three conditions are fulfilled:

- i) the non-resident investment fund manager of the investment fund is registered in an OECD country;
- ii) at the time of the acquisition of the collective investment security, according to the investment policy set forth in the of the relevant investment units of the investment fund is aimed at investing more than 50% of the value of its assets - minus all the obligations of the fund, the convertible currency and the bank deposits placed in convertible money - into securities falling within the scope of Section 35/A of the Foreign Exchange Act (i.e. more than 50% of the assets are invested in shares and bonds issued by issuers registered in OECD member countries);
- iii) the first series of the issued collective investment securities are offered in an OECD member country.

## **II. Provisions of the Securities Act**

In addition to the governing regulations of the Securities Act with respect to the offering in Hungary of serial securities by non-resident issuers, as of July 1, 2000 the new Section 64/A of the Securities Act provides for the application of certain provisions<sup>1</sup> of Act LXIII of 1991 on Investment Funds mainly with respect to the information and reporting duties of the issuers of investment units also for the case of offering and trading in Hungary of foreign collective investment units. The reason behind this regulation is to impose the same information and reporting requirements on foreign investment funds as is the case for Hungarian investment funds whose activity is regulated by the Investment Funds Act.

By the subsequent introduction of the compliance requirement by foreign investment funds with the Hungarian Act on Investment Funds in practice hinders the trading with foreign investment units in the Hungarian capital market. This policy, however, reflects an interim protection of interest to the benefit of the Hungarian financial and investment services institutions active on the Hungarian capital market until a further phase takes place in the revision of securities trading regulations and liberalization of foreign exchange regulations in the light of the harmonization of Hungarian laws with EU norms (primarily with respect of the requirement of free movement of services).

It may be useful, however, in the course of further development of the regulations, which may be expected due to strong arguments against the current regulations from market participants,

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<sup>1</sup> §9, §11(2)-(4), §§12-13, §23(1), §§24-28, §43(1) b)-h), §44 and §49. The references to the fond manager in §11(3) and §§24-28, shall also mean the resident trader.

to consider that different and less strict “creditors protection” rules apply to the acquisition of foreign investment units by Hungarian institutional investors than to customers.

### **III. Mediating Services of a Trader**

If resident clients wish to purchase foreign collective investment security from non-residents, they may only do so, if they employ the mediating services of a Hungarian trader, unless the securities were offered or introduced on the securities market in Hungary, whether privately or publicly. The trader always has to draw the client's attention to the possible authorization requirements and the reporting obligations towards the Foreign Exchange Authority.

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