This memorandum has been prepared and submitted upon request of Professor Robert G. Eccles with the purpose of assisting on the analysis of the viability of an Annual Board “Statement of Significant Audiences and Materiality”.

This memorandum is not intended to be comprehensive, nor to provide legal advice. It shall be used only to the purpose described above.

Setting the legal landscape

1. Briefly explain the broader legal landscape regarding the obligations that a company has to its stakeholders or with regard to its impact on stakeholders, and in particular whether its primary duty is or is not to shareholders over all other stakeholders.

In Hungary Act V of 2013 on the Civil Code (Civil Code) serves as the main source of companies’ obligations. Company law obligations with regard to stakeholders other than shareholders are relatively limited. Shareholders are in the focus regarding legislation. Please refer to questions 7, 9, 10 11 and 13.

Regulatory Framework

2. To what legal tradition does your jurisdiction belong, i.e. civil/common law, mixed?

Civil law

3. Are corporate/securities laws regulated federally/nationally, provincially or both?

In Hungary the corporate/securities laws are regulated nationally.
4. Who are the government corporate/securities regulators and what are their respective powers (in summary only)?

**Hungarian Parliament**: supreme body of popular representation, adopts acts, such like the Civil Code.

**Hungarian Central Bank**: oversees payment and settlement systems, securities settlement systems, and within this framework shall oversee the operations of the system and the operations of the organization performing the activity of the central counterparty, in order to ensure the sound and efficient functioning of these systems and the uninterrupted completion of cash transactions.

**Financial Security Board**: one of the bodies of the Central Bank, monitors the stability of the financial intermediary system as a whole and of the financial markets

**Hungarian Competition Authority**: protects the freedom and fairness of competition, safeguards the enforcement of competition rules, oversees mergers above a certain threshold

5. **Does the jurisdiction have a stock exchange(s)?**
Yes, the Budapest Stock Exchange (BSE), a private limited company, which is the key institution of the Hungarian financial market.

6. **Do the concepts of „limited liability” and „separate legal personality” exist?**

Both the concept of limited liability and the separate legal personality exist under Hungarian law. The limited liability company (Korlátolt felelősségű társaság or Kft.), the public limited company (Nyílt részvénytársaság or Nyrt.) and the private limited company (Zárt részvénytársaság or Zrt.) are the most common types of the legal entities in Hungary.

Limited liability companies are business associations founded with an initial capital consisting of capital contributions of a predetermined amount, in the case of which the liability of members to the company extends only to the provision of their initial contributions, and to other contributions set out in the
memorandum of association. Unless otherwise provided for in the Civil Code, members shall not bear liability for the company's obligations.

Limited companies (private and public) are business associations founded with a share capital consisting of shares of a pre-determined number and nominal value, where the obligation of shareholders to the limited company extends to the provision of funds covering the nominal value or the accounting par value of shares. Unless otherwise provided for in the Civil Code, shareholders shall not be held liable for the limited company's obligations.

However the most common types of business associations adopt the concept of limited liability the Hungarian Civil Code defines legal entities which may not adopt it, such like the General Partnership (Közkereseti társaság or Kkt.).

According to the Civil Code, a legal person shall have its own name and seat, shall have assets separate from its members and founders, and shall have a management and representative body. By the general rule legal persons shall be liable for their debts with their own assets; members and founders of a legal person shall not be held liable for the legal persons debts. In the event of abuse of limited liability on the part of any member or founder of a legal person, on account of which any outstanding creditors claims remain unsatisfied at the time of the legal persons dissolution without succession, the member or founder in question shall be subject to unlimited liability for such debts.

Moreover we should note that the Hungarian law also knows the “piercing the veil” doctrine. In specific cases, the court leaves the legal personality of the business association out of consideration and in these cases the member of the association shall bear liability for the obligations of the association. For example in the event of abuse of limited liability on the part of any member or founder of a legal person, on account of which any outstanding creditors claims remain unsatisfied at the time of the legal persons dissolution without succession, the member or founder in question shall be subject to unlimited liability for such debts.

7. Did incorporation or listing historically, or does it today, require any recognition by the company or its directors of a duty to society, an
obligation to take account of the company’s social or environmental impacts, or to respect its stakeholders?

Incorporation of a company does not, and to our knowledge has not required such recognition.

8. Do any stock exchanges have a responsible investment index, and is participation voluntary? (See e.g. FTSE4Good, Dow Jones Sustainability Index, the Johannesburg Stock Exchange’s Socially Responsible Investment Index.)

The Budapest Stock Exchange has no responsible investment index.

Directors’ duties

9. To who are directors' duties generally owed?

According to the general rules of the Civil Code applicable to all the legal entities, executive officers shall perform their management functions representing the legal person’s interests. According to the general rules of the Civil Code applicable to business associations, the executive officer shall manage the operations of the business association independently, based on the primacy of the business association’s interests. The executive officer shall manage the operations of the business association under a personal service contract or under a contract of employment, as agreed with the company. The executive officer may not be instructed by the members of the business association and his competence may not be negated by the supreme body. In this capacity, the executive officer shall discharge his duties in due compliance with the relevant legislation, the instrument of constitution and the resolutions of the company’s supreme body. As regards single-member business associations, the sole member may instruct the management, which the executive officer is required to carry out.
10. What are the duties owed by directors — please state briefly. Please indicate if there are express or implied duties to avoid damage to the company’s reputation?

According to the general rules of the Civil Code applicable to all the legal entities:

- the executive officers shall perform their management functions representing the legal person’s interests.
- the executive officer is required to keep the members of the legal person, or the founders in the case of non-membership legal persons, informed concerning the legal person, and to provide access for them to the legal person’s documents, records and registers.
- the executive officer shall manage the operations of the business association independently, based on the primacy of the business associations interest.
- the executive officer shall provide the representation of the legal person.

In case of limited liability companies:

- managing directors shall maintain a register on the members of the company.
- the managing director shall notify the court of registry of the reduction of capital within thirty days thereof, and shall take measures for the disclosure of the capital reduction by way of public notice at least on two occasions. The two disclosures shall be made at least thirty days apart.

In case of limited companies:

- The management board shall prepare a report on the management, the financial situation and the business policy of the company at least once every year for the general meeting, and at least once every three months for the supervisory board, if the limited company has one.
- The management board of a public limited company shall present to the annual general meeting the company governance and management report prepared according to the rules applicable to the actors of the given stock exchange.
In certain cases the management board shall, with simultaneous notice to the supervisory board, call a general meeting within a period of eight days in order to provide for the necessary measures, or initiate a decision-making process without having to hold a meeting.

11. More generally, are directors required or permitted to consider the company's impacts on non-shareholders, including impacts on the individuals and communities affected by the company's operations? Is the answer the same where the impacts occur outside the jurisdiction? Can or must directors consider such impacts by subsidiaries, suppliers and other business partners, whether occurring inside or outside the jurisdiction? (See e.g. s. 172 UK Companies Act 2006, and in particular, ss.(1)?)

Hungarian law does not regulate this subject in details, however paragraph 2 of section 3:112.§ of the Civil Code provides that the executive officer shall manage the operations of the business association in due compliance with the relevant legislation, but the interpretation of this section by the judicial practice does not constitute such requirements. According to the law directors are not prohibited to consider the company's impact on non-shareholders. In addition directors shall comply with the other provisions of the Hungarian law, such as provisions related to consumer protection or competition law.

12. If directors are required or permitted to consider impacts on non-shareholders to what extent do they have discretion in determining how to balance different factors including such impacts? What, additional liabilities, if any, do the board or individual directors assume in exercising such discretion?

Please refer to question 11.

13. What are the legal consequences for failing to fulfil any duties described above; and who may take action to initiate them? What defenses are available? Can these issues given rise to other causes of action or regulatory routes whereby a stakeholder can exert pressure on company with regard to its actions?

*In case of noncompliance regarding providing information:*
If the requesting party considers the refusal of information unjustified, he may request the court of registry to order the legal person to provide access to the information.

Failure to operate the business association based on the primacy of the business association’s interest:
The executive officer shall be held liable for damages caused to the legal person resulting from his management activities in accordance with the provisions on liability for damages for loss caused by non-performance of an obligation.

Failure to notify the court regarding the reduction of capital:
Failure of reduction of the capital.

14. Are there any other directors’ duties which are relevant to the interest of stakeholders?

Please refer to question 10 and 13.

15. For all the above, if these exist in your jurisdiction, does the law provide guidance about the role of supervisory boards in case of two tier board structures? What obligations are owed by senior management who are not board directors? Is this determined by law if no specific contractual provision applies?

The Hungarian Civil Code allows the two-tier (or dual) model characterized by boards with separate supervisory and executive functions. The Civil Code provides detailed provisions related to the establishment, membership, powers, operation and liability of the supervisory board. Furthermore the Civil Code regulates the relation between the supervisory and executive board.

Reporting

16. Are companies required or permitted to disclose the impacts of their operations (including stakeholder impacts) on non-shareholders, as well as any action taken or intended to address those impacts? Is this required as part of financial reporting obligations or pursuant to a separate reporting regime? Please specify for each reporting route whether it is mandatory is voluntary. Please describe any mandatory
reporting requirement, major voluntary initiative or trend towards voluntary reporting with regard to transparency (for example, payments to government or state-owned entities, reports on government orders to undertake surveillance or interception, reports on tax payments etc.)

According to the Accounting Act, the economic entities shall prepare a financial statement on their operation and on their financial position and performance, supported by an accounting system prescribed in the Accounting Act, following the closing of the books pertaining to the financial year. This obligation is mandatory. One of the principal duties of the supreme body of a business association is the approval of the annual account. If the company has a supervisory board, the supreme body of the company may adopt a decision concerning the financial report in possession of the written report of the supervisory board.

Issuers of securities that have been offered to the public must disclose essential details to the public on a regular basis of their financial position and the general course of their business. Issuers shall, at the same time, file that information with the Authority as well and shall ensure that it remains publicly available for at least five years. Issuers shall comply with the requirement of regular disclosure of information in the form of half-yearly report; annual report and interim management report for issuers of publicly offered securities. Issuers must disclose to the public without delay or within the following business day any information that concerns, directly or indirectly, the value or yield of their securities issue, and which may have any bearing on the reputation of the issuer. Issuers shall, at the same time, file that information with the Authority as well. The management board of a public limited company shall present to the annual general meeting the company governance and management report prepared according to the rules applicable to the actors of the given stock exchange.

Further disclosure requirements regulated in the Civil Code: If the legal person decided to terminate the department’s legal personality, such decision shall be made public. The adopted draft terms of transformation shall be made public together with the decision on transformation. In case of publicly-limited company the managing director shall notify the court of registry of the reduction of capital within thirty days thereof, and shall take measures for the disclosure of the capital reduction by way of public notice at
least on two occasions. The two disclosures shall be made at least thirty days apart. In case of public private company the management board shall take measures within thirty days following the date of the resolution on capital reduction for the disclosure of such resolution by way of public notice at least on two occasions. The two disclosures shall be made at least thirty days apart.

17. Do legal reporting obligations extend to such impacts outside the jurisdiction; to the impacts of subsidiaries, suppliers and other business partners, whether occurring inside or outside the jurisdiction?

The information disclosed may include information on subsidiaries or business partners outside the jurisdiction of Hungary or on the effects of such decisions outside of the Hungarian jurisdiction.

18. Who must verify these reports; who can access reports; and what are the legal or regulatory consequences of failing to report or misrepresentation? Is there a regulator tasked with investigating complaints of misreporting?

Generally judicial oversight of legal persons shall in general be carried out by the competent court of registry. Judicial oversight shall not apply to cases that are normally subject to other court or administrative proceedings. The scope of judicial oversight shall not cover the business decisions of legal persons in terms of economic feasibility and efficiency. If the measures taken to restore the legality of operations prove ineffective, the competent court of registry shall declare the legal person terminated.

The statutory auditor appointed by the supreme body shall be responsible for carrying out the audits of accounting documents according to the relevant regulations, and to provide an independent audit report to determine as to whether the annual account of the business association is in conformity with legal requirements, and whether it provides a true and fair view of the company’s assets and liabilities, financial position and profit or loss. The state tax authority revises the compliance with the provisions concerning annual financial report. Publicity of company records shall be ensured by the courts of registry, the company information service, and by way of publication in the Cégközlöny (Company Gazette).
The National Bank of Hungary, acting within its function as supervisory authority of the financial intermediary system oversees the disclosure obligations of public limited companies.

19. What is the external assurance regime for reporting on company's impacts on stakeholders? Please specify any mandatory requirements and also where reporting is voluntary what the current market practice is as regards third party assurance. Please summarize any regulatory guidance on reporting that relates to impacts on non-shareholder stakeholders.

There are no regulations under Hungarian law related to the question.

Stakeholder engagement

20. Are there any restrictions on circulating shareholder proposal which deal with impacts on non-shareholders, including stakeholder impacts?

Under Hungarian law, the shareholders have the power to bring any question or subject and to decide on subjects related to the company, therefore no restrictions exist to such proposals.

21. Are institutional investors, including pension funds, required or permitted to consider such impacts in their investment decision? What is legal duty that pension funds owe with regard to investment decisions in this regard? How does the legal duty of the fund align with term and contractual performance criteria of fund managers- does this facilitate or deter consideration of such impacts?

There is no legal obligation in Hungary regarding this aspect of institutional investors’ decisions, such investors are entitled to consider every aspect and information they believe is relevant.

22. Can non-shareholders address companies' annual general meeting? What is the minimum shareholding required for a shareholder to raise a question at a company’s AGM?

All members of the business association shall have the right to partake in the activities of the supreme body in person or by way of a representative. Unless
the Civil Code contains provisions to the contrary, a member may delegate one representative, however, a representative shall be allowed to represent more than one members. Sessions of the supreme body shall not be public. The company’s executive officers and supervisory board members may attend sessions of the supreme body in an advisory capacity.

There is no minimum shareholding required for a shareholder to raise a question, however certain restrictions are applicable connected to the general meeting. The names of shareholders and proxies wishing to participate in the general meeting of the public limited company shall be entered into the register of shareholders at the latest by the second working day preceding the beginning of the general meeting. Any provision of the articles of association to the contrary shall be null and void.

23. Are there any other laws, policies, codes or guidelines or standards applied on the context of particular contractual relationship (for example project finance) or through adherence to particular sustainability principles (for example the UN Global Compact, the OECD Guidelines for Multinational Enterprises etc.), related to corporate governance that might encourage companies to consider in a structured way their impacts upon and the interest of their wider stakeholders including through a stakeholder engagement process?

The Budapest Stock Exchange has Corporate Governance Recommendations aiming to support the transparency and efficiency of the market and to support the rule of law. The Recommendations are considered to be an addition to relevant Hungarian legislation, primarily for listed, public limited companies registered in Hungary; however these are just Recommendations, and has no binding effect.

The Hungarian Asset Management Inc., based on the OECD Guidelines also has Recommendations to associations owned by the state.

The European Union also has legislation related to the subject of corporate governance (Green Book). The corporate governance framework for listed companies in the European Union is a combination of legislation and ‘soft law’, including recommendations and corporate governance codes.
24. Are there any laws requiring representation of particular stakeholder constituencies (i.e. employees, representatives of affected communities) on company boards?

According to the Hungarian Civil Code, if the annual average number of full-time employees employed by the business association exceeds two hundred, one-third of the supervisory board shall be made up of employee representatives. Where employee representatives are entitled to sit on the supervisory board, the instrument of constitution may preclude employee participation in the supervisory board for a maximum period of five years, subject to the prior consent of the works council. Any clause of the instrument of constitution to the contrary shall be null and void. Employee representatives shall be elected for the first time when the company’s supreme body debates the annual account for the financial year when the annual average number of employees reached two hundred. In a company established by way of succession, employee participation in the supervisory board shall be provided for from the time of registration, if the number of employees employed by the business association exceeds two hundred, and if the conditions for employee participation existed at the predecessor company, or at one of the predecessor companies, if there was more than one.

Employee representatives shall have the same rights and same obligations as all other members of the supervisory board. If the opinion of the employee representatives unanimously differs from the majority standpoint of the supervisory board, the minority opinion of the employees shall be stated at the next meeting of the business association’s supreme body. Employee representatives shall inform the company’s employees concerning the activities of the supervisory board.

25. Are there any laws requiring gender, racial/ethnic, religious or other stakeholder representation, or non-discrimination generally on company boards?

According to the Fundamental Law of Hungary, everyone shall be equal before the law and the state shall promote equal opportunities and social convergence. In 2003 the Parliament adopted the Act CXXV of 2003 on Equal Treatment and Promotion of Equal Opportunities according to which it is
considered a violation of equal treatment if the employer inflicts direct or indirect negative discrimination upon an employee, especially in regard of work conditions, hiring, promotion system, liability of damages, membership or participation in employees’ organizations. Furthermore the state established the Equal Treatment Authority to handle the related issues. Beside these general rules, there are no national regulations related to company boards.

We should note, that the European Union aims to accelerate progress towards a better balance of women and men on boards of companies, while allowing companies sufficient time to make the necessary arrangements. A recent proposal sets a quantitative objective of at least 40% representation for each gender among non-executive directors (supervisory board members in a dual board system) by 2020 (or 2018 for State-owned undertakings).

26. In your jurisdiction is there any legal route whereby a parent company can incur liability with regard to the impacts that one of its subsidiaries has had on stakeholders groups? Are there any serious proposals to impose such responsibility?

According to the Civil Code if any controlled member of the group is undergoing liquidation, the dominant member shall be held liable for any debt the member may have outstanding. The dominant member shall be relieved of liability if able to verify that the controlled member’s insolvency did not arise as a consequence of the group’s common business strategy. No provisions related to stakeholders other than shareholders. Currently we have no information regarding any serious proposals.

27. Are you aware of any incoming law or proposals that are relevant to the issues raised in this questionnaire? If so please descrirbe providing an indication of the anticipated date the legislation will come into force or be adopted.

We are not aware of any related incoming law or proposal other than mentioned in the above questions.