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Security Rights and the European Insolvency Regulation

REPORT for CENTRAL AND EASTERN EUROPE

- Focus on Hungary, Lithuania and Poland -

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I INTRODUCTION

A ABOUT THE PROJECT:

1. This report was produced as part of an international project made up of five partner universities – the University of Leeds (UK); Santiago de Compostela (Spain); Hamburg (Germany); Central European University (Hungary) and Palermo (Italy) – co-funded by the Civil Justice Programme of the European Union (JUST/2013/JCIV/AG/4631**).**

B The aims of the Project

2. The project aimed to critically analyse and evaluate the provisions governing security rights and the avoidance of transactions in the European Insolvency Regulation – Regulation 1346/2000 (*hereinafter: the Regulation or the EU Cross-Border Insolvency Regulation*) and address whether there is scope for reform of the law. Security rights are essentially rights over property intended to secure payment of a debt or obligation.

3. The project was focused in particular on the extent of the protection given to security rights under a select number of legal systems from the region of Central and Eastern Europe (*hereinafter: CEE or the Region*) – though limited to the Member States of the European Union (*hereinafter: EU*). This included also:

(1) identification (whenever possible) of the policy reasons behind protection;

(2) the questions whether, and to what extent, this protection also applies in the context of insolvency proceedings affecting the debtor;

(3) the appropriateness of the protection given to rights under Article 5 of the Insolvency Regulation in light of the Regulation's overriding objectives to facilitate the more effective administration of cross-border insolvency cases in Europe;

(4) the compatibility with Article 5 of particular provisions of national law that may (a) impose temporary stays on the enforcement of security rights during the course of insolvency proceedings or (b) permit the paying off or writing down of debt contrary to the wishes of the secured creditor;

4. The ultimate goal of the project was answering the question ***whether reform of the law relating to security rights and the avoidance of transactions is appropriate and desirable*.**

C The coverage of the report

5. This report adresses security rights and the avoidance of transactions from the perspective of a select number of national legal laws from the region of Central and Eastern Europe (hereinafter: CEE).

6. Hungary is in the focus and is thus the legal system discussed in most detail. In case of the other systems, the main and idiosyncratic features are targeted only. It is to be noted, however, this Report is not a Commentary of national laws. It rather aims only to provide a fairly in-depth insight into the Region's laws but without commenting on each provision. Consequently, consulting local laws is a must whenever the application of these laws comes into the picture.

D The contributors

7. This report was drafted by Professor Tibor Tajti (Thaythy)[1] – consortium member and main investigator for the CEE region – from Central European University, Budapest, relying on national laws as supplemented by the received Project questionnaires from some of the CEE national jurisdictions. The list of those contributors who have submitted a (fully or partially) filled questionnaire is added as Appendix One to this document.

8. A number of interviews have also been concluded as part of the Project. These were relied on primarily as a source of empirical evidence showing the gaps in the laws and their strengths and weaknesses.

9. I especially acknowledge the comments as well as exchanges with Prof. Lina Aleknaite- van der Molen (Kazimieras Simonavičius University, Vilnius & Law Firm Eversheds, Vilnius, Lithuania) and Krzysztof Kaźmierczyk (Law Firm Dentons, Warsaw, Poland). My thankfulness goes also to the 'Notarial Office Mándoki'[2] from Kecskemet, Hungary – in particular to István Mándoki and Gergely Kovács (apprentice) as well as to CEU doctoral students Catalin Grabriel Stănescu (Romania), Virág Ilona Blazsek (Hungary) and Patricia Živković (Croatia).

E Methodology caveats

10. As this Project aimed to canvass not only the positive law (i.e., black-letter law in force) but also to collect information and indicia on the how the targeted laws work in reality – in particular the EU Regulation 1346/2000 on Insolvency Proceedings – in particular the following caveats ought to be highlighted. Needless to say, much more

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[2] Website at: <http://www.notaryoffice.hu/illetekes.html >.

is known about how national secured transactions and insolvency laws work in practice compared to their cross-border kin.

11. On national level the quite frequent amendments or complete revamping of law is that creates lots of uncertainty yet not just in their practical application. Due to incomprehension, inappropriate *travaux preparatoire* and speed of changes, gaps, imperfect drafting language and similar defects plague local laws because of why often it is hard (or impossible) to provide proper answers even to simple questions.

12. Although the number of publicized domestic court cases (or decisions/positions of regulatory bodies) has been growing in all the countries in the Region during the last decade or so, the relatively low number of available publicized cases continues to be an obstacle for the researcher.

13. The inadequacy and problems with access to empirical sources of law is even more intense when we turn to the international scene, more precisely to cross-border insolvency cases and the recast EC Regulation on Insolvency Proceedings (2015/848) (Recast Regulation) or its predecessor Regulation 1346/2000. Here, the number of publicized court cases is even lower in CEE though one should not deny that a handful of such decisions have been reached by the courts of the EU Member States and some of the cases that reached the ECJ stem, indeed, from the Region. What matters is, however, that often on the basis of these one could hardly draw firm conclusions though admittedly some of the cases do prove the emergence of dilemmas known outside the Region as well. Among these the concept of COMI seems to lead the way.[3] Not infrequently the problem is that simply no empirical evidence are available.[4] For these central reasons essentially it is impossible, or at least, difficult to pass a verdict on the quintessential question whether the Recast Regulation or its predecessor works fairly and efficiently in practice as evidence of sufficient quality and quantity is unavailable.

14. Although no empirical studies seem to have been made on such less fathomable factors influencing the efficiency of a law as the intensity of the bankruptcy stigma or incomprehension of such – in the region – relatively novel branches of law as secured transactions and insolvency, these are very much present in the Region. As Professor Bork quite apply put it – even if related to German law – "*[i]t may be tempting to disregard this factor as non-serious, but any earnest attempt to consturct an efficient restructuring law must take it into account until there is a wide-ranging and sustained*

[3] For example, the only book specifically devoted to cross-border insolvencies in Hungary written by Andrea Csőke mentions three COMI-related cases from Hungary. *See* Andrea Csőke, *A határokon átnyúló fizetésképtelenségi eljárások* [Cross-Border Insolvency Proceedings] (HVG-Orac, 2008), at 98-100.

[4] One may point again to the fact that Andrea Csőke in his treatise, given the lack of cases on cross-border insolvency generated in Hungary – was forced to resort to foreign judicial decisions. Out of 37 cases used to explain and illustrate the mechanics of Regulation 1346/2000 only four stemmed from Hungary. Although the book was published in 2008 and some additional cases did emerge in the meantime in Hungary, the general feature has hardly changed.

change in popular mentality."[5] These still meaningfully impact the application of the EU cross-border insolvency regulatory regime. The most important caveat that follows from this is that the lack of court cases and other empirical evidences related to Regulation 1346/2000, the Recast Regulation or domestic insolvency laws should not be taken that these function properly in practice.

15. These caveats should definitively be borne in mind when reading the ensuing Report. Given these determinants, whenever the law is unclear on a point, that will be noted. Likewise, when no clear position could be taken on whether a given provision or law properly works in practice, that will be clearly stated though the empirical evidence is scarce.

16. From the perspective of CEE, however, a common EU insolvency and secured transactions law would be not just desirable but – in particular with respect to the similar paths of reforms and the many commonalities in the context of secured transactiond and insolvency laws – possible and presumably desirable.

[5] *See* Reinhard Bork, Rescuing Companies in England and Germany (Oxford Univ. Press, 2012), section 2.12.

II LIST OF ABBREVIATIONS

CEE	**-**	**Central and Eastern Europe**
COMI	**-**	**Centre of main interest (Regulation 1346/2000 and the Recast Regulation)**
EBRD	**-**	**European Bank for Reconstruction and Development**
EU	**-**	**European Union**
HUF	**-**	**Hungarian Forints (national currency)**
IP	**-**	**Intellectual property**
PMSI	**-**	**Purchase-money security interest**
Recast Regulation	**-**	**the Recast EC Regulation on Insolvency Proceedings (2015/848)**
ROT	**-**	**Retain title (ownership)**
UCC	**-**	**Uniform Commercial Code (United States)**
UK	**-**	**United Kingdom**
US	**-**	**United States**

III ABOUT THE REGION AND ITS LEGAL SYSTEMS

A The Geographic Reach of the Report

17. This Report extends to those of countries of Central and Eastern Europe (hereinafter: CEE or the Region) that have after the fall of the Berlin Wall acceeded to the European Union (hereinafter: EU). Geographically these include (proceeding from North to South):

a/ the Baltic States – to wit, Estonia, Latvia and Lithuania

b/ Poland, the Czech Republic, Slovakia, Hungary and Romania, and

c/ finally the two successor countries of the former-Yugoslavia: Slovenia and Croatia.

18. The limits of this Report, though do not allow for providing equal attention to each of the jurisidictions.

19. The geographic proximity and the shared history of some of these countries often is of relevance for the topics touched upon by this Report. For example, while the presence of Scandinavian banks and thus influence of Scandinavian banking practices has been expressed in the Baltic States, primarily German, Austrian and Italian universal banks dominated the scene in the other countries listed above.

20. Needless to say, being part of the same state for decades meant also that many common elements of the legal super-structure were inherited by the successor countries – i.e., the Czech Republic and Slovakia on one hand and Croatia and Slovenia on the other. For example, the post-Yugoslav countries have no civil codes but property, contract and tort law are in separate statutory enactments. Consequently, while in Hungary and Romania secured transactions law is in the Civil Codes, in Croatia and Slovenia distinct statutes should be looked for to find the applicable law.

21. However, no far reaching conclusions should be drawn purely based on either geographic proximity or (more or less) shared common history with respect to fields of law covered by this Report.

B About the Legal Systems of the Region

22. Primarily for the sake of orientation, two common features of the legal systems of the Region ought to be stressed: *first,* these systems all belong to the civil law legal tradition (family) and, *secondly,* they were all until the 1990s socialist (communist) systems.

23. A few quite practical implications ensue from these for the purposes of this project.

24. **The legal origins:** Notwithstanding that fundamental differences exist among the systems of the Region, the common ancestry remains of importance in some respects up until today. A few examples of relevance for this Project ought to be mentioned.

25. *First* of all, this is reflected on **the sources of law** relied on not just by courts and those applying the law but also by scholars. Similarly to German- but contrary to English law, the civil codes (or their equivalents) are the most important and thus most frequently referred to fountains of law. Although according to conventional wisdom Continental European Civil Codes are supposedly gap-less and answers to any and all disputes could be found in them, often what they contain are no more than general principles and rules rather than concrete answers. This is why of fundamental importance is the increasing importance of case law and the so-called 'unifying positions' of the supreme courts. Needless to say, this will be reflected also on this report as often key decisions close the gaps that arise in respect of new and fast-changing fields of law such as insolvency and securities laws – considered in this Report.

26. Although meaningful changes have occurred in most of the CEE states, what is the concrete rule of law is often times obscure because only a small – though increasing – proportion of decisions gets published.

27. *Secondly,* the kinship is due to the fact that **most of the legal categories, principles and rules – or lack of these – are shared**. Examples could easily found from the realms of branches of law of interest to this Report, like the lack of the concept of 'tracing' known by common law systems, the conceptual unity of real and personal property law, or the accessory nature of in rem securities.[6]

28. *Thirdly,* **the perception of insolvency** – in particular the bankruptcy stigma – is also [unfortunately] a feature widely shared by the systems. In this respect the Region resembles Germany.

29. The same could be said also of the presence – or rather the absence or fledgling nature (at least) – of a business rescue culture. Although the insolvency laws have also been upgraded following western models in the post-1990 period – including introduction of the local (close or remote) version of US Chapter 11 reorganizations though looking at German or French law (typically) as the direct models – one could hardly speak of a major breakthrough in that respect as of yet.

[6] See, e.g., Tibor Tajti, Could Continental Europe Adopt a Uniform Commercial Code Article 9-Type Secured Transactions System? The Effects of the Differing Legal Platforms, Adelaide Law Review, Vol. 35, No. 1, 2014, pp. 149-178.

30. If blue chip corporations are being rescued, then they are bailed out by the government rather than negoations, workouts or other forms of private ordering.

30. The socialist/communist past: In the eyes of communist systems credit and credit security were despised ideological enemies of the system. As a result, during the years of communism the law on credit-securities was in decline to say the least though admittedly the attitude began to change for the better from the end of the 1970s onwards in some countries of the region.

31. Nonetheless, at the time of the fall of the Berlin Wall the law on securities was underdeveloped in the entire region due exactly to the hostility of the former regime. It was not without a reason that EBRD[7] itself was established exactly to help these countries in introduced (or reintroducing) market economy and that exactly the reform of secured transactions laws became EBRD's first priority project.

32. For the purposes of secured transactions law this meant, in particular, the following.

33. The available in rem (proprietary) security devices were essentially limited to possessory pledge and mortgage of immovables. As far as personal securities concerned, especially in the 1980s and related to foreign trade, bank guarantees and letters of credits became as well quite often utilized.

34. The lack of a developed security law was mitigated in certain contexts by contractual penalties (though this was primarily characteristic to the USSR and less in those countries that have in the meantime become Member States of the EU).

35. Primarily in the countries neighboring Germany, some forms of non-registrable security devices (the so-called "*kautelarische Sicherheiten*") have become common in practice. As latent securities, these caused priority problems after the introduction of the registration-based security interests as part of the post-1990 reforms. This was the case, for example, in Hungary and Poland. For Hungarians, it took quite a while to realize that the two systems cannot co-exist: changes ensued only with the 2013 new

[7] The European Bank for Reconstruction and Development (EBRD), seated in London, UK, was established at the beginning of the 1990s to assist CEE countries in their transition towards market economy. Its secured transactions law reform was among the first and began in 1992 and has been ongoing ever since; lately expanding also to the Maghreb countries. The Bank's objective has been "*to encourage counties to modernise their secured transactions laws and it offers assistance at all stages of the reform process [..].*" See Frederique Dahan and John Simpson, Legal Efficiency of Secured Transactions Reform: Bridging the Gap between Economic Analysis and Legal Reasoning, in: Dahan & Simpson, Secured Transactions Reform and Access to Credit (Edward Elgar, 2008), at 122. *See also* D.R.R. Dunnett, the European Bank for Reconstruction and Development: A Legal Survey, Common Market Law Review 28: 571-597 (1991) and Attila Harmathy, the EBRD Model Law and the Hungarian Law, in: Norton & Andenas, Emerging Financial Markets and Secured Transactions (Kluwer, London, UK, 1998), 197-209.

Civil Code. In Poland, for example, these security devices continue to play a meaningful role.

36. Needless to say, as time passes by, the socialist past is of of less and less relevance; especially in the systems that have reformed their security and insolvency laws.

C Reformed and Unreformed Legal Systems of the Region

37. While some cross-fertilization is detectable in case of some of the Region's countries, the rule is rather that each of the jurisdictions has had a distinct path of reforms (if any) and post-1990 evolution of secured transactions and insolvency law. As a result, the systems' solutions differ often quite meaningfully. For example, the operation of the newly introduced registers for security interests on movables have been entrusted to different bodies and have been subjected to differing rules – what might be an obstacle should the EU decide to link these in the future.[8]

38. Irrespective of the distinctions and without the pretension of completeness, some commonalities can be identified as well. These include the following.

39. Most of the systems that have embarked on reforming their secured transactions law have been *influenced by Anglo-Saxon laws*, typically English and/or US law (i.e., UCC Article 9). As a rule, the source of inspirations and support was critical in that respect. For example, while the Hungarian reforms were primarily influenced by the documents and instruments produced by EBRD, Article 9 of UCC[9] was the primary model in Romania.

40. There have been *waves of reforms*[10] each trying to make headways though backpedalling was not unheard of either; perhaps best illustrated by the new

[8] *See, e.g.,* Tibor Tajti, *Post-1990 Secured Transactions Law Reforms in Central and Eastern Europe – Focus on Hungary and its Neighbors, in:* Bulletin of the Chamber of Public Notaries of County Szeged (Hungary), vol. II, Nos. 3-4 (27 October 2013), at 18 e*t seq.* Available also via < http://www.SSRN.com > and Researchgate.

[9] *See,* e.g.,Victor Padurari & Andreea Simona Burtoiu, Taking Stock of Romanian Secured Transactions after 15 years of Reform: A mapping of past, present and future milestones, in: Frederique Dahan (ed.), Research Handbook on Secured Financing in Commercial Transactions (Elgar, 2015), Nuria de la Peña & Heywood W. Fleisig, Romania: Law on Security Interests in Personal Property and Commentaries, 29 Review of Central and East European Law 2004 No.2, 133-217, at 404; at 164; Ileana M. Smeureanu & Florentin Giurgea, Enforcement of Contracts in Romania, in: Stefan Messmann & Tibor Tajti (eds.), the Case Law of Central and Eastern Europe – Enforcement of Contracts (European University Press, Bochum, Germany 2009), at 723-731. The Romanian reform was assisted also by the United States Agency for International Development (USAID), which is a federal agency that assists low income countries, among others, in achieving self-sustaining socioeconomic development. In Romania, this included the reform of secured transactions law.

[10] In case of Hungary, for example, the security law-related parts of the Civil Code were significantly revamped three times in the post-1990 period: in 1996, in 2000 and in 2013. While the 1996 amendments introduced the new regime, the ones from 2000 were limited essentially only to its

Hungarian (2013) and Romanian (2013) Civil Codes. While the Hungarians have decided to discard the nominated 'property encumbering charges' (i.e., the local equivalents of the English floating charges), the Romanians have cut back the self-help related rules originally introduced in 1999 directly based on UCC Article 9.

41. It is also common and of importance from the perspective of secured transactions and insolvency laws that none of the systems has introduced a comprehensive secured transactions law resting on the unitary concept of security interests. This applies especially to what is referred to in this Report as quasi-securities, which remains a concept largely foreign to CEE. As a result, various more advanced forms of leasing or factoring contracts remain legal categories strictly distinct from security agreements. Though the walls have already begun falling. For example, under the new 2013 Hungarian Civil Code financial leasing and factoring contracts – while remaining distinct legal categories – have become subject to registration in the registry of security rights on movables introduced as part of the reforms.

42. Consequently, one has to be always cautious to explore which particular types of transactions, or asset-types, have remained outside the reach of the newly introduced regime. Besides ships, aircraft, fixtures and some forms of intellectual property, this applies especially to receivables, transactions containing retained title (ownership), investment property and 'global' security extending to all (or substantially all) present and future assets of a debtor.

43. Put simply, compared not just to UCC Article 9, and the Australian or Canadian provincial' PPSAs, but also to Book IX of the Draft Common Frame of Reference (DCFR), these systems still tend to be fragmented.

D The Synopsis of the Secured Transactions and Insolvency Laws of Selected CEE Jurisdictions

E HUNGARY – THE JURISDICTION IN THE FOCUS:

44. The fall of the Berlin Wall meant a new beginning for both secured transactions and insolvency law in Hungary.[11] This applies especially to the former, which was reformed with the assistence of the EBRD resulting in a system adopting common law concepts.

upgrading and refinements. However, the 2013 new Civil Code not only expanded the system, but also made important advancements towards the Anglo-Saxon models and Book IX of the DCFR. For example, notice-filing was introduced and financial leasing contracts were subjected to registration. On the Hungarian developments *see* Tajti *Id.* On the 1996 and 2000 amendments of the Civil Code s*ee* the Chapter on Hungary in Tibor Tajti, *Comparative Secured Transactions Law* (Akadémiai könyvkiadó, Budapest, 2002).

[11] *See, for example,* the Chapter on Hungary in: Tibor Tajti, Comparative Secured Transactions Law (Akadémiai könyvkiadó, Budapest, 2002).

45. Secured transactions law is enshrined in the Civil Code and thus the three significant amendments of the Code each meant another reform: while the first in 1996 introduced the new system[12] and the second of [year] 2000 aimed only at refining the law and filling the gaps,[13] the one from 2013 – introduced by a brand new Civil Code[14] – brought about a major advancement towards the unitary model of UCC Article 9. In particular, financial leasing, factoring and retained title (ownership) was made subject to registration in the charge register, as well as a version of notice filing was introduced, together with a milder version of self-help repossession. Needles to say, the ensuing Report will state the law as per the 2013 Civil Code and will rely on the related Commentaries.[15] In early 2016 no major changes have been announced by the government. However, upon the insistence of the National Organization of Public Notaries and the Banking Association requests for meaningful changes to the 2013 systems have been raised, including to discarding the notice-filing system and re-introducing instead the old document authentication system as well as the reintroduction of independent security rights.

46. Insolvency law was also amended significantly in the post-1990 period though following the developments in Germany and other civil law countries of Europe rather than Anglo-Saxon systems. The core of the system is Law No. XLIX of year 1991 on Insolvency and Liquidation Proceedings (as amended) [hereinafter: the Insolvency Act];[16] amended fundamentally five times in the meantime.[17] Besides these, the

[12] The 26th Law of Year 1996 on Amendment of Certain Provisions of the Hungarian Republic's Civil Code (hereinafter: the 1st Reform Act).
[13] The 137th Law of Year 2000 on the Amendment of the Law Regulating Charges (hereinafter: the 2nd Reform Act).
[14] The 5th Law of Year 2013 on the Civil Code *(„A Polgári Törvénykönyvről szóló 2013. évi V. törvény*"). The law on security rights is in Book V on Property Law, Part III on Limited Proprietary Rights, Title VII on Security Rights, §§ 5:86 through 5:144. All the references to various paragraphs – unless otherwise specifically stated – will be related to this part of the 2013 Civil Code.
[15] Professor Lajos Vékás was at the helm of the team drafting the new Civil Code just as he was the editor of one of the Commentaries published by the Complex Publishing House in 2013. The full reference is: Lajos Vékás (ed.), *A polgári törvénykönyv magyarázatokkal* [Commentary of the Civil Code] (Complex – Wolters Kluwer, Budapest 2013) – hereinafter: Complex Commentary.
The other Civil Code Commentary is: György Welmann, *Az új Ptk. magyarázata* (HVGORAC, Budapest, 2013) – hereinafter: HVG Commentary.
[16] "*1991. évi XLIV. törvény a csődeljárásról és a felszámolási eljárásról."*
[17] The literature speaks of these, due to their in-depth nature, as 'Novellas' to differentiate them from other minor amendments. Notwithstanding the indeterminacy inherent to such classification, we will follow the established standards in this respect. In light of that, the list of the most important amendments in the post-1992 (passage of the Insolvency Act) – called Novellas – are the following.
The first novella of 1993 (Act No. LXXXI of year 1993) discarded the concept of mandatory insolvencies and the automatic conversion of reorganizations to liquidation. This was possible because after the 1992 passage of the Insolvency Act the national-level wave of insolvencies – caused by circular indebtedness amounting to more thousand billion Hungarian Forints – subsided. **The second novella of 1997** (Act XXVII of year 1997), among others, increased the entitlements of the creditors' committee and of the equity holders. **The third novella of 2004** (Act XXVII of year 2004) were needed because Hungary joined the EU on the 1st of May 2004 and therefore in effect they implemented EU law. **The fourth novella of 2006** (Act IV of year 2006), on the one hand, reconciled the Insolvency Act with the

insolvency regime was affected (at different levels) also by the three waves of Secured Transactions reforms mentioned earlier and also by various amending statutes though some of these addressed only minor matters.[18]

47. Already these few lines could show how dynamic (if not hectic) the post-1990 development of Hungarian insolvency has been. The hastily passed amendments and the big number of changes could not but cause problems in the application of the law. As the transition of the economy from planned to market economy in this period was completed and essentially similar challenges exist in Hungary as in other Central European countries today, nothing forestalls passing of a new consolidated act enriched by the latest-generation experiences of developed legal systems. Unfortunately, no such initiative seems to be on the agenda of the law-makers save the issue of the bankruptcy of individuals – triggered by the systemic-risk generated by the widely used Swiss Franc denominated (primarily) housing mortgage loans. Although the subject of political and some scholarly debates during the last few years, no legislative action has been taken so far.

F SYNOPSIS OF THE LAWS OF LITHUANIA AND POLAND

48. The developments in the ensuing jurisdictions cannot be scrutinized with the level of detail employed toward Hungary, the main jurisdiction herein. Still, as it will be seen, the review of developments and some of the key – sometimes idiosyncratic – solutions demonstrate that the upgrading (modernization) of secured transactions law ranked high on the agenda of each of these countries; principally by borrowing from Anglo-Saxon systems. The introduction and gradual refinement of insolvency laws has also been an important agenda of law reforms in the region.

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then passed Company Act and also refined the law on some key building blocks of the system (e.g., new criteria for insolvency, costs of insolvency). Finally, **the fifth novella of 2009** (Act LI of year 2009) again significantly revamped insolvency law, among others, by 1/ introducing the institution of immediate 'moratorium', 2/ subjecting the filing of creditor claims to payment of fees, 3/ increasing the powers of the administrator (trustee), and 4/ introducing once again the rule that unsuccessful reorganizations automatically convert to liquidation proceedings. *See* László Juhász, *A Magyar Fizetésképtelenségi Jog Kézikönyve* (Handbook of the Hungarian Insolvency Law – Publisher: Novotni Kiadó, 2014) (hereinafter: the Hungarian Insolvency Handbook), at 38-40.

[18] Insolvency law was affected by the following acts: 1/ Act LXI of year 2007 (e.g., faster publication in the Bulleting of Companies, ranking of security interests); 2/ Act LXXVIII of year 2007 (aimed to deal with circular indebtedness but touched upon some insolvency issues); 3/ Act CXV on Sole Proprietors (made registered sole proprietorships subject to insolvency law); 4/ Act XCVI of year 2009 (introduced the duty of the debtor's CEO to file a tax return); 5/ Act CXLIX (changes to the system of criminal records and the related duties of the insolvency administrator); 6/ Act CL of year 2009 (changes in the laws regulating the financial system); 7/ Act CXV of year 2011 introduced the category of the 'enterprise of national importance' ("*nemzetgazdaságilag kiemelt gazdálkodó szervezet*"); 8/ Act CXCVII of year 2011; 9/ Act CIV of 2012; 10/ Act CCLII of year 2013 (making the insolvency system compatible with the new 2013 Civil Code); and finally 11/ Act XV of year 2014 (modification of the rules on administrators). *See* Hungarian Insolvency Handbook, at 39-40.

49. Lithuania was no exception in the CEE: it modernized its mortgage and secured transactions law in the post-1990 period as well.

50. As part of that it established a centralized registry (the Central Mortgage Office) in 1998 , a budget-funded institution monitored by the Ministry of Justice, the work of which by now has become electronic.[19] The Office maintains a separate registry for some specific types of contracts of relevance to this Report as well, in particular credit and financial leasing contracts.[20]

51. The main source of mortgage law is the Civil Code[21] of 2000 (as last amended in April 2015) and its Book IV, Chapter XI (the last amendment is from 2011, which came into force on the 1 July 2012); parallel with which the earlier *lex specialis* Law on Pledge over Movable Assets was quashed.[22] One should mention also *Resolution No 1246 of 18 October 2001 of the Government of the Republic of Lithuania on the Approval of the Regulations of the Mortgage Register of the Republic of Lithuania (Official Gazette, No. 90-3173, 2001),* as amended by Resolution No. 571 of the Government of Lithuania of 23 May 2012.[23] Both, the number of registrations (relative to the size of the country)[24] and the overall achievements are meaningful though dilemmas persist.[25]

52. In many respects, Lithuania faced the same problems as the other CEE reform-oriented countries caused by the civil law heritage. Perhaps the most important was the reluctance to give way to the realization that the analogous application of rules applicable to real property (immovables) mortgage law is ill-suited to use of movables,

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[19] The English language pages of the Central Mortgage Office are at < https://www.hipotekosistaiga.lt/index.php?881562680 >; last visited on 5 January 2015.

[20] The English language pages of the Central Mortgage Office for these specific contracts are at < https://www.hipotekosistaiga.lt/index.php?1927692242 >; last visited on 5 January 2015. Note that the register of real property and cadastre is maintained by another body, by the State Enterprise Centre of Registers at < http://www.registrucentras.lt/index_en.php# >.

[21] The Civil Code of 18 July 2000, Law No. VIII-1864 (as amended). The English text of the Civil Code of the Republic of Lithuania is available at < http://www3.lrs.lt/pls/inter3/dokpaieska.showdoc_l?p_id=245495 >; last visited on 5 January 2015.

[22] Although not in force since 1 January 2003, one has to make mention of it because some sources mistakenly mention it as a key act on security rights. The act was part of the reform package and was enacted on 10 June 1997 as Law No. VIII-250.

[23] The English text of the amended Resolution is available at < http://www3.lrs.lt/pls/inter3/dokpaieska.showdoc_e?p_id=450749&p_query=&p_tr2=2#>; last visited on 5 January 2015.

[24] For statistics (though in Lithuanian language) on registrations by type of asset see < https://www.hipotekosistaiga.lt/Statistika/HR_statistika%28projektas2014%29.htm >; last visited on 5 January 2015.

[25] For two cases dealing with security rights (with excerpts from the judgments themselves in English) *see* Lina Aleknaite, *Enforcement of Contracts in Lithuania, in:* Stefan Messmann & Tibor Tajti (eds.), *the Case Law of Central and Eastern Europe – Enforcement of Contracts* (Eur. University Press, Bochum-Germany, 2009), at 370 – 384. Hereinafter this chapter will be referred to as Aleknaite.

rights and claims as collateral.[26] Although, undoubtedly the 2011 revamping of the relevant Civil Code provisions was a major advance – for example by recognizing a form of enterprise mortgage (shifting stock as collateral) and a limited form of out-of-court enforcement – the drafters have nonetheless failed to go as far as introduction of notice-filing (in contrast with Hungary). Under the present law, notaries still are entrusted with meaningful roles in the constitution and registration of security rights.[27]

53. The new Lithuanian insolvency law – for businesses – is encapsulated in the Enterprise Insolvency Act of 2001;[28] one could say a typical Continental European insolvency law.

54. A public register exists with data on business enterprise insolvencies; basic insolvency-related information is searchable via Internet.[29] For advanced research, the searcher has to be pre-authorised and payment of modest fee is also required. The Ministry of Economy through its Department of Enterprise Insolvency Management publishes furthermore not only data related to business insolvencies[30] but also – since 2013 – on individual bankruptcies.[31]

55. Restructuring of enterprises is regulated separately by the Law on Enterprise Restructuring, which was also passed in 2001.[32] The Law on Enterprise Restructuring governs the whole restructuring procedure, starting with initiation of restructuring case in court, through appointment of restructuring administrator, drawing up of restructuring plan, to approval and satisfaction of creditor claims. The law sets a rather

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[26] *See* Article 4.199 of the Lithuanian Civil Code that impose the duty to apply the rules on immovables mortgages *mutatis mutandis* to "pledging" movables, rights and claims.

[27] For a rundown of the main changes introduced by the 2011 amendments to the Civil Code *see* the brief commentary publicized by the Klaipeda City First Notary's Office from 2013 available at < http://www.notarius.lt/?en=1390464172> or through the Oxford Secured Transactions Reform Project led by Prof. Gullifer at < http://securedtransactionslawreformproject.org/lithuania/>; both last visited on 5 January 2015.

[28] The Act was passed on 20 March 2001 as act No IX-216 (last amended on 18 November 2014, amendments came into force on 1 January 2015 – XII-1309). The English text of the act is available at <http://www.doingbusiness.org/law-library/lithuania >; last visited on 5 January 2015. For an overview of the Act *see* the material compiled by the Department of Enterprise Bankruptcy Management operating under the Ministry of Economy at <http://www.bankrotodep.lt/Index.php >.

[29] *See* the Centre of Registers at < http://www.jar.lt. >; last visited on 5 January 2015.

[30] *See* the data for year 2013 at <http://www.bankrotodep.lt/Doc/2013_00_en.pdf>; last visited on 5 January 2015.

[31] *See, e.g.,* for year 2014 at <http://www.bankrotodep.lt/Doc/FABIS_G.pdf >; last visited on 5 January 2015.

[32] The Act was passed on 20 March 2001 as act No IX-218 (last amended on 16 December 2014, amendments will come into force on 1 August 2015 – XII-1456). The English text of the act is available at <http://www3.lrs.lt/pls/inter3/dokpaieska.showdoc_l?p_id=418092>; last visited on 5 January 2015. The list of amendments is available at < http://www3.lrs.lt/pls/inter3/dokpaieska.rezult_l?p_nr=&p_nuo=&p_iki=&p_org=&p_drus=1&p_kalb_id=1&p_title=%E1moni%F8%20restrukt%FBrizavimo&p_text=&p_pub=&p_met=&p_lnr=&p_denr=&p_es=0&p_tid=&p_tkid=&p_t=0&p_tr1=2&p_tr2=2&p_gal=&p_rus=>; last visited on 5 January 2015.

straight framework according to which the restructuring procedure should be conducted. Ultimately, the procedure is creditor driven, as a restructuring plan can only be adopted upon creditor approval. The restructuring procedure is not available to companies that the court finds to be insolvent.

56. **A methodological caveat: the analysis of Lithuanian law in this Report is based on the last available English versions of the Civil Code and the Insolvency Act. This means in case of the Civil Code the version valid until 1 October 2011**[33] **and in case of the Insolvency Act the version valid until 3 July 2012.**[34]

H POLAND:

57. Poland, similarly to Hungary, embarked on the modernization of its secured transactions law right after the fall of the Berlin Wall. It passed a special statute named the *Registered Pledge and Register of Pledges Act* in 1996,[35] which extends to movables, rights and claims.

58. Three key determinants played a role in shaping the act. *First,* the drafters have tried to exploit the pre-WW II experiences with a number of laws allowing creation of registered pledges on some specific types of assets (timber, motor vehicles, equipment and agricultural registered pledge).[36] *Secondly,* the act has tried to incorporate into the Polish system a number of modern developments (e.g., by exploiting the EBRD's secured transactions law-related work). *Last but not least,* the act yielded also to local expectations. As Spanogle aptly put it: "*Polish professors*

[33] For the list of articles affected by subsequent amendments *see* <http://www3.lrs.lt/pls/inter3/dokpaieska.rezult_l?p_nr=&p_nuo=&p_iki=&p_org=&p_drus=1&p_kalb_id=1&p_title=civilinio%20kodekso&p_text=&p_pub=&p_met=&p_lnr=&p_denr=&p_es=0&p_tid=&p_tkid=&p_t=0&p_tr1=1&p_tr2=2&p_gal=&p_rus=1> or <http://goo.gl/2hlkgb>; last visited on 27 April 2015.

[34] For the list of articles affected by subsequent amendments *see* <http://www3.lrs.lt/pls/inter3/dokpaieska.rezult_l?p_nr=&p_nuo=&p_iki=&p_org=&p_drus=1&p_kalb_id=1&p_title=%E1moni%F8%20bankroto&p_text=&p_pub=&p_met=&p_lnr=&p_denr=&p_es=0&p_tid=&p_tkid=&p_t=0&p_tr1=2&p_tr2=2&p_gal=&p_rus=1> or <http://goo.gl/hTdNmb>; last visited on 7 January 2015.

[35] The English translation of the original text of the act is available at < http://www.ebrd.com/downloads/legal/core/polandls.pdf >; last visited on 12 February 2016. Note that the act has been amended in the meantime. The Act will be hereinafter referred to as the Registered Pledge Act.

[36] For short references to these laws *see* Krzysztof Kaźmierczyk & Filip Kijowski, *Chapter on Poland, in:* Stefan Messmann & Tibor Tajti (eds.), *the Case Law of Central and Eastern Europe – Enforcement of Contracts* (European University Press, Bochum-Germany, 2009), note 162, page 607. This chapter and book will be referred to hereinafter as 'Kaźmierczyk-Kijowski.'

Keeping the strange designation combining pledge (inherently possessory) with registration (means of perfection of non-possessory securities) seems to stem from the pre-WW II period as well. Though as Kaźmierczyk-Kijowski noted a better alternative was also known yet was eventually abandoned. *Id.*

drafted the statute in their own style, using their own principles and civil law values."[37] For example, the quasi-securities known as 'security transfers' ("*przewlaszczenie na zabezpieczenie*") and 'security assignments' ("*przelew na zabezpieczenie*") – not subject to registration with a public registry – were tolerated by the system, what could not but negatively affect predictability on the market.[38] Leasing remains separate from the system of registered pledges as well up until today.

59. The Polish lawmakers – similarly to the Hungarians – have also struggled with the dictates imposed by the conceptual unity of security law; a characteristic of all Continental European civil law systems. As the drafters did not dare to part with the concept, this had important consequences, affecting the efficiency of the new system.

60. The greatest novelty of the reforms, the "registered pledge" was looked upon as the weaker brother of the mortgage of immovables and consequently whenever possible (no matter how ill-suited) the same principles and solutions were applied also to the latter.[39]

61. This, most importantly, made introduction of notice-filing impossible and rather entrusted courts and judges with maintaining the system. This made the system very cumbersome and slow because judges were entrusted with "constitution" of registered pledges and running of the registry.[40] The system is not faultless yet it is fair to say that it works relatively smoothly and that the system of registered pledges has, indeed, contributed meaningfully to increasing access to finance.

62. Polish security law, however, is not enshrined only in the Registered Pledge Act. The rules on possessory pledges (called also as civil code pledge or ordinary pledge in Polish), some rules on "pledging" of rights and claims as well as some generally applicable rules on securities are in the Civil Code.[41] The relationship of the Civil Code

[37] *See* John A. Spanogle, *Secured Transactions Law in Eastern Europe: the Polish Experience as an Example,* 31 T. Jefferson L. Rev. 279 (2009), at 279.

[38] *See* the case II CK 409/2003 decided by the Supreme Court (excerpts from the decision and comments in English) in Kaźmierczyk-Kijowski at 625-630.

[39] Article 1.2. of the Registered Pledge Act proclaims that the provisions of the Civil Code apply to registered pledges if something is not regulated explicitly by the Act. Note, however, that mortgage law is regulated by the Act on Land and Mortgage Register and on Mortgages. Only the general rules applicable to all proprietary rights come into the picture. These include, in particular, rules on creation of proprietary rights (Article 245), rules on transfers of proprietary rights (Article 246), rules on expiry of proprietary rights (Articles 247 through 248), rules on changes to proprietary rights (Article 248) and priority rules (Article 249 through 250).

[40] As per Article 36.2. the register of 'registered pledges' is kept by district (commercial) courts. Although as per Article 40.3. the court may reject an entry only if that would evidently violate the law, actually the judge must go into the merits as well as its mandate is to " *[verify] only the form and content of the application and the documents on whose basis the entry is to be made and only within the scope of the data to be entered*." *See also* John A. Spanogle, *Secured Transactions Law in Eastern Europe: the Polish Experience as an Example,* 31 T. Jefferson L. Rev. 279 (2009), at 288.

[41] The Civil Code was originally enacted on the 23 April 1964 [hereinafter: Polish Civil Code] but has been in the meantime amended many times. For the general rules on securities *see* Articles 244 through

and the Registered Pledge Act is that of the *lex generalis* versus the *lex specialis.* In other words, for matters not regulated in the Registered Pledge Act one must consult the Civil Code. Furthermore, separate acts cover mortgages on immovables[42] and financial collateral.[43]

63. As far as insolvency law is concerned, laws from 1934 were revived with the fall of socialism in Poland. These were soon proved to be inadequate for modern times yet a brand new law – the Insolvency and Rehabilitation Act[44] – was enacted only in 2003 (hereinafter: the 2003 Insolvency Act). The Act seems to have been modelled primarily after German law.

64. The desire to promote rescue of business was proclaimed as one of the primary functions of the Act[45] but this desire has not been fulfilled appropriately. This realization led to the 2015 Restructuring Act (passed in May 2015), which stepped into force on the 1st of January 2016.[46] As the Statement of Reasons attached to the bill put it, the primary purpose is to boost restructuring instead of liquidations that so far has been the predominant aim of insolvency prcedures. A *lex specialis* was opted for – instead of only amending the 2003 Act – to deal with the all-pervasive bankruptcy stigma. Although pre-II WW law was also considered, the main source of inspiration was US Chapter 11 reorganization proceedings. The Act also proposes to enhance the position of creditors and establish a Central Insolvency and Restructuring Register.[47]

The 2015 Restructuring Law introduced four types of restructuring proceedings: 1/ pre-packaged arrangements ("*postępowanie o zatwierdzenie układu*"); 2/ accelerated arrangement proceedings ("*przyspieszone postępowanie układowe*"), 3/ arrangement proceedings ("*postępowanie układowe*"); and 4/ rehabilitation proceedings ("*postępowanie sanacyjne*").

65. **A methodological caveat:** as in case of Lithuania, the ensuing analysis of Polish law this Report relied on the last available English versions of the Civil Code and other cited acts. Here, however, the central act – the Registered Pledge Act – underwent

251, on possessory pledges Articles 306 through 326, and for "pledging" of rights s*ee* Articles 327 through 335.

[42] *See* Act of 6 July 1982 on Land and Mortgage Registers and on Mortgage (as amended) [hereinafter: the Polish Mortgage Act].

[43] *See* Act of 2 April 2004 on Certain Financial Collaterals (as amended).

[44] Note that due to the changes introduced by the 2015 Restructuring Act, the restructuring-related provisions in the 2003 Act have been deleted. Consequently, the designation of the Act has been reduced to *Insolvency Act.*

[45] *See* Article 2 of the Polish Insolvency Act.

[46] The Restructuring Law of 15 May 2015, published in Journal of Laws 2015, item 978.

[47] As per the new Act, it is envisaged that the new Registry will commence its operations on the 1 February 2018.

only technical changes only in the mean-time[48] and thus the publicly available English version could have been worked with. As far as insolvency law is concerned, the entry into force of the mentioned *lex specialis* Restructuring Act and the Consolidated Insolvency Act (containing 268 changes) on the 1st of January 2016, were the main, obviously fundamental, developments.[49] Statistical data on insolvency proceedings is regularly published by the Ministry of Justice as part of the report on the operation of general courts.[50]

I A LOOK AT SELECTED OTHER CEE REFORM JURISDICTIONS

CROATIA

66. The Balkan wars delayed the passage of the reform of secured transactions law in Croatia yet it became a reality in 2006 before the country's accession to the EU. The *Law on the Registry of Court and Public-Notary Security Interests on Movables and Rights*[51] was quite innovative and a trend-setter. It introduced an electronic public

[48] In 2015 there have been 3 amendments to the 2009 version on which the latest translation was based. First, on 28.07.2015 Article 42(4a) was added a technical amendment concerning release of public entities from costs of registration proceedings. Second, on 18.11.2015 Article 42(4a) was again amended only specify the conditions for the release of public entities from payment of registration fees. Finally, the new Restructuring Law also brought a technical amendment to Article 4(1)(3).

[49] The English translations of the relevant Polish acts are the following. **A. Private and commercial law**: 1/ the Act on Registered Pledges - translation based on text published in Journal of laws 2009 No 215 item 1663, three technical amendments since then; 2/ the Civil Code - translation based on text published in Journal of laws 2014 item 121, published on 23.01.2014, nine amendments since then; 3/ Code of civil procedure - translation based on text published in Journal of laws 2014 item 616, published on 01.07.2014, twenty seven amendments since then, and finally 5/ The Act on Land and Mortgage Registers and on Mortgages - translation based on text published in Journal of laws 2013 item 941, published 2013.12.01, three amendments since then.

B. Insolvency law: 1/ The Insolvency Act - translation based on text published in Journal of laws 2013 item 613, published 2013.06.12, eight amendments since then. 2/ from the Insolvency Act distinct brand new Restructuring Law (enacted on 15 May 2015). It ought to be noted that the new Restructuring Law has significantly amended the earlier insolvency act as well mainly by transposing the reorganization-related law to the new Act.

The website of the Polish Parliament listing the amendments (in Polish) are: 1/ for Civil Code: < http://isap.sejm.gov.pl/RelatedServlet?id=WDU19640160093+2000%2412%2409&type=12&isNew=true >; 2/ for the Code of Civil Procedure: < http://isap.sejm.gov.pl/RelatedServlet?id=WDU19640430296+2015%2401%2410&type=12&isNew=true >; 3/ for the Insolvency Act < http://isap.sejm.gov.pl/RelatedServlet?id=WDU20030600535+2014%2412%2431&type=12&isNew=true >; 4/ for the Registered Pledge Act: < http://isap.sejm.gov.pl/RelatedServlet?id=WDU19961490703+2010%2401%2418&type=12&isNew=true >; and 5/ for the Mortgage Act < http://isap.sejm.gov.pl/RelatedServlet?id=WDU20130000941+2013%2412%2401&type=12&isNew=true >.

[50] Statistical report in insolvency and rehabilitation matters for the year 2014, available at the web page of the Ministry of Justice < http://isws.ms.gov.pl/Data/Files/_public/isws/jednoroczne/2014/spr_zbior_2014/ms-s20un_2014.pdf. >

[51] The Croatian language text of the act is available at <http://www.zakon.hr/z/276/Zakon-o-Upisniku-sudskih>; last visited on 7 January 2015.The floating security is regulated by Article 38(1) of the Act. *See also* Tibor Tajti, *Post-1990 Secured Transactions Law Reforms in Central and Eastern Europe –*

register and a version of floating (global or enterprise) security.[52] It made subject to registration[53] not only securities on movables – including the floating security – but also retained title and even negative pledge clauses.

SLOVAKIA

67. Slovakia, similarly to Hungary, primarily relied on EBRD's work on secured transactions law. The common law-inspired security law was introduced via amendment to the Civil Code in 2002.[54] Similarly to Hungary, the running of the brand new centralized and computerized register of security interests was entrusted to public notaries.[55]

ROMANIA

68. Romania is special because the secured transaction law reforms were here introduced with assistance from the US. This was clearly reflected on the act Law No. 99/1999 on Security Interests in Movable Property that was closer to UCC Article 9 than any of the other CEE systems.[56] This included, not only the creation of a new registry system, but also the introduction even of self-help repossesion. The subjection of leasing contracts (at least with respect to some classes of assets) to public notice was another such US-inspired revolutionary innovation, not really followed elsewhere in CEE. The drafters of the new Civil Code of 2011 have, however, backpedalled and made the security law more typical to Continental Europe; in particular as far as self-help repossession is concerned.[57]

Focus on Hungary and its Neighbours, Bulletin of the Chamber of Public Notaries of County Szeged (Hungary), vol. II, No. 3, pp. 14-21 and No. 4 pp. 18-26, available also at < http://www.SSRN.com > and < http://www.researchgate.net >.

[52] *See also* Patricia Živković, *Floating Security Interest – Comparative Analysis of US, English and Croatian Approaches,* conference paper (Bratislava, 2013) available electronically at < http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2243590 >; last visited on 7 Jan. 2015.

[53] The register of security interests on movables and shares is maintained by FINA – the Financial Organization – that provides other services as well. Website is at < http://www.fina.hr/Default.aspx?sec=976 >; last visited on 7 Jan. 2015.

[54] Articles 151a through 151md of the Civil Code contain the new law.

[55] The register of pledges – with English, German, French and Hungarian pages (besides Slovak) – is available at < http://www.notar.sk/en/MainPage/Centralnotaryregisterofdeeds.aspx >; last visited on 7 Jan. 2015.

[56] *See* Ileana M. Smeureanu & Florentin Giurgea, *Enforcement of Contracts in Romania, in:* Stefan Messmann & Tibor Tajti (eds.), the Case Law of Central and Eastern Europe – Enforcement of Contracts (European University Press, Bochum – Germany, 2009), at 726 *et seq.*

[57] On self-help in Romania *see also* Klaudia Fabián, Alexandra Horváthová, Catalin Gabriel Stănescu, *Is Self-Help Repossession Possible in Central Europe,* 4 Duke J. of Eurasian Law 83, available at as well at < http://www.SSRN.com >.

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IV SECURITY RIGHTS COMPARED

Question 1: In general terms, to what extent is it possible in your legal system to create security rights (rights in rem) over assets?

Hungary:

69. The spectrum of security devices known to Hungarian law could be subdivided into the following: proprietary (in rem), personal (in personam) security devices as well as other creditors' position enhancing devices.

70. While this Report will focus exclusively on in rem security devices, it ought to be added that some of the devices belonging to the third group have quasi-in rem effects (like subordination or comfort letters) or are source of receivables that may be used as collateral (e.g., letter of credit). It ought to be added that the law on suretyships and guarantees (as paradigm in personam security devices) was upgraded by the 2013 Civil Code as well;[58] a development that together with the three times revamped secured transactions system is the best proof of the increased importance security devices in toto have received since the fall of the Berlin Wall.

71. Turning to security rights (i.e., in rem securities), Hungary has managed to upgrade its system from the conservative and minimalist one inherited from socialism to a credit and security-friendly one due to the common law-inspired reforms launched in 1996. Notwithstanding the fluctuations, data properly evidence a meaningful growth.

72. Given that the new 2013 Civil Code integrated the earlier widely exploited – and prohibited one specific category of – secured transactions, a brief look at the earlier law is needed. Before 2013 four main groups of in rem security rights were widely exploited: 1/ real property (immovables)[59] mortgages, 2/ security interests on movables, rights and claims, 3/ the so-called fiduciary securities ("*fiduciáris hitelbiztosítékok*")[60] as well as 4/ three specific devices that had their own isolated life: to wit, sales contracts with retained-ownership (clauses), financial leasing and

[58] Suretyship and guarantee contracts (as in personam security devices) are regulated by Book VI: Obligations, Part Three: Individual (Nominated) Contracts, Title XXI of the Hungarian Civil Code.
[59] For the purposes of this Report, it will be presumed that the common law category of 'real property' is equal (or substantially equal) with the civil law concept of 'immovables.' The two terms will thus used interchangeably.
[60] The three main forms utilized in practice were: 1/ transfer of ownership (on an immovable), 2/ assignment (transfer) of a claim and 3/ granting of an option to purchase (right of first refusal) an asset (typically an immovable, like a flat) – in each case as a security for a debt. The two main problems with these were that, on one hand, they gave considerably more entitlements to the creditor than what would be legally justified and, on the other hand, these contravened the prohibition of strict foreclosure (*lex commissoria*). As the Complex Comments say, through these devices "*the creditors ... acquired ownership as most complete forms of proprietary rights, or - based on their purchase options - could acquire it based on a unilateral declaration*." *See* Complex Commentary at 574.

factoring. As it may be concluded, leaving out any of these categories when assessing the economic importance of in rem securities would distort the overall picture. At any event, the exploitation of each of these reached unprecedented levels in the post-1996 period.

73. Contrary to the law on real property (immovables) mortgages that underwent modest yet meaningful changes (especially with respect to computerization of the registry), the law on securities on movables, rights and claims was the centre of the three waves of reforms. The fiduciary securities were the products either of legal innovation or were transplanted financing patterns from western legal systems.

74. Until the 2013 new Civil Code, the legal system looked *only* on the real property mortgage and the security devices on movables, rights and claims as being true in rem securities. As a result, they were placed in the same part of the Civil Code, both were subjected to registration and the same principles applied to them unless something else followed from their different nature.

75. As opposed to that, fiduciary securities were looked upon as different kinds of legal institutions and the related provisions were in different parts of the Code. In fact, their exact legal status remained the subject of polemies and courts had no common position on whether to recognize them: some recognized them, others have either declared them null and void or have subjected them to registration and mortgage law.[61] Most importantly, however, they escaped registration and the strict priority regime applicable to genuine security rights. More because of the many abuses rather than because of their unclear legal status, the 2013 Civil Code prohibited them.[62] Foreseeably this change will not negatively affect the market given that the other avenues remain widely open.

76.The other novelty of the 2013 Code is the imposition of registration (filing) in the charge register requirements in respect of financial leasing,[63] factoring[64] and sales contracts with retained ownership (title)[65] clauses. This was introduced to prevent the bypassing of the registration system applicable to movables, rights and claims. In other words, the new system has come close to the unitary concept of security interests.[66]

[61] *See* Complex Commentary at 574.
[62] *See* Book VI on Obligations § 6:99 of the Hungarian Civil Code.
[63] *See* Book VI on Obligations, Part III on Specific Contracts, Title XX on Credit and Account-Contracts, Chapter LIX on Financial Leasing Contracts, §6:410 of the Hungarian Civil Code.
[64] *See* Book VI on Obligations, Part III on Specific Contracts, Title XX on Credit and Account-Contracts, Chapter LVIII on Factoring Contracts, §6:406 of the Hungarian Civil Code.
[65] *See* Book VI on Obligations, Part III on Specific Contracts, Title XIV on Contracts for Transfer of Ownership, Chapter XXXII on the General Rules on Sales contracts, §6:216(3) of the Hungarian Civil Code.
[66] *See* Complex Comments at 417.

Notwithstanding the increased transaction costs, this novelty is not expected to constrain the market either.

77. The 2013 Civil Code, "*departs from the fact that credit is one of the vital elements of market economies and that the availability of efficient security devices is a crucial precondition of that.*"[67] In line with such a policy goal, the Code declares that any asset can serve as collateral[68] – including after-acquired property[69] – that the collateral may be identified by description only and that the security right will extend to the parts, products, and other proceeds of the collateral.[70]

78. A pro-credit novelty is the introduction of the notice-filing system instead of the earlier document-registration model that relied on the same principles that have remained valid for real property mortgages. With this measure the transaction costs of the constitution of security rights have been decreased radically though the transition to the new system and ignorance of the notice filing requirement may generate unexpected risks and costs.

LITHUANIA:

79. As a result of the post-1990 efforts aimed at modernization of Lithuanian secured transactions law (i.e., in rem rights on movables, rights and claims), now it is possible to grant securities in a wide range of circumstances.

80. The caveat is that the terminology & system of the Civil Code – that contains security law – and the available English translations might blur the picture. This applies especially to Book IV, Chapter XII that contains possessory "pledges" and known possessory securities. What makes Lithuania interesting is that besides the floating charge (security) covering the whole enterprise (Chapter XI), [71] a narrower version of floating security is also in existence. The latter one extends only to some specific property like equipment or goods for sale (inventory) and is regulated distinct from the previous one in Chapter XII.

POLAND:

81. A wide range of securities – both in rem and in personam – may be granted in Poland today, too. As far as in rem securities are concerned this is to a great extent due to the reform efforts of the post-1990 transitory period. This includes mortgage of immovables, possessory as well as "registered pledges" (i.e., non-possessory

[67] *See* Complex Comments at 416.
[68] *See* § 5:101 of the Hungarian Civil Code. The restrictions stem from the nature of the asset used as collateral. Thus, possessory pledge can be constituted only on movables (Id. §5:101(2)). Furthermore, security right cannot be constituted on an asset in condominium unless the ownership share of the debtor cannot be determined or in case of divisible obligations (Id. § 5:101(3)).
[69] *See* § 5:89(4) of the Hungarian Civil Code.
[70] *See* §5:103(1)(2) of the Hungarian Civil Code.
[71] *See* Article 4.202 of the Lithuanian Civil Code.

securities) basically on almost all kinds of assets from specific movables, through various rights and claims (receivables) to the encumbering of an enterprise as a whole[72] or a particular part of it.

Question 2: Is it possible to create security rights over all assets of the debtor?

Hungary:

82. The Code proclaims as a general principle that "*Any property [type] may be used as a collateral*."[73] Based on the definition of 'property' ("*vagyontárgy*") this may include assets (things), rights and claims. [74] Further, a security interest may be created on more[75] and shifting assets.[76] as well as it automatically extends to the components, accessories, and proceeds of the assets used as collateral.[77]

83. This general rule must be, however, qualified. *First,* some methods of "pledging" are limited to certain specific types of assets. For example, the objects of possessory pledge can be only movables and other tangible assets (e.g., certificated securities). Moreover, the sui generis possession and control-based security device – the security-bailment interest ("*óvadék*") – can be instituted solely on some specific types of assets, to wit cash, investment property and payment accounts ("*fizetési számla*").[78]

84. *Secondly,* certain assets may not be freely transferable – and thus their use as collateral would also be restricted – due to some specific legal restrictions. Insolvency law lists a number of such assets from national parks, historic buildings, public waters, land separated for restitution, former church estates separated for restitution, trade union membership fees, unpaid taxes that have been deducted from an employee's wages before the opening of insolvency proceedings but have not been transferred to the tax authorities.[79]

85. *Thirdly,* the Code foresees that as a general rule pledging parts of assets or of claims is not possible without pledging also the whole "unit." Pledging separable parts of movables or portions of claim are nonetheless allowed through explicit exceptions: the part (e.g., appartment) owned by the debtor in a condominium, the portion of a

[72] *See* Article 7.2(3) of the Registered Pledge Act, which refers to "*a set of movable things or rights that constitutes an economic unit, even if the constituent elements change*". Note that the definition of "enterprise" here is different from the one in article 55[1] of the Civil Code, which is a general private law definition of enterprise.
[73] *See* § 5:101(1) of the Hungarian Civil Code.
[74] *See* § 8:1(1)(5) (Book Eight, Concluding Provisions – Part One, Interpretative Provisions).
[75] *See* § 5:105 of the Hungarian Civil Code.
[76] *See* § 5:104 of the Hungarian Civil Code.
[77] *See* § 5:103 of the Hungarian Civil Code.
[78] *See* on security-bailment point two under Question 6 below.
[79] *See* § 4(3) of the Insolvency Act [assets that are not part of the insolvency estate].

right held by more persons (e.g., a patent held by the debtor and another person) and the specific part of a divisible claim.[80]

86. That Hungarian law is based on the all-asset policy is highlighted by the few limitations known by the Insolvency Act. These do not prohibit the use of some specific assets as collateral but rather only grant the right of first refusal (option to purchase) to some specific persons. These assets are, on the one hand, national parks and national monuments, in case of which the right of first refusal belongs to the competent governmental bodies.[81] On the other hand, if part of the debtor's estate is a residential real property that has already been paid fully or partially by a private individual yet the ownership had not been transferred before the opening of the liquidation proceedings, such buyer will have the right of first refusal.[82]

LITHUANIA:

87. A form of floating security – introduced by an explicit provision in the Civil Code – makes that possible.[83] The available English language literature speaks of these though as 'company mortgages.'[84] As this device was introduced only recently, the exacts of this security device are not yet fully known. Security interests can be created over a wide array of assets including movables and property rights such as receivables. Floating security over stock was introduced back in 2001.

88. The newest amendments of the Civil Code expanded the provision to permit the use of any property complex constituted of movables as collateral, including stock, equipment and claims as specifically stated by the Civil Code. In addition to that, the amendments of 2011 have introduced a possibility to create floating charge over the whole property of an enterprise.

POLAND:

89. As indicated under Question 1, today one can use as collateral all types of transferrable assets. This includes also fixtures (i.e., movables affixed inseparably to immovables),[85] commingled, processed or mixed assets[86] or enterprises (or organized parts thereof). Limitations exist though like the prohibition of the constitution of registered pledges on assets that may be encumbered by either mortgages or maritime mortgages (which are subject thus to a distinct regime).[87]

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[80] *See* § 5:101(3) of the Hungarian Insolvency Act.
[81] *See* § 49/C(1) of the Hungarian Insolvency Act.
[82] *See* § 49/C(2) of the Hungarian Insolvency Act.
[83] *See* Lithuanian Civil Code Article 4.202.
[84] *See* the brief commentary publicized by the Klaipeda City First Notary's Office from 2013 available at < http://www.notarius.lt/?en=1390464172> or through the Oxford Secured Transactions Reform Project led by Prof. Gullifer at < http://securedtransactionslawreformproject.org/lithuania/>; both last visited on 5 January 2015.
[85] *See* Article 9 of the Registered Pledge Act.
[86] *See* Article 8 of the Registered Pledge Act.
[87] *See* Article 7.1. of the Registered Pledge Act.

Question 3: Is it possible to create security rights over assets not yet owned by the debtor at the time of the creation of the security interest?

Hungary:

90. As per the new 2013 Civil Code (as it used to be the case since the first secured transactions law reform of 1996), it is possible to create security rights over after-acquired property.[88] This includes also assets that are not yet owned by the debtor at the time of the creation of the security interest.

LITHUANIA:

91. Yes, as it is explicitly provided by the Civil Code.[89]

POLAND:

92. Yes, also explicitly provided for by the Registered Pledge Act.[90]

Question 4: Is it possible to create security rights over assets that are not yet in existence at the time of the execution of the security agreement?

Hungary:

93. As per the new 2013 Civil Code (as it used to be the case since the first secured transactions law reform of 1996), it is possible to create security rights over assets that are not yet in existence at the time of the execution of the security agreement.[91]

LITHUANIA:

94. The Civil Code states in article 4.201(1) that any existing or future movable or other property right can be used as collateral.

POLAND:

95. The Registered Pledge Act has no explicit provision on this issue. However, it has rules that make that possible in certain circumstances. These are: 1/ automatic extension of security interests to products and proceeds of collateral;[92] 2/ possibility to "pledge" after-acquired property (but existing at the time of execution of the pledge

[88] This is proclaimed explicitly by the second sentence of § 5:89(4): "*The collateral must be indicated by type and quantity or by using another appropriate method the identification*. *Such assets may also be identified that are not yet in existence or with which the debtor cannot dispose of [at the time of the identification].* "
[89] *See* Article 4.201(1) of the Lithuanian Civil Code.
[90] *See* Article 7.3 of the Registered Pledge Act.
[91] *See Id* – the text of the quoted § 5:89(4) of the Hungarian Civil Code.
[92] *See* Article 10.1 of the Registered Pledge Act.

agreement);[93] and 3/ possibility to encumber an enterprise in its totality (or a particular part of it).[94]

Question 5: Is it possible to have a "global security agreement" i.e., covering all assets of the debtor?

HUNGARY:

96. A version of floating charge – allowing for encumbrance of all present and future assets of a debtor – was first introduced in Hungary with the first secured transactions law reforms in 1996 under the designation of '*property encumbering charge*' ("*vagyont terhelő zálogjog*").

97. The drafters relied on the EBRD Secured Transactions Model Law[95] rather than on any one single national model. The provision in the Model Law was, however, similar to the English floating charge and not the US floating lien. As a consequence, the exact priority point of the property encumbering charge was initially controversial as it was not clear whether the time of the registration in the charge registry (maintained by public notaries) or rather the time of the 'crystallization' was the crucial time.

98. This was remedied first by a Supreme court decision[96] and finally by an explicit provision in the 2000 amendments of the secured transactions provisions of the Civil Code.[97] According to this the secured creditor was entitled "*to exercise its enforcement right on the priority position he acquired on the date of the registration of the property encumbering charge*."[98]

99. Notwithstanding such teething problems, the property encumbering charge has become a quite popular security device in Hungary within a relatively short period of time. Exactly because of this it came as a complete surprise that the drafters of the brand new Civil Code discarded the concept.[99] More precisely, the property encumbering charge – as a distinct nominated security device – was "only" given up. According to the drafters, however, nothing prevents the parties from encumbering

[93] *See* Article 7.3 of the Registered Pledge Act.
[94] *See* Article 7.2(3) of the Registered Pledge Act.
[95] EBRD, *Model Law on Secured Transactions* (1994), available electronically at < http://www.ebrd.com/downloads/research/guides/secured.pdf>; last visited on 7 January 2015.
[96] *See* BH 120/2006.
[97] *See* § 266(3) of the pre-2013 (old) Civil Code valid from 1st of September 2001.
[98] *See* §266(3) of the pre-2013 (old) Hungarian Civil Code. *See also* the article of István Mándoki, *A vagyont terhelő zálogjog ranghelye* [the Priority Position of the Property Encumbering Charge], in the Bulletin of Public Notaries, Nos. 7-8 (July-August, 2006), pp. 14 – 17 [in Hungarian]. Mándoki was the public notary acting in the case that was published eventually as case No. BH 120/2006.
[99] *See* Complex Commentary, at 417.

various categories of assets separately,[100] from indicating the collateral by mere description[101] (except immovables and catalogued movables and rights)[102] and from giving the debtor unfettered dominion over the collateral.[103]

100. From the 15th of March 2014 (the date of the coming into force of the new 2013 Civil Code) Hungary has no floating security with which one could encumber all the present and future assets of a debtor through a single contract and single entry in the register of charges. As per the advice of the drafters of the Code, however, the same results could be achieved through a series of secured transactions each encumbering different asset classes and thus at the price of a string of separate registrations.[104] Nothing seems to prevent though the inclusion of all encumbrances in the same security agreement. Given that this is a brand new development, dilemmas exist.

101. At any event, one may legitimately question whether a proper comparison has been made, on the one hand, between the transaction costs accompanying the old painfully introduced but eventually satisfactorily functioning system relying on a nominated single security device and, on the other hand, of the transaction costs that the new multiple-securities-based regime has introduced. As far as the latter is concerned, not only the costs corollary to the creation of multiple security devices should be reckoned with, but also the costs the risks of possible conflicts among these separate security devices.

LITHUANIA:

102. Yes. Two versions of global security are known by the Civil Code. The first is narrower and allows for pledging of shifting and complex asset classes including raw materials, equipment, receivables (etc.)[105] The other, the all-encompassing, makes

[100] *See* § 5:101(1) of the Hungarian Civil Code which proclaims that any asset (type) may be used as collateral. *See also* Complex Commentary at 417.
[101] *See* § 5:93(4) of the Hungarian Civil Code that foresees that entries into the charge register – contrary to the register of mortgages on immovables – may be made either by individualizing the asset used as collateral or by describing it. *See also* § 5:102 on collateral indicated by description. According to this section, if the collateral is indicated by description ("*körülírás*"), the collateral will be composed of those assets over which the debtor will have a right of disposal at any point in time. It is presumed that the right of disposal for the purposes of this paragraph will survive if the collateral was not disposed of through regular commercial channels or if it was not disposed of in good faith and without consideration.
[102] *See* § 5:93(3) of the Hungarian Civil Code according to which in case of mortgages on immovables and charges on catalogued chattel, the collateral must be individualized ("*egyedileg meghatározott zálogtárgy*").
[103] *See* Complex Commentary at. 417. *See also* § 5:108(1) of the Hungarian Civil Code, which contains the basic rule according to which the debtor has the right to possess the collateral, to use and exploit it in the ordinary course of business and to keep it in good condition. *See* § 5:108(2) off the Code applicable to security agreements where the collateral is identified by description. In this case, "*the debtor is entitled to process, transform, assemble, commingle or dispose of the collateral in the ordinary course of business*."
[104] *See* Complex Commentary, at 417.
[105] *See* Article 4.202 of the Lithuanian Civil Code.

creation of a security interest over the whole company possible.[106] The fact that global security is possible is also apparent from the regulation on the running of the Mortgage Registry that requires filing a digital copy of the company's inventory for registration.[107]

POLAND:

103. Yes. A full and a limited version of global security have been introduced by the Registered Pledge Act. As the Act provides, a security right can be established on *"a set of movable things or rights that constitutes an economic unit, even if the constituent elements change."*[108] The assets that cannot be encumbered with registered pledge (i.e. immovable property and other rights that may be subject to a mortgage or vessels that may be subject to a maritime mortgage) will be however excluded from the enterprise pledge and should be encumbered separately under the security interests applicable to them (i.e. mortgage or maritime mortgage).

Question 6: In general terms, what are the formalities in your legal system for the creation of a security interest over assets?

HUNGARY:

104. The system imposes two groups of formalities for the creation of securities over assets: 1/ requirements that apply to all security agreements (general requirements); and 2/ collateral-specific ones (i.e., rules that differ depending on the asset class used as collateral). Here we will focus on the first category only and under the next question on the asset-specific rules.

105. Preliminary qualification ought to be added though. Namely, the Code's language and structure may be misleading as in fact it imposes specific preconditions for the validity of security interests but does not speak of them as such. Three points need to be stressed here.

106. *First,* the Comments to the Civil Code speaks of **the written form** of security agreements as the *only* formal requirement imposed by the system.[109] While under the pre-2013 Civil Code the validity of security agreements on movables, rights and claims was subject to a special form – the public document ("*közokirat*") form[110] – this heightened formal requirement was discarded by the new 2013 Code and now a

[106] *See* Article 4.177 of the Lithuanian Civil Code.
[107] *See* section 27 of the Resolution No. 571 amending Regulation 1246 on the Approval of the Regulations of the Mortgage Register of the Republic of Lithuania.
[108] *See* Article 7.2(3) of the Registered Pledge Act.
[109] *See* Complex Commentary, at 428.
[110] This requirement was imposed by § 262(2) of the old (1959) Civil Code. The public document requirement – something similar to a deed made by a public notary – was, interestingly and quite illogically, imposed only on security interests on movables, rights and claims but not on mortgages of immovables or security interests on special categories of movables for which specific registries have been in existence (ships, aircraft, some IP forms). *See* Complex Commentary at 428.

simple written form of security agreements would suffice. The main reason for the simplification was that the public document requirement imposed significant transaction costs on the parties to security agreements, which deterred exploitation of the new secured transactions system.[111] The only exception (or rather alternative of written form) recognized is the possibility of the issuance of a recognized form of investment property, negotiable paper or documents of title[112] in lieu of a written security agreement. This option is available, however, only as a substitute of possessory pledge.[113]

107. *Secondly,* the Code imposes additional duties on the debtor, which are nothing more than "mere" obligations yet are spoken of linked to the security agreement. These in some foreign systems are looked upon, either as perfection forms, or integral parts of perfection; because of this they should be mentioned here. For example, in case of using receivables as collateral, it speaks of '***the duty of the debtor'*** to, either **notify** the obligor (account debtor) on the security agreement in writing, or to issue a declaration on that to the secured creditor[114] – in lieu of speaking of it as a precondition for the creation of security interests.[115]

108. The difference between the two notification methods is that while in the first case the obligor is informed about the pledging before default and in the latter case later at the option of the secured creditor but typically on default. Note, however, that in case of claims (receivables) in addition to the duty (obligation) to notify the account debtor, registration with the register of security interests on movables, rights and claims is also a must.[116] Likewise, in case of possessory security (pledge), it imposes the duty (obligation) on the debtor **to transfer possession** or control ("*hatalmat*") over the collateral.[117]

109. *Thirdly,* even though the drafters of the reformed Hungarian secured transactions law have relied on Anglo-Saxon laws and – especially the 2013 version of the Civil Code – on UCC Article 9, the dualistic concepts of attachment and perfection have not

[111] *See* Complex Commentary, at 428.
[112] Note that for Hungarian law the category of 'securities' is broader than, for example, in US law because it encompasses also negotiable instruments and documents of title as well; though the new Civil Code does not list the recognized securities by name. *See* § Book VI on Obligations, Part Five on securities. The drafters of the provision in question, for example, departed from the case of pawn receipts, which are routinely used by Hungarian pawn-shops and are in particular favored because the name and other personal data of the debtors are not recorded (what would be the case if contracts would be made instead of the issuance of pawn receipts). *See* Complex Comments at 428-29.
[113] *See* § 5:89(6) of the Hungarian Civil Code. Such security (negotiable instrument) should entitle its holder to request the transfer of the collateral within the therein specified time and up to the sum specified in the security (negotiable instrument).
[114] *See* § 5:89(c) of the Hungarian Civil Code.
[115] To readers from common law systems this may be puzzling. However, it should be borne in mind that as a civil law country, Hungary has never known 'equity' as a distinct legal category and thus the tandem of equitable and legal security interests (liens) cannot be but foreign. This is why the system rather speaks of creation versus the additional obligations of the parties.
[116] *See* Complex Commentary at 430.
[117] *See* § 5:89(2)(a) of the Hungarian Civil Code.

been taken over; nor does the Code use such a terminology. Actually, the Hungarian system knows for more than two phases in the life of a security right. What may be puzzling is that, in effect, attachment and perfection could be identified (and we will use such terminology), though some additional requirements also need to be satisfied in order to have a fully enforceable security right.

110. As far as the generally applicable (i.e., applicable to all security agreements) preconditions are concerned, the new 2013 Civil Code (expressed somewhat non-transparently) differentiates **three phases** in the process of coming into being of security interests: to wit, attachment, constitution ("*alapítás*") and emergence ("*létrejötte*") of security interests. That 'attachment' phase can be extrapolated from a distinct provision proclaiming that the security agreement will be valid between the debtor and secured creditor even if the security interest was not constituted (i.e., perfected).[118] However, no distinct designation was attributed to such 'attached' security interests.

111. The situation is clearer with respect to '**constitution**' that presumes either transfer of possesion to the secured creditor by the debtor or registration in one of the existent registers; requirements that could be referred to as *perfection*.[119] A security interest, on the other hand, '**emerges**' once it was constituted plus the debtor can dispose of the collateral;[120] what one may conveniently name as a **thick concept of perfection.**

112. What further adds to the puzzle and makes comparison with other systems uneasy is that a distinct provision imposes the requirement that the collateral and the claim secured must be **identified.**[121] Even though the system is flexible and allows for identification of the collateral by any appropriate method and may include after-acquired property,[122] the language of the Code clearly speaks of this as a precondition for "*the coming into being of the security agreement*."[123] This remains a precondition of the validity of the security agreement notwithstanding that the secured claim may as well be determined by any appropriate method[124] (not only the identification of the collateral).

[118] *See* § 5:91 of the Hungarian Civil Code.
[119] *See* § 5:88 of the Hungarian Civil Code.
[120] *See* § 5:87(b) of the Hungarian Civil Code.
[121] *See* § 5:89(3) of the Hungarian Civil Code.
[122] *See* § 5:89(4) of the Hungarian Civil Code.
[123] *See* § 5:89(3) of the Hungarian Civil Code.
[124] *See* § 5:89(5) of the Hungarian Civil Code.

113. In case of consumer contracts[125] two further requirements are imposed for the sake of consumer protection: the exact value (sum) of the secured debt must also be specified[126] and the collateral must be individualized (i.e., collateral in this case cannot be determined only be description and after-acquired property cannot be pledged).[127]

114. To this list one has to add various forms of perfection by way of **constructive possession**:[128] i.e., when a third person holds possession of the collateral instead of the secured creditor. In such case, the third party-possessor has to be informed on the pledging of the asset held by him.[129] This ought to be mentioned because of the popularity the local version of field warehousing – called 'artificial warehousing ("*művi raktározás*")' – has gained during the last two decades.[130] In this case, it is not the collateral that is transported to a public warehouse but the warehouse comes to the place where the collateral is located (e.g., farm, factory). The Code itself recognizes as a valid transfer of possession for the purposes of the creation of security interests also a joint holding of the collateral by the secured creditor and the debtor (e.g., lockbox arrangements).[131] The precondition of validity in such cases is that the debtor cannot have unfettered dominion over the pledged asset in any circumstances.[132]

LITHUANIA:

115. Lithuanian law conditions the validity of security agreements on two requirements: 1. written form and 2. notary certification and registration (the latter does not apply to possessory securities). Requirement of written form means that the validity of security agreements is conditioned on some form of writing evidencing either

[125] The Code defines consumer contracts as forms of PMSIs – specific individual asset acquired by the debtor through the loan or trade-credit – and assets which are not used by the debtor for his professional or business activity. *See* § 5:90 of the Hungarian Civil Code.
[126] *See* § 5:90(b) of the Hungarian Civil Code.
[127] *See* 5:90(a) of the Hungarian Civil Code and Complex Comments at 429.
[128] *See* § 5:94(1) of the Hungarian Civil Code.
[129] *See* § 5:94(2) of the Hungarian Civil Code.
[130] Field warehousing is regulated by the 48th (XLVIII) Act of year 1996 on Public Warehousing *("1996. évi XLVIII. törvény a közraktározásról")* [hereinafter: Warehousing Act 1996], as (meaningfully) amended in 2013 by the 66th (LXVI) Act of year 2013 *("2013. évi LXVI. törvény a közraktározásról szóló 1996. évi XLVIII. törvény módosításáról")* [hereinafter: Warehousing Act 2013]. Actually field (artificial) warehousing is now more often resorted to then public warehousing in Hungary As per the separate statute regulating both types of warehousing, both can issue negotiable warehouse receipts, pledging of the goods in the warehouse is subject essentially to the same rules: the warehouse receipts are pledged with the financing bank. Contrary to the typical American field warehousing arrangement, the debtor – e.g., his employee or agent – cannot be appointed as warehouseman in Hungary. Rather, only licensed and properly equipped warehousing companies and their staff may engage in field warehousing. In this way, the issue of whether dominion (possession) over the collateral was left with the debtor could not arise. *See* Tibor Tajti (Thaythy), *the Resurrection of Field Warehousing – the Booming Hungarian Field Warehousing Sector, the Incomplete English Narrative and the Unexplored Field Warehousing Law of the United States,* **A**CTA **J**URIDICA **H**UNGARICA 55, No 3, pp. 185–235 (2014).
[131] For example, if the parties keep the collateral in a lockbox which could not be opened either by the debtor or the secured creditor only. *See* Complex Commentary at 431.
[132] *See* § 5:94(3) of the Hungarian Civil Code.

the existence of the security agreement – made separately or as part of the credit agreement – or a unilateral declaration proving the intention to pledge certain assets.

116. For non-possessory securities, to which also the second requirement (of notary certification and registration) applies, before the 2011 amendments to the Civil Code came into force on the 1 July 2012, the written form requirement could have been satisfied only by using a special form approved by the Minister of Finance; today there is no such requirement.

117. Yet what makes Lithuanian law peculiar is that written form is required even in case of possessory securities. Such written contracts on possessory pledges are not subject, however, to registration. Likewise, no registration is required when receivables (claims) are used as collateral for financing purposes under a factoring agreement.[133]

POLAND:

118. Two prerequisites apply: written form security agreements (except possessory pledges) and registration.[134] Separate rules apply to security assignments, where written agreement is required only if the assigned claim is evidenced in writing (however for the security to be effective in insolvency, written form with date certified by a notary is required) and no registration requirement exists (security assignments are "secret liens" perfected by a notice to the debtor of the assigned claims).

119. While encumbering of immovables requires special notarial written form, in case of registered pledges a *simple* written form agreement is required.[135] The agreement should, at least, 1/ specify the date of the agreement; 2/ identify the debtor and creditor (i.e., business name and registered office or address); 3/ specify the collateral (based on its features); as well as 4/ specify the claim secured by the pledge and the maximum amount secured.[136]

120. Polish law is idiosyncratic in two matters in respect of the securing of obligations from debt securities issued in a series (i.e., fixed-income securities like bonds). Firstly, the security agreement need not be concluded between the debtor and the secured creditor(s) but by the debtor (pledgor) and the pledge administrator.[137] Although the

[133] See chapter XLV of Book VI of the Civil Code on factoring. Registration is also not required when receivables (claims) are being sold.
[134] For registered pledges *see* Article 2.1. of the Registered Pledge Act.
[135] *See* Article 3.1. of the Registered Pledge Act, which stresses that "*provisions on special written form set forth elsewhere [i.e., other legal acts] do not apply to agreements to establish a registered pledge on claims and rights*." Registration is not required in case of financial pledges that are created by a written agreement and perfected by a notice.
[136] *See* Article 3.2. of the Registered Pledge Act.
[137] *See* Article 2.4. of the Registered Pledge Act.

contents of such agreements are not regulated by the Act, this may amount to a control agreement. Secondly, the securities are established for the benefit of all creditors[138] – who will be represented by a pledge administrator (who may but must not be one of the creditors) the appointment of whom is mandatory by the issuer of the securities.[139]

Question 7: Do the rules for the creation of security rights vary depending on the nature of the asset in question?

HUNGARY:

121. If one departs from the specific titles of the paragraphs of the Code,[140] one may easily be misled into thinking that the Code does not impose any further formal requirements on the creation of security interests except what has been listed under question 6. In fact, however, through scattered provisions, the creation of security rights is subject to additional preconditions depending on the nature of assets used as collateral and – in case of the distinct security device we will conveniently name as 'security-bailment' ("*óvadék*") – tradition.

122. If these additional conditions are also taken into account, we may realize that actually the Code knows **three (perfection) methods** for the creation of security interests over assets: transfer of possession (including constructive possession), registration in one of the public registers and control – the last essentially disguised as the separate security device of 'security bailment.'[141]

123. Notification of an obligor (account debtor) is also a requirement – cast in the form of debtor' obligation[142] – for security interests over rights and claims as well as registration in the register of security interests. In other words, perfection of security interests on rights and claims is by registration as well[143] as opposed to the old Civil Code's perfection method that was notification only.

124. It should be emphasized that a written security agreement is a general condition applicable to all secured transactions, which could be substituted only by certificated

[138] *See* Article 4.3. of the Registered Pledge Act.
[139] *See* Article 4.4. of the Registered Pledge Act.
[140] For example, the above cited § 5:87 of the Hungarian Civil Code is named "Emergence of the Security Interest" ["*A zálogjog létrejötte*"] and that of § 5:88 "Constitution of the Security Interest" ["*A zálogjog alapítása*"]. Truth be told, all the referred to provisions are located in the relatively short Chapter XXI entitled also "the Emergence of the Security Interest" ["*A zálogjog létrejötte*"].
[141] *See* § 5:95 of the Hungarian Civil Code.
[142] *See* § 5:89(2)(c) of the Hungarian Civil Code.
[143] *See* Complex Commentary at 424 which proclaims: "*[The new Civil Code] makes a step ahead and extends [registration] to intangible assets, as well as to rights and claims. As a result, constitution of security rights by registration becomes a possibility for all kinds of assets.*"

securities (documents of title and negotiable paper satisfying the definition of 'security' under Hungarian law).[144] We will briefly summarize each perfection method.

A Perfection by Transfer of Possession

125. The basic rule is that a possessory pledge can be created only on movable (tangible) assets[145] (or equivalents such as certificated securities) either by the possessor ("*birtokos*" or "*főbirtokos*") or his agent (called the sub-possessor ["*albirtokos*"]). Two forms of joint constructive possession are recognized by the system as substitutes for the transfer of possession from debtor to secured creditor: 1/ joint-possession by the debtor and secured creditor, and 2/ possession by a third party as a pledge-holder for their account.[146]

B Security Bailments and Perfection by Control

126. While the rules on perfection by transfer of possession are more or less common, that may not be so with respect to a specific type of secured transaction – or a specific method of pledging – called the 'security-bailment' ["*óvadék*"]. This device has "*historically developed parallel with security interests and grew into a kin institution;*"[147] a process that ended with its integration into security law. The integration did not, however, end with the complete disapparance of this device: specific rules only applicable to it are part of the Code of 2013.

127. Two distinguishing features make the security-bailment special: *first,* only some specific types of assets may be used as collateral; and *secondly,* the secured creditor has a direct right of enforcement on the asset bailed. As far as the first prong is concerned, only cash, investment property (securities), some bank accounts and similar forms of personal property may qualify.[148]

128. The enforcement rules ensure direct enforcement and provide the secured creditor with a strict-foreclosure-like rights: i.e., he may upon default unilaterally declare to the debtor that he is acquiring title (ownership) on the bailed collateral, or if he has already acquired title that he has no obligation to return to the debtor assets of the same quantity and type that had been transferred to him initially.[149] These rules are, however, less onerous compared to the generally applicable strict foreclosure

[144] *See* § 5:89(6) of the Hungarian Civil Code.
[145] *See* § 5:101(2) of the Hungarian Civil Code.
[146] *See* § 5:94(1) of the Hungarian Civil Code. The language of the Code is quite short and does not regulate the details of the contract between the third party and the parties to the security agreement. The Comments leave this to the parties and point to the provisions on deposit contracts. *See* Complex Commentary at 432.
[147] *See* Complex Comments at 432.
[148] *See* § 5:95 of the Hungarian Civil Code.
[149] *See* § 5:138(1) of the Hungarian Civil Code.

rules. Namely, given that the value of the collateral subject to a security-bailment is always easily determinable, there is no need for the extra step of secured party-offer and acceptance by the debtor.[150]

129. Hungarian law allows for perfection of security-bailments by transfer of possession and control (though the Code does not use this term but rather describes what actions need to be taken).[151] The perfection rules follow the nature of assets and hence in case of cash and certificated securities – tangible assets that can be physically possessed – the perfection method is by transfer of possession; i.e., the rules on possessory pledges apply. As opposed to that, in case of bank accounts the method is by control. Strangely, the Code talks of transfer of possession also in case of dematerialized securities; or forges an artificial concept of possession for this specific case.[152]Given the direct reliance on comparative law by the drafters of the 2013 Code, this formula is hardly comprehensible.

130. The Comments speak of the perfection of security-bailment by way of registration only as a curiosity "*having little if any practical importance*."[153] Yet this possibility is not excluded either. As the Comments themselves admit, this may be the case whenever the collateral is identified through a wide-reaching description, like all movables or receivables of a company.[154] Notwithstanding the cautionary language, the Code does have an explicit priority rule according to which if the same asset is encumbered by both a security-bailment and a registered security right, the former enjoys priority.[155]

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[150] *See* Complex Commentary at 474. For the offer & acceptance process applicable to other types of secured transactions *see* § 5:137 of the Hungarian Civil Code.

[151] *See* § 5:95(2)(a) of the Hungarian Civil Code.

[152] *See* § 5:95(1)(b) of the Hungarian Civil Code. This anomaly was also noted by the HVG Commentary at 125. The explanation the Complex Commentary provides – a Commentary that was written by the drafters of the Code – reads as follows: "*Creation of a security-bailment in case of dematerialized investment property occurs by way of transfer of possession so that a transfer is effectuated between the investment accounts of the parties (i.e., by charging the debtor's investment account and crediting the secured party's investment account).* ***This can be looked upon as a form of possessory pledge because – based on the Civil Code and similarly to the earlier rules – the dematerialized security is also a security (investment property) to which the rules on 'things' must be appropriately applied [§ 5:14(2)] and as a result of the here described account transactions the secured creditor acquires real control over the securities (investment property) [§ 5:3(1)].***" *See* Complex Commentary at 434. In other words, the drafters – instead of introducing the concept of 'control' – opted for artificially stretching the concept of possessory pledge to extend also to physically clearly intangible goods: uncertificated securities.

This was a strange option especially as both the EU-Directive on Financial Collateral Arrangements of 2002 and the Draft Common Frame of Reference (see Article IX.-3:204: Control over financial assets) have introduced the concept of 'control.' While the EU-Directive is law also in Hungary as a Member States of the EU, the DCFR was used as a source as stated by the drafters (see Complex Commentary, Introduction, point 4, page 20).

[153] *See* Complex Commentary at 433.

[154] *See* Complex Commentary at 433.

[155] *See* § 5:123 of the Hungarian Civil Code.

131. Perfection **by control** presumes a tripartite (the debtor-account-holder, the secured creditor and the service-provider with whom the account is maintained) written agreement according to which the service-provider proclaims that, while it will follow the instructions of the debtor only with the consent of the secured creditor, it will obey the instructions of the secured creditor without the approval of the debtor.[156] In case the secured creditor is the service provider itself (bank or broker), a bipartite contract guaraneeying the same right to the service provider would qualify.[157]

132. If one adds up all these elements, one can see that what is a semi-distinct nominated security device for Hungarian law, is actually content-wise equal to with the rules on perfection by control in systems like UCC Article 9.

C Perfection by Registration (Filing)

133. Prior to the first 1996 secured transactions reforms – save for some registers dealing with specific high value assets and IP rights (see below) – no register was in existence for the registration of security interests on movables, claims or rights in Hungary. This changed with the common law-inspired reforms in 1997 when a brand new electronic registry was introduced specifically for recording security interests on movables (but not for claims/receivables). The National Chamber of Public Notaries ("*Országos Közjegyzői Kamara*") was entrusted with the running of the system.[158]

134. Then, the registration system was structured to follow the system for registration of mortgages on immovables;[159] including the constitutive and authentic nature of entries.

135. This has radically changed with the 2013 Civil Code. On the one hand, the provision that entrusted the Chamber with the running of the system was deleted and no specific body was nominated in lieu. The intention was to give the government freedom to decide and to change the service-provider if necessary in the future.[160] Nonetheless, in 2014 (the year of the coming into force of the Civil Code), the right to run the system was still left with public notaries and at the moment no change is expected.[161]

136. A more meaningful change occurred, however, in respect of the perfection rules. The system has **switched to notice-filing**; a system originating in the American UCC

[156] *See* § 5:95(2)(a) of the Hungarian Civil Code.
[157] *See* § 5:95(2)(b) of the Hungarian Civil Code.
[158] The webpage of the Chamber is < http://www.mokk.hu >. *See also* § 262(2) of the former Civil Code for the mandate given to the National Chamber.
[159] *See* Complex Commentary at 457.
[160] *See* Complex Commentary at 457.
[161] *See* § 2 of Act No. CCXXI of year 2013 on the Register of Security Interests (stepped into force on 16th of March 2014). *See also* Ordinance No. 18/2014 (III.13) of the Ministry of Justice and Administration on the Detailed Rules for the Operation of the Register of Security Interests.

Article 9. This means that now the entries in the register serve "merely" to notify third parties on the existence of security interests and to ensure priorities.[162] In practical terms, while earlier the security agreement *itself* had to be made before a public notary who had also the duty to check the data and to instruct the parties of their rights, now only a notice needs to be filed with the registry containing the basic data necessary for the identification of the transaction, the parties and the collateral.[163] The fact that an entry has been made is now not an authentic proof of the existence of the security interest.[164] Besides these, the register displays also the date and the ranking of the entry.[165] Under the new system, entries are effectuated without checking the contents (merits) by the public notaries.[166] To avoid misunderstandings, it should be noted that no new term was introduced for 'filing' instead of 'registration' to express the change.

137. At the same time, to ensure ease of access, the Act proclaimed that "*the register of security interests is public and its contents are freely accessible via Internet without any identification*."[167] In brief, the system became electronic, linked via Internet and thus quicker as well. While searching the database is **free of charge**,[168] for entries a modest fixed fee is charged.[169] Both the secured creditor and the debtor are entitled to file (creation, modification or deletion), however, only if first registered as users. [170] Prior registration as users ensures electronic identification of the parties.[171]

138. The entry process has become electronic and fast. *First,* entries can be made solely by way of electronic forms (the outlook and elements of which are fixed by law)

[162] *See* Complex Commentary at 458.
[163] These include 1/ the name and some other data determined by special statute of the debtor; 2/ the name and some other data determined by special statute of the secured creditor: 3/ name of the agent of a legal person or other association and data determined by special statute, as well as 4/ the determination of the collateral either by specification or by description. *See* § 5:115(1) of the Hungarian Civil Code. The entry may (but must not) specify also the amount of the debt the collateral secures. *See Id.* § 5:115(2).
[164] As the Complex Commentary says: "*… the function of the register is not to authentically prove the existence of the security interest but rather to inform the public about the constitution of the security interest, ensure its validity against third persons (§ 5:91) and its priority position (§5:118) to enhance predictability* ("*hozzájáruljon a forgalom biztonságához*") *on the market*." *See* Complex Commentary at 459.
[165] *See* § 5:116 of the Hungarian Civil Code.
[166] *See* § 5:113(1) of the Hungarian Civil Code.
[167] *See* § 5:112(2) of the Hungarian Civil Code.
[168] *See* § 5:112(2) of the Hungarian Civil Code.
[169] As per the amended Ordinance of the Ministry of Justice on the Tariffs of Public Notaries No. 14/1991 (XI. 26) the fees payable (work and costs included) are: 1/ 6,000 HUF for each entry (§ 30F(1)), and 2/ in case of registration through a permanent representative 6,000 HUF for each hour of commenced work but not exceeding 18,000 HUF (even if when working more than three hours) (§ 30F(2)). As per the exchange rate in December 2014 (1 Euro = 307,277 HUF), six-thousand Hungarian Forints were slightly less than 20 Euros.
[170] *See* § 5:113(3) of the Hungarian Civil Code.
[171] *See* § 5:113(5) of the Hungarian Civil Code.

via the Internet webpage of the Chamber of Public Notaries.[172] *Secondly,* the parties are automatically informed electronically of any entry effectuated by the other party.[173]*Thirdly,* although both the secured party and the debtor can make entries both of the creation and deletion of an entry, however, no entry on the creation of a security interests can be valid with the electronic signature of the debtor,[174] and vice versa – for deletion the consent of the secured creditor is a must.[175] The secured creditor's consent (declaration) for deleting the security interest is deemed to be given if the secured creditor has failed to make declaration to the contrary within thirty days.[176] To ensure performance, the Code adds to this an obligation for the secured creditor neither to withhold his consent if the secured transaction has ceased to exist, nor to file an objection against deletion without a legal basis.[177]The secured creditor breaching these rules is liable for all damage caused.[178]

139. Last but not least, the 2013 Civil Code expanded the reach of the register of security interests in two directions. Firstly, unlike as it was earlier, the filing requirement has been extended from security interests on movables to cover also security interests on receivables (claims) and rights that are not subject to registration in a specific register.[179] This means that in the case of receivables, besides notification of the obligor (account debtor), filing in the security interest register is also a must (a perfection requirement). On the other hand, financial leasing,[180] factoring[181] and contracts with retained title[182] are also subject to registration with the register of security interests.

D Perfection by Constitutive Registration

140. Hungarian law does not know of the real versus personal property securities divide of the common law and hence regulates both in the same part of the Civil Code and continuaedly – even after the meaningful infliltration of common law concepts through the secured transactions reforms – looks upon the two as two sides of the same coin. For this reason one has to devote some attention to security rights on

[172] *See* § 5:113(1) of the Hungarian Civil Code.
[173] *See* § 5:113(2) of the Hungarian Civil Code.
[174] *See* § 5:114 of the Hungarian Civil Code. This, in other words means, that while the electronic signature (consent) of the secured creditor is not a must, if the secured creditor began the filing, the entry will not become valid until consented to by the debtor electronically.
[175] *See* § 5:117(3) of the Hungarian Civil Code.
[176] *See* § 5"117(3)(b) of the Hungarian Civil Code.
[177] *See* § 5:117(4) of the Hungarian Civil Code.
[178] *See* § Complex Commentary at 460.
[179] *See* § 5:93(1)(b) of the Hungarian Civil Code. *See also* Hungarian Insolvency Handbook, at 750.
[180] *See* § 6:409 of the Hungarian Civil Code.
[181] *See* § 6:405 of the Hungarian Civil Code. With this innovation the Hungarian system has come closer to the American UCC Article 9 that likewise extends to both sale of receivables (factoring) and use of receivables "only" as a security. The crucial difference is that the Hungarian system linked factoring to the secured transactions system only through filing in the common security interest register. All the other possible rules are located outside secured transactions law.
[182] *See* § 6:216 of the Hungarian Civil Code.

immovables, i.e., mortgage law. As special registers exist for some specific classes of personal property (movables) (e.g., ships, aircraft) and as they typically function in a similar way to the real property mortgage registries, the two will be discussed together.

E Mortgage of Immovables

141. In case of mortgage law, instead of reforms, one could speak only of improvements as far as the new 2013 Civil Code is concerned. The most significant changes relate to the technical rules on the operation of the immovables registries given that the primary problems did not concern mortgage law itself (i.e. the applicable provisions of the Civil Code) but were rather of a technical and technological nature (e.g., lag of entries, need of modernization). These, however, will not be discussed here.

142. As already mentioned, until the arrival of the new 2013 Civil Code, the legal regime for the registration of security interests on movables was intentionally structured to follow, so far as possible, the one applicable to mortgages of immovables. The two most important basic rules were that the entries into the register of mortgages of immovables had constitutive force and the entries were presumed to be authentic proofs of the entries ("*közhitelesség*"). In the new 2013 Civil Code, these remain key features of the law in the context of immovables (as well as security interests on specific personal property registries) but not in case of the register for security rights on movables, rights and claims. The volte face occurred as result of the realization that the features of these asset categories require distinct legal treatment.[183]

143. Another key difference is that while the immovables register operates as an asset-based database ("*reálfólium*"), the register for security interests on movables, rights and claims uses a debtor-based listing ("*perszonálfólium*"). As a consequence mortgages could be registered, on the one hand, only on *individualized* and already *existing* immovables and only on immovables that were already *in the ownership* of the debtor (and therefore have been entered into the books) at that point in time.[184] In case of the immovables register entries can be made either based on the security agreement itself or based on the permission of the debtor.[185] The system imposes a specific obligation on the debtor to provide the secured party with permission and this obligation gives the secured party some additional leverage.[186]

[183] *See* Complex Commentary at 457.
[184] *See* § 5:93(3) of the Hungarian Civil Code.
[185] *See* § 5:93(3) of the Hungarian Civil Code.
[186] *See* § 5:89(2)(b) of the Hungarian Civil Code.

F Specific Registered ("*Lajstromozott*") Movables

144. It is hardly a specificity of Hungary that certain high value classes of personal property (movables) and the encumbrances that could be created on them are registered in distinct registers. In Hungary, the most important ones are the following: 1/ ships; 2/ aircraft; 3/ patents; 4/ trademarks; 5/ specimen/models and 6/ shares in limited liability companies.[187] The perfection and other rules for these assets are all contained in *lex specialis,* which tend to be replicas of the immovables registry system.

LITHUANIA:

145. There are some variations depending on the nature of the collateral though the basic division is along the lines of immovables versus movables-cum-rights and possessory versus non-possessory securities. Based however, on the language of the Code – what could be taken as an idiosyncratic feature of Lithuanian law – one may get the impression that the main division is between the so-called legal and contractual mortgages.[188] As this Report focuses on consensual (contractual) security rights, we will abstain from detailed analysis of the treatment of legal (statutory) mortgages. The variations depending on the nature of the asset used as collateral would be the following.

146. In case of mortgage of immovables, registration has constitutive force and thus mortgages on immovables can come into existence only by registration in the appropriate public register.[189]

147. The situation is a bit more complex in case of movables and rights. Formally the system knows not the dualism of attachment and perfection of security rights; i.e., there are no such distinct designations. Content-wise, however, the Code's provisions make such a differentiation in case of non-possessory securities as it is provided that the security right is valid *against third parties* and bankruptcy administrator only after registration with the Register of Mortgages.[190] In case of possessory securities, the situation is simpler as perfection is linked to transfer of possession plus conclusion of a written pledge agreement.[191] As already noted, the latter makes Lithuanian law distinctive.

148. The law provides specific rules when negotiable documents are used in practice. Thus, while for pledging with pawnshops the Code requires the issue of a pawn-ticket.[192] In case of documents of title granting rights to the holder, the transfer of

[187] *See* Complex Commentary at 430.
[188] *See* Article 4.175 of the Lithuanian Civil Code.
[189] *See* Article 4.187 of the Lithuanian Civil Code.
[190] *See* Article 4.213 of the Lithuanian Civil Code.
[191] *See* Article 4.213 of the Lithuanian Civil Code.
[192] *See* Article 4.227(2) of the Lithuanian Civil Code.

possession may be substituted by transfer of the document (e.g., warehouse receipts).

149. The rules on pledging of receivables are somewhat obscure. Namely, the Civil Code regulates use of claims (receivables) as collateral as part of the law on factoring[193] though without entering into details. The factoring rules, however, do not provide for registration of security rights as a precondition of creation but rather link that to notification of the obligor (account debtor).[194] On the other hand, the Civil Code rules on "pledges" recognize pledging of 'real rights'[195] – which includes claims (receivables)[196] – just as one could extend the company charge onto receivables;[197] both subject to registration under this part of the Code.

POLAND:

150. There are some variations depending on the nature of the asset used as collateral though the basic rules are typical to a reformed Continental European civil law system.

151. *First,* constitution of a mortgage of immovables presumes execution of a notarized deed (writing)[198] and registration in the land and mortgage register.[199]

152. *Secondly,* the rules on establishment of possessory pledges are somewhat peculiar under Polish law. Namely, transfer of possession over the collateral and the pledge agreement (which may be even oral) makes the pledge valid only between the parties to the transactions.[200] In order to make it valid against third parties, besides transfer of possession, a *written* contract with *a certified date* is needed.[201] The requirement of certified date was not introduced until 2009 (with the effect from 20th of February 2011) to prevent the abuse of the possessory pledge due to its secret nature. Since this change the possessory pledge may "compete" with other security interests

[193] *See* Article 6.903(2) of the Lithuanian Civil Code.
[194] *See* Article 6.909(1) of the Lithuanian Civil Code.
[195] *See* Article 4.204 of the Lithuanian Civil Code.
[196] For pre-2011 court cases and scholarly analyses are of continued relevance. *See* on this Lina Aleknaite, *Receivables Financing in Lithuania: Is the Legal Regulation Suited to Accommodate the Practical Needs of Industry?, in:* Review of Central and East European Laws vol. 34 (2009), at 257-258 [hereinafter: Aleknaite, Receivables in Lithuania, 2009].
[197] Reference is primarily made to Articles 4.202 and 4.177 of the Lithuanian Civil Code.
[198] *See* Article 245 with reference to Article 158 of the Polish Civil Code; i.e., the rules on the transfer of ownership requiring a notarized deed apply mutatis mutandis also the establishment of limited proprietary rights. The requirement of notarial form is limited only to the statement of the property owner however (Article 32.1 of the Polish Mortgage Act). Furthermore, in the event the mortgage is established as security for banking transactions (such as bank loans) for the benefit of a bank, notarial form may be waived if a special form of "banking documents" is used. These documents are to be duly certified and stamped by representatives of the bank (see article 95.3 of the Banking Law, statute dated 29 August 1997, published in Journal of Laws 2015 item 128). The rationale of these simplifications is to make mortgages cheaper through decreasing the transaction costs.
[199] *See* Article 67 of the Polish Mortgage Act.
[200] *See* Article 307 of the Polish Civil Code.
[201] *See* Article 307.3. of the Polish Civil Code.

in distribution of enforcement proceeds[202] and therefore the moment of its creation becomes relevant.

153. *Thirdly,* non-possessory security rights on movables, rights (on intangible property) and claims (receivables) as well as rights to financial instruments (with the exception of financial instruments covered by the relevant EU legislation) come into being if registered with a public register; the "*Register of pledges*."[203] Enterprise (global) securities are treated as a variant of registered pledges and are subject to the same registration rules as movables, rights and claims.[204]

154. *Last but not least,* two further registration-related solutions of Polish law deserve mention. One of them is related to security interests on motor vehicles that are also subject to registration with the register of registered pledges, however, the pledge is additionally indicated on the registration document of the vehicle.[205] This is a peculiar yet useful solution of Polish law. Another such idiosyncracy of Polish law is that security interests on civilian aircraft and industrial property rights are also subject to registration with the register of registered pledges irrespective of the fact that that distinct registers exist for those items. There is provision however for exchange of information between the two registers.[206] In both cases, registration with the register of 'registered pledges' enjoys primacy.

[202] *See* Articles 1025 and 1026 of the Polish Code of Civil Procedure.
[203] *See* Article 7.2. of the Polish Registered Pledge Act.
[204] *See* Article 7.2(3) of the Polish Registered Pledge Act.
[205] *See* Article 12.1. of the Polish Registered Pledge Act.
[206] *See* Article 41a. of the Polish Registered Pledge Act.

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V ENFORCEMENT OF SECURITIES COMPARED

Question 8: To what extent is it possible for the secured party to enforce the security without having to use formal court procedures?

HUNGARY:

155. Similarly to other Continental European civil law systems and contrary to common law systems,[207] Hungarian law looks as well with suspicion on out-of-court enforcement. Hence, the basic rule is that security rights are to be enforced through formal court procedures. However, due to a number of reasons, this stance has begun to change already in the 1990s. This notwithstanding that facially the basic rule remained essentially the same in the new 2013 Civil Code which provides among the fundamental principles that "*The enforcement of rights provided by the Act [i.e., the 2013 Civil Code] is through courts, unless otherwise provided.*"[208] [Emphasis added].

156. Perhaps the best expression of the shift are the provisions related to enforcement of security interests. That the drafters have attributed heightened importance to this novelty is visible already from the fact that these, essentially procedural rules, have found their place not in the separate statute – that otherwise used to and continues to regulate court enforcement of security rights[209] – but in the Civil Code itself; a solution per se novel in Hungary.[210] Furthermore, the out-of-court enforcement system is now not only regulated in more detail compared to the earlier law[211] but the reach of the rules has expanded as well.

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[207] For common laws, encouragement of self-help is said to be one of the eight principles forming the '*philosophy of commercial law*.' *See* Roy Goode, *the Codification of Commercial Law* (1988) 14 Monash University Law Review 136, at 148. This is definitively not so in civil law systems, which either prohibit or severely restrict out-of-court enforcement of rights based on private or commercial law. *See* also Tibor Tajti, *Testing the Equivalence of the new Comprehensive Australian Personal Property Securities Act, its Segmented European Equivalent and the Draft Common Frame of Reference,* 24 Bond Law Review, 85-148 (June 2012), at 132.

[208] *See* §1:7. of the new Hungarian Civil Code titled: [Guarantying Court Enforcement]. The earlier formulation of the same principle in §7 of the 1959 Civil Code (Act No. IV of year 1959 on the Civil Code) was: "*It is the duty of every state (governmental) body to protect the rights guaranteed by this act. Their enforcement – unless otherwise provided by law – is through courts*."

[209] The court enforcement of security rights is regulated by Act No. LIII of year 1994 on Court Enforcement.

[210] As it is commonly known, out-of-court enforcement of security interests is an integral part of Article 9 of the American Uniform Commercial Code and all the other systems that have taken over the unitary security-interest-based system; in particular the Canadian common law provinces, New Zealand, Australia. Book IX of the European Draft Common Frame of Reference should also be added to the list.

[211] *See* the Complex Comments that proclaim that the 2013 Civil Code "*enlarges and, compared to the earlier system, regulates in more detail the out-of-court enforcement of security rights*." *See* Complex Comments, at 465.

157. The following features of the new rules should be mentioned to properly describe their contents and reach.

First, the new regime for the enforcement of security rights is ***cumulative***: secured party may opt for any of the options[212] (court versus out-of-court or may shift from one to another form of self-help).[213] While these rights are not subject to limitations in case of business finance, in the context of consumer contracts there are two limitations. On the one hand, the collateral may be disposed of only at a public sale (except if the parties have agreed[214] – in writing and after default – on another method of disposal). On the other hand, strict foreclosure is prohibited: i.e., the secured creditor may not acquire the title (ownership) of the collateral (save on cash, certificated and uncertificated securities as well as on some bank accouts).[215]

158. *Secondly,* the Code itself talks explicitly of three out-of-court enforcement methods only: disposition, limited version of strict foreclosure (i.e., acquisition of title/ownership by the secured creditor on the collateral), and collection of receivables or enforcement on a right (that was used as collateral).[216] To the mind-set of Hungarian law, repossession (i.e., retaking possession of the collateral) is not a distinct form of self-help but only a prerequisite of disposition.[217]

159. *Thirdly* and most importantly, the 2013 Civil Code introduced a restrained and notification-conditioned form of self-help repossession.[218] This novel institution rests on more footings as follows.

160. It is proclaimed that the secured creditor is entitled to take possession (repossess) of the collateral upon default of the debtor, however***, only for the sake of disposition.***[219] This last precondition makes the Hungarian solution somewhat peculiar because – as the commentaries state – "*repossession is not to serve its own end [but] may be exercised solely for the purpose of disposition. Therefore, if the secured party would not be in the position to sell the collateral because of a lack of demand on the market, then he would not be entitled to take possession from the debtor.*"[220] The same prohibition would apply if disposition could be effectuated without first repossessing from the premises or hands of the debtor.[221] Such a solution is a clear example of the debtor-protective nature of the system as it fails to recognize the

[212] *See* § 5:126(3) of the Hungarian Civil Code.
[213] *See* § 5:127(2) of the Hungarian Civil Code.
[214] *See* § 5:128(a) of the Hungarian Civil Code.
[215] *See* § 5:128(b) of the Hungarian Civil Code.
[216] *See* § 5:127(1) of the Hungarian Civil Code.
[217] *See* § 5:132(1) of the Hungarian Civil Code.
[218] *See* § 5:132 of the Hungarian Civil Code.
[219] *See* § 5:132(1) of the Hungarian Civil Code.
[220] *See* HVG Commentary at 188 referring to the reasoning of the amendment proposal that was transposed to the final formulation of this paragraph.
[221] *See* Complex Commentary at 468.

value inherent to the changed strategic position repossession entails. It disregards the realities of the market as well given that often nobody can readily foretell whether there is a market for the collateral or whether the market will freeze by the time of the disposition unexpectedly, at all.

161. It is also peculiar that the system somewhat naïvely departs from the presumption that debtors are normally willing to cooperate with the secured creditor. As the related commentaries and scholarly papers cite no empirical studies whatsoever on that, one may conclude that this presumption of the drafters rested on purely theoretical projections. True, the Code imposes two related obligations on the debtor as well: on the one hand, to hand over the collateral or to allow repossession by secured creditor,[222] and on the other hand, to refrain from any such action that may hinder disposition by the secured creditor.[223]

162. Similar to the DCFR yet in stark contrast to UCC Article 9, the new Civil Code's most significant out-of-court repossession-weakening rules impose ***the duty to notify the debtor in advance*** related to his obligation to (re)transfer possession of the collateral. Although the rules are not fully clear, such notification must contain a demand to the debtor[224] and set also a deadline within which to transfer possession. As far as the latter is concerned, the basic – pretty vague – rule is that the deadline must be appropriate to the given circumstances.[225] This is then supplemented by further limitations according to which the deadline *cannot be less than ten days* in case of movables and *twenty days if immovables* were used as collateral.[226] Moreover, letting the creditor take possesion of vacated dwelling-immovables cannot occur in less than, at least, three months.[227]

163. *Last but not least,* the greater reliance on out-of-court enforcement is further counter-balanced – with respect to all out-of-court (self-help) forms – by two *new court remedies* aimed at protecting the debtor in addition to his right to damages caused by improper exercise of enforcement rights.[228] These are court orders (*injunctions*) either to suspend the out-of-court enforcement of security rights or to enforce them according to the terms and conditions determined by the court;[229] both presume filing of a claim to the court by the debtor himself or by any other third person having a legal interest.[230]

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[222] *See* § 5:132(3) of the Hungarian Civil Code.
[223] *See* § 5:132)3) of the Hungarian Civil Code.
[224] *See* § 5:132(3) of the Hungarian Civil Code mentioning the demand ("*felszólítás*").
[225] *See* § 5:132(2) first sentence of the Hungarian Civil Code („*a körülmények által indokolt határidő*").
[226] *See* § 5:132(1) of the Hungarian Civil Code.
[227] *See* § 5:132(2), second sentence of the Hungarian Civil Code.
[228] *See* Complex Commentary at 466.
[229] *See* § 5:130 of the Hungarian Civil Code.
[230] What qualifies as legitimate 'legal interest' is not defined by the Code, nor is the list of persons who may have such interests. For example, as the HVG Commentary suggests, all persons that should have been notified of the secured creditor's intention to dispose of the collateral or all the secured creditors

It is incomprehensible why only (one of the) Commentaries – and not the text of the Code itself – declared that these new tools were introduced to "*prevent irreversible harm and damages*" as such a guidance might have helped the courts better understand the nature and the intended function of these. Similar critique could be formulated for the drafters' failure to ensure swift issue of these measures through specific prescriptive language,[231] for example, in summary or even ex parte proceedings. At the moment nothing seems to guarantee that.

A Recognized Out-of-Court Enforcement Forms
Private Disposition

164. Sale of the collateral – private or public[232] – after default is listed as one of the out-of-court forms of enforcement of security interests[233] for the exercise of which no special agreement is needed: it is a statutorily-granted right of the secured creditor.[234] This enforcement avenue can be exercized solely via public sales in case of *consumer contracts*, unless the parties make an agreement in writing on another method of disposition - and after default.[235]

165. The Code has tried to find a formula for balancing two contrasting goals: opening the doors more widely to private disposition yet providing the debtor, other affected creditors and third parties (e.g., surety) with efficient counter-balances. While the secured creditor's position was strenghtened through reduction of the formal requirements tying the hands of the secured creditor (including the right to choose the enforcement avenue), the debtor and other (junior) secured creditors are protected through a set of explicit rules all originating in the standard of commercial reasonableness.[236]

166. The balance rests on six footings. ***First,*** it declares that dispositions must be undertaken in commercially reasonable manner and that "*the interests of the debtor and of the surety must also be taken into account during disposition*."[237] The rebuttable presumption that the disposition was commercially reasonable is presumed only for sales on stock-exchanges and only if quoted price exists for the given security-collateral (i.e., market price valid at the time of sale) and for sale in the ordinary course of business (i.e., sale by a known method on a recognized market and in the ordinary

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who have been harmed by the inappropriate – not satisfying the standards of commercial reasonable disposition – may qualify. *See* HVG Commentary at 185.

[231] *See* Complex Commentary at 466.

[232] *See* § 5:134(2)(b) of the Hungarian Civil Code.

[233] *See* § 5:127(1)(a) of the Hungarian Civil Code.

[234] *See* the Complex Commentary at 465.

[235] *See* § 5:128 of the Hungarian Civil Code.

[236] *See* Complex Commentary at 466.

[237] *See* § 5:133(1) of the Hungarian Civil Code.

course of business).[238] This standard – imported from US law – comes on top of the generally applicable principles of good faith and honesty (long known by Hungarian law) and the duty to "*act as it is expected in a given situation*."[239]

167. ***Secondly***, disposition is subject to certain **notification requirements**; a requirement that can be disregarded only in case of quickly deteriorating as well as collateral the value of which would significantly fall due to delay inherent to notification or that is traded on commodities or stock exchanges.[240] Notwithstanding the good intentions, the notification requirements are quite burdensome as they protect basically all parties that might have any kind of right on the collateral, from the debtor, surety (and his guarantor), other (junior) secured creditors, and all parties who either have registered rights or prove the existence of rights otherwise.[241]

168. ***Thirdly***, as already explained above, the Code introduced a *sui generis*, debtor cooperation-presuming form of self-help repossession (retaking) of the collateral.[242] This is another meaningful departure with conventional civil law doctrines that look with great suspicion on any forms of out-of-court enforcement. It is a bit strange that while Hungarian law looks on this "merely" as a precondition for private disposition – part of the law that transplanted the American doctrine of commercial reasonableness – it failed to heed the extremely rich experiences with self-help repossession. One of the issues that will presumably cause lots of headache in the future is that the system departed from the idealistic postulate that most of the debtors are willing to cooperate and return the collateral voluntarily. As a result, the 'without the breach of peace' standard known to UCC Article 9 (or anything resembling that) was not taken over.

169. ***Fourthly***, more as an illustration and encouragement rather than a restriction, a few shorter provisions declare that the secured creditor is entitled – as a statutory agent of the debtor[243] – to sell (i.e., to transfer the ownership) the collateral on behalf of the debtor,[244] in altered or unaltered form,[245] privately or publicly,[246] in bulk or

[238] *See* § 5:133(2) of the Hungarian Civil Code.
[239] *See* Complex Commentary at 469. The principle of good faith and honesty is defined by § 1:3. of the Hungarian Civil Code. Sub-section (2) of this provision contains the concrete example in civil law known as the maxim of *venire contra factum proprium; a* rough equivalent of the common law [equitable] estoppel. Concretely: "*It infringes the principles of good faith and honesty to act contrary to one's earlier behavior which the other party had reasonably relied on.*"
The principle of expected behavior, on the other hand, is contained by § 1.4. of the Hungarian Civil Code. This is a general principle that reads: "*Unless a different standard of behavior is expected by this Code, one has to act as it would be normally expected in the given situation*." This, in other words, is a sort of rationality standard just expressed with different words.
[240] *See* § 5:131(4) of the Hungarian Civil Code.
[241] *See* § 5:131(1) of the Hungarian Civil Code.
[242] *See* § 5:132 of the Hungarian Civil Code.
[243] *See* Complex Commentary at 469.
[244] *See* § 5:134(1) of the Hungarian Civil Code.
[245] *See* § 5:134(2)(a) of the Hungarian Civil Code.
[246] *See* § 5:134(2)(b) of the Hungarian Civil Code.

separately (if the collateral is made of more assets).[247] The only limitation is that the secured creditor may acquire the ownership of the collateral disposed of at a public sale only if that is done through an exchange.[248]

170. ***Fifthly***, the Code imposes the duty on the secured creditor to prepare a written account for the disposal without delays, which needs to contain five classes of information: 1/ identification of the sold collateral, 2/ the price received, 3/ the proceeds collected by the secured creditor, 4/ the costs of safekeeping, maintenance, processing, transformation and disposal, as well as 5/ the ranking of the security interests and the respective claims secured by each (if known by the secured party).[249]

171. It is unclear why does the Code use different standards for, on the one hand, for communicating the intention to dispose of the collateral and, on the other hand, for making the written accounts and their dispatch to the debtor and all the parties entitled to notification. Namely, while – as described above – in case of the former – fixed deadlines apply, in the latter case the Code speaks only of 'without delay'[250] for the preparation of the accounts and it does not fix any specific rule as a deadline for dispatching the information on the accounting.[251]

172. The other part of the duty to account is the duty to distribute the collected moneys according to the priorities of the security interests. First though the disposing secured creditor may deduct from the sales price and the collected proceeds the costs incurred for safekeeping, maintenance, processing, transformation and sales. If there is anything remaining after having paid all the secured creditors, that should be turned over to the debtor.[252]

173. ***Sixth,*** the Code counter-balances the secured creditor's self-help rights by explicitly granting to the debtor, surety and generally to any other person having a legal interest a right to turn to courts for an order suspending the enforcement stage or for ordering enforcement subject to court-formulated conditions. These remedies may in principle be resorted to only in case the secured creditor disregards any of his enforcement-related obligations fixed by the Code.

174. ***A final*** concluding point ought to be added. Namely, the rules on private disposition are obviously the product of a new – but clearly salutary – approach that yields to practical needs, empirical evidences and comparative law in lieu of theoretical considerations. Concretely, besides refining the earlier adapted American concept of

[247] *See* § 5:134(3) of the Hungarian Civil Code.
[248] *See* § 5:134(4) of the Hungarian Civil Code.
[249] *See* § 5:135 of the Hungarian Civil Code.
[250] *See* § 5:135(1) of the Hungarian Civil Code.
[251] *See* § 5:135(2) of the Hungarian Civil Code.
[252] *See* § 5:135(3) of the Hungarian Civil Code.

'commercial reasonableness',[253] the Code took into account the past experiences with the limited predecessors of these legal institutions not requiring court involvement.[254] The provision giving the right to senior secured creditors to take over the already commenced private disposition might be a further encouraging novelty pointing in the right direction.[255]

Collection of Receivables

175. The basic principle is that until the obligor (account debtor) is served with the so-called order to perform ("*teljesítési utasítás*") – or collection order – by the secured creditor, he has to make payments to the debtor.[256]This order needs to identify the secured creditor[257] unless that has already been done with the notification on the "pledging" of the receivables. In other words, though without using such vocabulary and rather resorting to obscure descriptive language, the system aims to recognize both notification and non-notification receivables financing.

176. Thus, when the Code states that the order to perform may be provided together with the notification on pledging,[258] it speaks of indirect (non-notification) receivables financing as the account debtor (obligor) is not informed on the fact that the receivables were used as collateral until default. The same provision allows, however, also for the possibility of notification of the account debtor (obligor) on the "pledging" of the receivables at the time of the creation of the security interest, in which case – if the account debtor was informed on who the secured creditor is – the order to perform may be issued solely by him.[259]

Strict Foreclosure

[253] The standard of commercial reasonableness entered the Hungarian legal system through the Directive 2002/47/EU on financial collateral arrangements (6 June 2002), which was borrowed from the commercial law of the US. *See* Complex Commentary at 470.
[254] For example, as opposed to the earlier version of the Code, now no provision is devoted to joint disposition by debtor and secured creditor because this did not work in practice. *See* Complex Commentary at 468.
[255] *See* § 5:129 of the Hungarian Civil Code. According to this the senior secured creditor may do that through a written declaration addressed to the junior secured creditor (who has already having started disposition) and if he defrays the related costs of the latter. The junior secured creditor, on the other hand, is obliged to appropriately inform the senior creditor of the steps already taken and of the concomitant costs.
[256] *See* § 5:111(1) of the Hungarian Civil Code.
[257] *See* § 5:111(1) of the Hungarian Civil Code. The provision is somewhat ambiguous. Namely, it states that legal entity needs to be identified but specifically mentions only the seat; obviously insufficient for identification. As opposed to that, in case of physical persons the domicile, habitual residence or the identification of the account is required. It is not clear whether the requirement of the identification of the account whereto the moneys are to be transferred is a requirement in case of both, juridical and physical persons.
[258] This follows from § 5:111(2) of the Hungarian Civil Code.
[259] *See* § 5:111(2) of the Hungarian Civil Code.

177. The Code kept the prohibition of *lex commissoria.* Hence, the agreement of the debtor and secured creditor according to which the latter would ***automatically*** acquire ownership on the collateral upon debtor's default – is null and void.[260]

178. However, as a form of out-of-court enforcement, the Code recognizes the validity of ***agreements*** according to which the secured creditor acquires ownership of the collateral as a full or partial substitute of the (payment for the) secured claim, if concluded ***after default***.[261] The system presumes that in that stage the debtor "*is not exposed to the [opportunistic behavior of the] secured creditor anymore and is in the position to make a [learned] decision whether to accept the purchase offer taking into account his own interests*."[262]

179. The resort to this enforcement form is subject to a number of preconditions; some serving the interests of the strategically weaker party, the debtor, and others protecting third parties.

180. The debtor is intended to be protected through rules on the form such strict foreclosure may take: it is not only the secured creditor who must make an offer to purchase the collateral in written form[263] and by specifying all the key components of the offer[264] but the debtor must accept the offer also in **written form** – within a statutory fixed time limit.[265] Besides the debtor, the secured creditor has to notify also other parties of interest on the offer made to the debtor.[266]

[260] *See* § 5:136 of the Hungarian Civil Code.
[261] *See* § 5:137(1) of the Hungarian Civil Code.
[262] *See* Complex Comments at 472.
[263] *See* § 5:137(2) of the Hungarian Civil Code.
[264] As per § 5:137(2) the secured creditor's offer must identify: 1/ the debtor and the secured creditor; 2/ the collateral (for which the offer has been made); 3/ the amount of the outstanding debt secured by the collateral; and 4/ the reason and the time of the default. The offer must specify also 5/ what portion of the secured debt would be extinguished by the strict foreclosure (i.e., acquisition of title/ownership by the secured creditor). Or, in case the price of the collateral would be higher than the debt secured, it should specify what amount of money would be paid by the secured creditor in addition to acquiring the title/ownership on the collateral.
[265] The time within which the debtor may accept such offer is twenty days counted from the receipt of the secured creditor's offer. *See* §5:137(5) of the Hungarian Civil Code.
[266] *See* § 5:137(3) of the Hungarian Civil Code which imposed the duty of notification on the following categories of third parties: 1/ sureties and guarantors as well as the those who have guaranteed performance by these; 2/ secured creditors who have a security interest on the [same] collateral; 3/ all those persons who have rights and interests (proprietary rights) on collateral subject to registration ("*lajstromozott zálogtárgy*"), as well as 4/ all those other who claim to have rights on the collateral and have informed and provided the secured creditor with proofs about that – provided that such information has reached the secured creditor in writing and not later than the 10th day before the offer of the secured creditor.

181. Those third parties who have to be notified by the secured creditor on the intented offer to acquire the collateral may object if that would endanger their secured claims.[267] If the debtor accepts the offer in writing within twenty days and none of the third parties of interest files an objection in writing [also] within twenty days, it will be presumed that a sales contract has been concluded between the debtor and the secured creditor.[268] It is also presumed that the secured debt will extinguish fully or partially as it was specified in the offer of the secured creditor. Based on this the debtor is obliged to transfer the collateral into the possession of the secured creditor and to issue permission for the registration (entry) of the secured party's ownership (in the case of assets for which a system of registration of ownership exists such as immovables).[269]

LITHUANIA:

182. Until the 2011 amendments of the Civil Code, enforcement of security rights was exclusively via courts and court-bailiffs. Changes have been introduced to increase the efficiency of the system in particular by reducing the role of courts to deciding on challenges of the actions of the notary or the bailiffs. Under the new system, the creditor applies to the notary, receives the so-called executive entry, which he can then bring directly to the bailiff for enforcement. The bailiff conducts the enforcement irrespective of whether the debtor cooperates or not. Empirical data are lacking on whether that works well in practice in Lithuania. Out-of-court repossession is illegal in Lithuanial.

183. **Strict foreclosure** is known as well in Lithuania in case of both real property mortgages and pledges of movables.

POLAND:

184. Poland belongs to the Continental European legal tradition and as such is hostile to self-help. Even the Registered Pledge Act – concidered to be a modern statute comparable to the EBRD Model Secured Transactions Law – declares court enforcement to be the rule.[270] Court enforcement is declared also for possessory pledges.[271] Yet this Act has already introduced some steps that represent some limited forms of out-of-court enforcement. A form of self-help was introduced for financial collateral based on EU law.

185. One such out-of-court enforcement method is the transfer of title on the pledged collateral to the secured creditor (strict foreclosure). It can be resorted to if so

[267] *See* § 5:137(4) of the Hungarian Civil Code.
[268] *See* § 5:137(5) of the Hungarian Civil Code.
[269] *See* § 5:137(5) of the Hungarian Civil Code.
[270] *See* Article 21 of the Polish Registered Pledge Act.
[271] *See* Article 312 of the Polish Civil Code.

stipulated by the security agreement, without involvement of courts.[272] The time of the transfer of the title differs for the different classes of collateral.[273] Special rules regulate the determination of the value of collateral in such instances.[274] The Civil Code provides for a similar solution for possessory pledges.[275]

186. While sale of the collateral at a public tender held by a public notary or enforcement officer might also qualify as out-of-court enforcement methods,[276] enforcement of a registered pledge on an economic unit (enterprise or global security)[277] is perhaps the best example corroborating the claim that Polish law has opened the doors to self-help (out-of-court enforcement) quite wide as well. In this process the court gets involved only if the pledgor files a claim for an injunction to prevent enforcement. In practice, normally the security agreement will regulate such receivership (private enforcement) in great detail, moreover, normally at much harsher terms to the debtor than the default rules (compulsory administration) enshrined in the Code of Civil Procedure.[278]

187. Last but not least, enforcement of security assignments is also made outside courts: the assignee (secured creditor) notifies the debtor of the assigned claims that the receivables should be paid directly to him.

[272] *See* Article 22(1) of the Polish Registered Pledge Act.
[273] *See* Article 22.2. of the Polish Registered Pledge Act.
[274] *See* Article 23 of the Polish Registered Pledge Act.
[275] *See* Article 313 of the Polish Civil Code.
[276] *See* Article 24 of the Polish Registered Pledge Act.
[277] *See* Article 27 of the Polish Registered Pledge Act.
[278] The procedure of enforcement by 'compulsory administration' are regulated by articles 1064^{1} through 1064^{13} of the Polish Code of Civil Procedure.

IV SECURITY RIGHTS IN INSOLVENCY

Question 9: Is the secured party affected by a "stay" on the enforcement of security rights if the debtor enters insolvency proceedings?

HUNGARY:

188. Although the position of Hungarian law has fluctuated in the post-1990 on this issue, the law in force does stay the enforcement of security rights in case of both, reorganization and liquidation proceedings. However, the system does not have a comprehensive concept of 'automatic stay' known, for example, to US law. The Hungarian system rather relies on a set of specific provisions which have the effect of stay. Instead of a single broad concept, therefore Hungarian law is based on a set of particular provisions. The underlying philosophy is that*, first*, security interests can be enforced solely as part of liquidation proceedings, *secondly*, the collateral becomes part of the estate and, *thirdly*, the secured parties enjoy a somewhat limited right to ***separate satisfaction within bankruptcy proceedings.***[279]

189. The Hungarian "stay" formula could be said to be made of two building blocks: three forms of moratoria (called "*moratórium*" in Hungarian) and a number of specific rules that have the effect of 'stay.' As far as the latter category is concerned, of special importance is the general rule that enforcement of security rights (including security-bailment) can be effectuated solely within bankruptcy proceedings (both liquidation and reorganization). The starting point of the stay is either the receipt of the notification on the opening of bankrutpcy proceedings by the creditor or the moment when the notice on the commencement of proceedings becomes public.[280]

190. The Hungarian moratorium is a limited device and is nothing more than *extra time for performance* of obligations applicable in the context of both, liquidations and reorganizations with legal consequences.[281] Most importantly, during the moratorium security rights cannot be enforced. In other words, it is not only that the opening of insolvency proceedings stays enforcement of security rights, but – if moratorium arises automatically based on the law (normal moratorium) or if approved either by the bankruptcy court (provisional moratorium) or the majority of creditors (prolonged moratorium) – security rights cannot be enforced while the moratorium is in place either.[282] It causes some unease that the related provisions are somewhat obscure.

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[279] *See* Hungarian Insolvency Handbook, at 760.
[280] *See* § 4/A of the Hungarian Insolvency Act (rules introduced in 2013).
[281] *See* primarily § 11 for reorganizations and §§ 34 – 36 for liquidations; both references are to the Hungarian Insolvency Act.
[282] In the case BH2013. 131, adjudicated by the Curia (Supreme Court), the enforceability of the fiduciary security of 'option to purchase' coupled with a mortgage on an immovable during a moratorium was the issue. As per the holding of the court, although default can be declared, securities cannot be enforced during a moratorium. This includes also the case when default occurred before a moratorium but the security remained unenforced until the declaration of the moratorium.

The overview of the fragmented and thus incomplete substitute of 'automatic stay' could be exemplified[283] as follows:

The Hungarian "Stay"	
Moratorium (extension of time for payment)	**Additional specific provisions exemplified**
A. Within reorganization § 9(1): *provisional moratorium* (if requested by debtor) § 11(1): *normal moratorium* (automatic upon opening the insolvency proceedings) § 18(7): *prolonged moratorium* (if requested by debtor and if approved by the qualified majority of creditors)	**A. Within reorganization** § 8(5): bank cannot enforce on bank account or privilege creditors §9(2): the debtor must add "cs.a." [under reorganization] to its name §10(5): court will reject requests for liquidation automatically
Corollary of moratorium (e.g.,) § 11(1): duty of debtor, administrator, financial institutions where the debtor' accounts are and creditors to refrain from any act that might frustrate the goals of moratorium[284] § 11(2)(a): prohibition of set-off § 11(2)(f): new debt only if approved by administrator	
B. Within liquidation	**B. Within liquidation**
§26(3): court may approve 45 days moratorium if requested by debtor	§ 35(1): all debts become due upon issuance of the decision on opening the proceedings § 38: court enforcement stopped § 49/D: sale of collateral by the administrator

[283] The chart is incomplete and does not contain a full list.
[284] This is similar to the effects of an injunction and also similar to the automatic stay under US law.

A. Reorganizations

191. Three types of moratoria should be differentiated in the context of reorganization. *First,* the **provisional moratorium** (called: "*ideiglenes fizetési haladék*") is granted within one working day by the bankruptcy judge ex parte and is valid from the day it is made public on the website of the Bulletin of Companies ("*Cégközlöny*").[285] Its function is to provide prompt protection to the debtor and is not linked to the opening of the reorganization proceedings but it depends on an application for reorganisation proceedings.[286] As opposed to that, *secondly,* the so-called **'normal'** ("*rendes*") **moratorium** is automatic from the publication of the decision on the opening of insolvency proceedings[287] and is effective for 122 days.[288]

192. *Finally,* the statutory moratorium can be extended by the bankruptcy court though only if approved (counter-signed) by the bankrutpcy administrator[289] and if supported by the qualified majority of creditors.[290] This is the *third* ***extended*** **form of moratorium**.[291] As in case of Hungarian reorganizations an administrator is appointed[292] notwithstanding that the debtor remains in possession (DIP), the majority of creditors may condition the prolongation of the moratorium to subjection of the managerial powers of the debtor's directors to the administrator's approval (couter-signing).[293]

193. Insolvency law tries to make chief executive officers of debtors cooperate with the administrator through monetary fines.[294] The function of the normal and extended forms of moratoria is to give sufficient time for reaching an agreement with the creditors[295] yet it may not be more than 365 days.[296]

B. Liquidations

194. Security rights cannot be enforced by the creditors after the opening of liquidation proceedings, save the so-called security-bailment. In case of the latter, the secured creditor can enforce his security right notwithstanding the opening of the

[285] The moratorium is in principle granted automatically upon filing a related claim by the debtor. The qualification has to be added because it is not fully clear on what bases can the judge refuse grating it. The law says merely that "*unless granting is refused instantaneously*" but it does not specify on what grounds. *See* § 9(1) of the Hungarian Insolvency Act. The literature points to formal deficiencies. *See* Hungarian Insolvency Handbook volume II at 157.
[286] *See* Hungarian Insolvency Handbook, volume II at 157.
[287] *See* § 10(2)(e) of the Hungarian Insolvency Act.
[288] *See* § 10(4) of the Hungarian Insolvency Act.
[289] *See* § 10(4) of the Hungarian Insolvency Act.
[290] *See* § 18(8) of the Hungarian Insolvency Act.
[291] *See* § 10(4) of the Hungarian Insolvency Act.
[292] *See* Hungarian Insolvency Handbook at 224.
[293] *See* § 18(10) of the Hungarian Insolvency Act.
[294] *See* § 13(2) of the Hungarian Insolvency Act.
[295] *See* Hungarian Insolvency Handbook volume II at 170.
[296] *See* § 18(1) of the Hungarian Insolvency Act.

proceedings, however, only if he does that within three months from the opening of the proceedings.[297] After that period his security right will be treated as other securities: i.e., the insolvency administrator will enforce them, deduct the amounts recognized by the Act (e.g., costs for the safekeeping or sale of the collateral, as well as the fees of the administrator) and will distribute the rest to creditors in accordance with their entitlements.[298]

LITHUANIA:

195. Although the law does not use the term 'stay,' rules having such effect do exist in case of court-run bankruptcy proceedings initiated against business enterprises. These presume first and foremost transfer of the management of the bankrupty enterprise into the hands of the court-appointed bankrutpcy administrator.[299] This includes also collateral and as the system provides for the enforcement of security rights primarily through the administrator, the stay affects also the security rights.

196. Moreover, acquitision (taking over) of the collateral by the secured creditor – as an alternative method to sales – may be exercised only if approved by the meeting of creditors after a failed auction.[300] In other words, private enforcement of security rights is unknown to Lithuanian law and all enforcement procedures take place as part of the insolvency proceedings.

197. The other rules having the effect of 'stay' include, in particular:
1/ the prohibition (to creditors and other persons) otherwise than in accordance with the Bankruptcy Act to manage and dispose of the assets of the bankrup company;[301]
2/ third parties holding the assets of the debtor are prohibited from entering into any transactions with third parties related to these assets;[302]
3/ court proceedings against the bankrupt company in other courts are stopped;[303]
4/ all debts become due[304] and
5/ bailiffs (enforcement officers) have to transfer to the bankruptcy court all the enforcement cases in process.[305]

POLAND:

[297] *See* § 38(5) of the Hungarian Insolvency Act.
[298] *See* § 49/D of the Hungarian Insolvency Act. Somewhat different rules apply for shifting securities (*see* § 49/D(2)).
[299] *See in particular* Article 10.7(1) and (2) of the Lithuanian Enterprise Insolvency Act.
[300] *See* Article 33(6) of the Lithuanian Insolvency Act.
[301] *See* Article 14.1(1) of the Lithuanian Enterprise Insolvency Act. The bankruptcy administrator is appointed by the bankruptcy court as per Article 10.4(1) of the Act.
[302] *See* Article 14.1(2) of the Lithuanian Enterprise Insolvency Act.
[303] *See* Article 15.1. of the Lithuanian Enterprise Insolvency Act,
[304] *See* Article 16 of the Lithuanian Enterprise Insolvency Act.
[305] *See* Article 18.1. of the Lithuanian Enterprise Insolvency Act.

198. **Given the separation of the insolvency (liquidation) and restructuring laws in 2015, we will separately discuss them.** Both know for a stay yet with variations in their contents.

199. As far as the Insolvency Law is concerned, once insolvency proceedings are opened, the debtor has to transfer all of its assets to the insolvency practitioner[306] because they automatically convert into and become part of the bankruptcy estate.[307] Based on explicit provisions, ongoing enforcement proceedings must be stayed.[308] The proceeds collected from disposition of certain collateral by the bankrupt but which have not been transferred to the creditors as of the date of the opening of the insolvency proceedings, will not become part of the estate.[309] The novelty introduced by the 2015 amendment is that the secured creditor's priority of satisfaction on proceeds from the sale of a collateral (whether sale occurred prior to or during the insolvency) will survive the opening of the insolvency procedure.[310]

200. Another important feature of the system is that Polish insolvency law knows not the private enforcement of security rights in the context of insolvency proceedings and thus security rights can be enforced only by insolvency practitioners or exceptionally as approved by the bankruptcy court.

201. This concretely means, that if the registered pledge (i.e., security) agreement does not provide for any out-of court enforcement methods, it is for the insolvency practitioner to sell the collateral, in which case the pledgee will have priority to the proceeds of sale. If the pledge agreement provides for out-of court enforcement methods, only strict foreclosure or sale at public auction may be resorted to by the pledgee in insolvency.[311]

202. The insolvency judge may set a deadline to exercise strict foreclosure by the pledgee; upon the expiry of which the collateral is sold by the insolvency practicioner. This is linked to the mandate of the insolvency practitioner to take control of the bankruptcy estate and start administering it immediately upon opening the proceedings.[312]This power extends also to the collateral though law has specific rules

[306] *See* Article 57(1) of the Polish Insolvency Act. Note that with the passage of the new Restructuring Law (April 2015) this rule will apply only in case of liquidation proceedings. Under the new Restructuring Law, except the rehabilitation proceedings, all types of restructuring proceedings are debtor-in-possession type of proceedings.
[307] *See* Article 61 of the Polish Insolvency Act.
[308] *See* Article 146 of the Polish Insolvency Act.
[309] *See* Article 63(1)(3) of the Polish Insolvency Act.
[310] *See* Article 146(2a) of the Polishy Insolvency Act.
[311] *See* Article 327(1) of the Polish Insolvency Act.
[312] *See* Article 173 of the Polish Insolvency Act. Note that with the passage of the new Restructuring Law (April 2015) this rule will apply only in case of liquidation proceedings.

for enforcement of possessory securities, i.e., collateral that are possessed by the creditor or third party at the time of the opening of the bakruptcy.[313]

203. As far as the 2015 Restructuring Act is concerned, different rules apply to the various restructuring alternatives. While there is no stay in case of pre-packaged arrangements, enforcement is stayed in case of rehabilitation proceedings.[314] As opposed to these, rules similar to the ones described above on insolvency proceedings apply to the arrangement and the accelerated arrangement proceedings. This means that the secured creditor may enforce its security interest but only from the collateral[315] notwithstanding that there is a stay on enforcement proceedings.[316]

204. The security rights are affected by the "stay" also in respect of interests. While the general rule is that interests stop to run with the opening of insolvency proceedings, that is not the case of security rights. However, they are limited to the proceeds that may be obtained from the sale of the collateral.[317]

Question 10/11: Can the secured party apply to have any stay lifted? Under what circumstances can the stay be lifted?

HUNGARY:

205. It seems that under Hungarian law there is no such possibility and getting paid from the collateral is always to occur within the context of insolvency proceedings.[318]

206. The only exception seems to be the security-bailment ("*óvadék*"), which due to its very nature – especially the nature of the collateral – ought to be treated differently. However, in this case, the right to enforce the security right is not dependent on any special approval either by the administrator or the bankruptcy court.[319] This is, in other words, rather a form of private realization (out-of-court enforcement) than an example of stay being lifted. As a result, there seems to be a conflict between the general rule that all security rights must be enforced within insolvency proceedings and the said right to directly realize the security-bailment by the secured creditor; or it is not fully clear what is exactly meant under "*to be enforced exclusively within insolvency proceedings*." According to Juhasz, a leading expert on Hungarina insolvency law, given that the provisions on the security-bailment are specific (lex specialis), they apply rather than the general rule.[320]

[313] *See* Article 327(2) of the Polish Insolvency Act.
[314] Article 312(1) of the Polish Restructuring Law.
[315] Articles 278-79 of the Polish Restructuring Law.
[316] Article 259(1) of the Polish Restructuring Law.
[317] *See* Article 92(2) of the Polish Insolvency Act.
[318] *See* § 4/A of the Hungarian Insolvency Act.
[319] For liquidations *see* § 38(5) of the Hungarian Insolvency Act. In case of reorganization, the exception is narrower as it applies only to netting transactions on the capital markets and among a group of qualified entities. *See* §11(2)(d).
[320] *See* Hungarian Insolvency Handbook, at 92.

207. This possibility is however, subject to some restrictions. In particular, the secured creditor must account for the surplus with the administrator. Furthermore, he can exercise this direct-enforcement method only within three months from the day the decision on the opening of the liquidation proceedings has been publicized. Moreover, if the secured creditor is a person controlled by the debtor, this enforcement avenue is not available as in such cases the collateral must be handed over to the administrator immediately upon the commencement of the case.[321]

LITHUANIA:

208. Lifting the "stay" and allowing secured creditor to enforce a security right outside the context of insolvency proceedings is not possible. In other words, enforcement of secured transactions is completely entrusted to the administrator. The system foresees the same process for all kinds of pledged and mortgaged assets.[322]

209. The basic disposal method is via auctions; the secured creditors must be informed about them.[323] The secured creditors may acquire the collateral only if the auction has proved unsuccessful and they wishe to acquire the collateral. From the collected funds, first the administrative expenses[324] will be deducted and then they must be credited – no later than 10 days from the date of receiving the price – to the respective creditor's account.[325] The secured creditors are paid in priority from the funds obtained from the sale of the collateral. In respect of the unpaid part they are treated as unsecured creditors.[326]

210. For quasi-securities (leasing and retained title), no specific rules are laid down in the Act on Enterprise Insolvency. Thus, the generally applicable enforcement rules, as supplemented by private law, will apply. In case of leasing, thus, the Civil Code comes first into the picture because the Insolvency Act introduces the principle that the rights of creditors granted by other laws remain intact to the extent they do not contradict any provisions of the Insolvency Act.[327]

211. Further, the administrator has the duty to inform the creditors whether he intends to perform executory contracts or whether he will reject them.[328]

[321] *See* § 38(5) of the Hungarian Insolvency Act.
[322] This follows even from the definition of "*creditors' claims secured by a pledge and/or mortgage*" in Article 2.7. of the Lithuanian Enterprise Insolvency Act.
[323] *See* Article 33.6. of the Lithuanian Enterprise Insolvency Act.
[324] *See* Article 36 on administrative expenses of the Lithuanian Insolvency Act.
[325] *See* Article 33.6. of the Lithuanian Enterprise Insolvency Act.
[326] *See* Article 34 of the Lithuanian Enterprise Insolvency Act.
[327] *See* Article 1.3. of the Lithuanian Enterprise Insolvency Act.
[328] *See* Article 10.7(4) of the Lithuanian Enterprise Insolvency Act.

212. According to the Civil Code retained ownership (title) in case of leasing contracts is looked upon as ownership rather than a mere security right, and therefore the owners are entitled to get back their property.[329]

POLAND:

213. As far as insolvency proceedings are concerned, the general rules is that stay cannot be lifted on enforcement proceedings.

214. However, as already hinted at above, certain methods of private enforcement of *registered pledges* are exempted from this general rule explicitly. If the underlying security agreement so provides, the creditor may take over (acquire) the collateral or turn to public notaries or bailiffs for disposal – as provided for by the Act on Registered Pledges.[330] However, if the collateral is in the possession of the insolvency practitioner, engagement of notaries or bailiffs is not possible anymore.

215. As far as the new 2015 Restructuring Law is concerned, given that enforcement of security interests in prepackaged and accelerated arrangements as well as arrangment proceedings is not stayed, questions 10/11 are not applicable to them. As opposed to these, in case of rehabilitation proceedings it is not possible to lift the stay on enforcement proceedings.[331] This comes as a surprise because possibility to lift the stay exists even in insolvency proceedings.

Question 12: In insolvency proceedings, can an Insolvency Practitioner enforce security, i.e., realise the secured assets without the consent of the secured party?

HUNGARY:

216. The distinctive solution of Hungary is that, indeed, the administrator (Insolvency Practitioner) can do that,[332] though this question may arise only in case of liquidations in Hungary. The system sets as the basic rule that the creditors – including secured parties – must file their claims to the Insolvency Practitioner within the fixed period of time of 40 days from the day of the publication of the decision on the opening of the liquidation proceedings. Claims filed within this 40 day period enjoy full recognition. As oposed to that the claims filed after 40 but before 180 days will be listed, however, will

[329] On the dilemmas and case law on leasing and retained title in Lithuania *see* Lina Aleknaite, *Leasing in Lithuania, in:* Stefan Messmann and Tibor Tajti (eds.), *the Case Law of Central and Eastern Europe – Leasing, Piercing the Corporate Veil and the Liability of Managers & Controlling Shareholder, Privatization, Takeovers and the Problems with Collateral Laws* (Eur. Univ. Press, Bochum-Germany, 2007), at 240-263 [hereinafter: Aleknaite – Leasing in Lithuania].
[330] *See* Article 327(1) of the Polish Insolvency Act.
[331] Article 312(1) of the Polish Restructuring Law.
[332] *See, e.g.,* Catherine Bridge, *Insolvency Office Holders: A new Study by the EBRD Provides Insight into Creditors' Rights in Insolvency, in:* Law in Transition (EBRD, October, 2014), p. 9.

be paid only if assets remain after preferential and secured creditor claims filed within the 40 day period.[333]

217. The same treatment applies also to secured claims, who also must file their claims within 40 fourty days from the publication of the decision on opening liquidation proceedings.[334] If the claim was filed with the administrator in time, the administrator will dispose of the collateral, deduct the preferential administrative expenses (i.e., costs of safekeeping, preservation of the collateral, as well as of enforcement and administrator's fee) and then will pay the secured party *without delay.*[335]

218. Now, in the situation when the secured party fails to file its claim within the statutory 40 days deadline, the administrator may sell the collateral – or as the language of the statute says: "*this is not an obstacle of the sale.*" In other words, the administrator may sell the collateral without the consent of the secured party given that the failure to file the claim obviously denotes lack of consent. In such a case, however, the administrator has to segregate the so collected moneys but can pay the secured creditor only if after having paid all the costs of liquidation, all secured creditors and a number of other preferential claims[336] there are still funds available for distribution.[337] Different rules apply though in case settlement is reached within liquidation.[338]

LITHUANIA:

219. There are no explicit provisions on this issue in the Lithuanian Act on Enterprise Insolvency.

220. There are however, broad powers granted to the creditors meeting with respect to, on the one hand, the continuation of the economic activities of the bankrut entity and, on the other hand, imposition of restrictions on the disposal with the assets of the enterprise,[339] and these may extend also to restricting the use and disposal with the collateral.

POLAND:

221. As in restructuring proceedings the arrangement does not extend to secured claims (i.e., mortgage, pledge, registered pledge, tax lien or maritime lien), unless the

[333] *See* § 37(1) of the Hungarian Insolvency Act.
[334] *See* § 28(2)(f) of the Hungarian Insolvency Act.
[335] *See* § 49/D(1) of the Hungarian Insolvency Act.
[336] *See* § 57(1) of the Hungarian Insolvency Act. *See also* § 57(2) for what qualifies as costs of the liquidation proceedings.
[337] *See* § 37(1) of the Hungarian Insolvency Act
[338] *See* § 37(1) of the Hungarian Insolvency Act.
[339] *See* Article 23.6 of the Lithuanian Enterprise Insolvency Act.

secured creditors consents,[340] the only instance where the insolvency practitioner may realise the assets contrary to the will of the secured creditor is the following – and applies only to insolvency proceedings. Namely, as Polish law prefers sale of the bankrupt debtor's enterprise as a whole rather than in a piecemeal manner, when it is more profitable to realize an individual security by selling the entire enterprise, or of an organized part of an enterprise, rather then enforcing each security independently, then the previous method will be given preference notwithstanding the desires of the secured party. In such a case however, the value of the asset subject to registered pledge must be put aside for the benefit of the secured party.[341]

Question 13. Are there are any conditions that must be satisfied before an IP may 'enforce' the security?

HUNGARY:

222. Presuming that the collateral still exists, besides the obvious requirement that the creditor must have a valid and recognized claim, the law imposes two further requirements on the enforcement of the security: duty to file the claim with the Insolvency Practitioner and payment of a registration fee.[342] These preconditions apply both to reorganization and liquidation proceedings though subject to somewhat differing rules mainly due to the distinct nature of the two proceedings.

223. Most importantly, while in case of liquidations the secured creditors must file their claims with the Insolvency Practitioner within 40 days from the publication of the decision on the opening of the liquidation proceedings,[343] in case of reorganizations the deadline is 30 days for pre-reorganization claims and 8 days for those that come into being after the opening of the reorganization proceedings.[344]

224. As far as the payment of the so-called registration (filing) fee ("*regisztrációs díj*") is concerned, in case of liquidations this is equal to 1% of the principal amount of the claim, which cannot be less than 5.000 and more than two-hundred thousand HUF. Evidence that the fee has been paid must be presented to the administrator.[345] In case of reorganization, only the upper limit is different and is one-hundred-thousand HUF.[346]

LITHUANIA:

225. *First,* the secured creditors must file their claims with the administrator within the time set by the bankruptcy court (may be maximum 45 days)[347] and the bankruptcy

[340] Article 151(2) of the Polish Restructuring Law.
[341] *See* Article 330 of the Polish Insolvency Act.
[342] *See* Hungarian Insolvency Handbook, at 770.
[343] *See* § 37(1) of the Hungarian Insolvency Act.
[344] *See* § 10(2)(f) of the Hungarian Insolvency Act.
[345] See § 46(7) of the Hungarian Insolvency Act.
[346] *See* § 12(1) of the Hungarian Insolvency Act.
[347] *See* Article 10.4(5) of the Lithuanian Enterprise Insolvency Act.

court must approve them within 45 days from the receipt of the list from the administrator.[348]

226. *Secondly,* secured creditors contribute together with all other creditors. Although not stated explicitly in the Act, normally once a creditor's claim is approved, administration costs are distributed pro-rata to all creditors depending on the size of their claims and then deducted before payments are made to creditors. Administration costs shall be paid from all funds of the company, including the moneys received after sale of collateral.[349] Namely, it is the creditors meeting that has the powers to determine '*the sequence and procedure for covering administrative expenses*.'[350] If that is not requested, these will be deducted by the administrator upon the disposition of the collateral before transferring the price collected to the secured creditor.[351]

POLAND:

227. Besides the existence of a properly constituted (perfected) security right, the Polish Insolvency Act as well requires the listing of the secured claim. The system is peculiar, however, in that it explicitly declares that the claims of secured creditors are listed ex officio notwithstanding of what the secured creditors have the right to file.[352] This seemingly redundant provision aims to allow for active participation of the secured creditor in case of disagreement with the insolvency administrator. Employees are the other such privileged class of creditors with equal entitlements.

228. The preconditions are logically most onerous if the entire enterprise, or organized part thereof, is the collateral. In such cases, *first,* the value of the enterprise-as collateral, as well as the value of any individual security rights that exist must be determined by experts.[353] *Secondly,* the public auction or tender must be confirmed by the bankruptcy judge before the insolvency practitioner may start disposition (e.g., notification).[354]

Question 14. Do the rules or conditions differ depending on the nature of the insolvency proceedings in question?

HUNGARY:

[348] *See* Article 26.1 of the Lithuanian Enterprise Insolvency Act.
[349] *See* Article 36 of the Lithuanian Enterprise Insolvency Act.
[350] *See* Article 23.5 of the Lithuanian Enterprise Insolvency Act.
[351] *See* Article 33.6 of the Lithuanian Enterprise Insolvency Act. The administrative expenses have to be paid in also in case the asset are acquired by secured creditors after unsuccessful auctions as per the same provision.
[352] *See* Article 236(2) of the Polish Insolvency Act.
[353] *See* Articles 318 and 319(3) of the Polish Insolvency Act.
[354] *See* Article 320(1) of the Polish Insolvency Act. The 2015 amendment to the Insolvency Act discarded the possibility of disposition outside of the public tender process with the approval of the bankruptcy judge (Article 326 of the old Act was deleted).

229. Even though both reorganization and liquidation are centralized and no private enforcement of security rights is known under Hungarian law (save bailment-securities), the fate of security rights differ under the two regimes.

230. In case of reorganizations, no security right can be enforced with the exception of security-bailments granted to specific participants in capital markets while a provisional or normal moratorium is in force.[355]
231. If the secured creditor's claim has been filed and recognized by the administrator and he has paid the due registration-fees, he will have a right to vote on the reorganization plan.[356] The affirmative vote of the majority of both, secured and unsecured classes should be acquired for prolongation of the moratorium for 240 days.[357]

232. As opposed to that, in case of liquidations, if the claim was filed within the prescribed 40 days with the liquidator, the secured claim will be separately satisfied. This means that the liquidator will sell the secured assets and then, after deduction of preferential administrative expenses and its fee, the price will be forwarded to the secured party. If the claim was filed late, the collateral will be nonetheless sold but the ranking of the claim will significantly fall – as already described above under points 12 and 13.

LITHUANIA:
233. The enforcement of security rights theoretically are subject to the same regime, i.e., sale by the administrator at auctions.

234. As a supplementary method, the secured party may, if he so desires, acquire the collateral, however, only if the auction has failed for specified reasons.[358] These rules are contained in a chapter that applies to the '*bankruptcy process*'[359] that extends to both judicial and out-of-court bankruptcy procedures. In other words, the system foresees this as the only enforcement method applicable to all types of recognized insolvency proceedings. Moreover, these rules apply even to out-of-court settlements of creditors as a separate nominated insolvency proceeding type, given that no specific enforcement rules are contained in this respect in the Act.[360]

[355] The list includes the Hungarian and the national banks of other EU Member States, banks and various other financial organizations. For the list *see* § 11(3) of the Hungarian Insolvency Act.
[356] *See* § 18(4) of the Hungarian Insolvency Act.
[357] *See* § 18(8) of the Hungarian Insolvency Act.
[358] *See* Article 33.6 of the Lithuanian Enterprise Insolvency Act.
[359] *See* the title of Chapter Eight devoted – besides sale of assets of the bankrupt entity – also to satisfaction of creditors' claims in the course of the bankruptcy process. The **bankruptcy process** is defined as "*the totality of judicial or extrajudicial enterprise bankruptcy procedures*."
[360] *See* Article 13.1. of the Lithuanian Enterprise Insolvency Act.

POLAND:

235. The old 2003 Act contained no special enforcement rules for reorganization except what follows from the nature of such proceedings. In other words, the reorganization plan did not affect the secured party unless it chose to participate. For example, a security right could have been waived, changed or replaced[361] as a measure to contribute to the success of the restructuring, however, only if consented by the secured creditor. In other words, collateral was included in the reorganization plan only if the affected secured party agreed.

236. Thus, security rights were enforced as in case of liquidations: unaffected by the plan unless the reorganization plan provides for taking over (acquisition) of collateral by creditors[362] or for waiver, modification or change of the security right. This approach was taken over by the Restructuring Act as well.[363] The new 2015 Restructuring Act's basic principle is therefore that none of the arrangement proceedings extend to secured claims.[364]

Question 15. Is a secured party liable to pay the general costs i.e. costs apart from those incurred in connection with the realisation of security, of insolvency proceedings affecting the debtor?

HUNGARY:

237. The system makes participation in the insolvency proceedings (both reorganization and liquidation) contingent on payment of a registration fee in addition to the costs deductable for the safekeeping, preservation and sale (collection) of the collateral (if any).

238. **In case of reorganizations**, the failure to file (and prove) the claim as well as *the failure to pay the registration fee* results in the refusal of the registration of the claim (creditor).[365] The registration fee is 1% of the registered claim, though not less than 5,000 HUF and not more than 100,000 HUF.[366] According to the law the fees have to be kept on a separate account by the administrator, who can spend the money only for the costs incurred by him and for his remuneration. Moreover, if the moneys collected as registration fees are insufficient to cover the costs and remuneration of the administrator, it is the debtor who has to cover the difference.[367]

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[361] Article 270.1(5) of the Polish Insolvency Act was repealed from the Polish Insolvency Law with the 2015 changes. The (identical) rule was moved to Article 156(1)(5) of the Restructuring Law.
[362] *See* Article 271 of the 2003 Polish Insolvency Act, repealed by the 2015 Restructuring Law,
[363] Article 156(1)(5) in connection with Article 151(2) of the Restructuring Law.
[364] Article 151(2) of the Restructuring Law.
[365] *See* § 12(1) of the Hungarian Insolvency Act.
[366] *See* § 12(1) of the Hungarian Insolvency Act.
[367] *See §* 12(1) of the Hungarian Insolvency Act.

239. Two tools aim to control spending by the administrator. On the one hand, the administrator has to prove all such costs with invoices and the creditors' committee or creditor representatives are entiteld to check the spending (if neither is in place, then the checking is done by the bankruptcy court).[368] On the other hand, all expenditures of the administrator must be proven by invoices. As in case of reorganizations security rights normally are not enforced (rather the system reckons with secured parties giving up something in order to rescue the bankrupt debtor), the registration fee is entirely spent on the general costs of the proceedings.

240. Even though sale of the collateral is the normal corrollary of **liquidations** (the costs of which are deducted from the price so received), the secured party is expected to contribute to the general costs of the liquidation proceedings as well. This is 1% of the claim, or at least 5,000 HUF or maximum 200,000 HUF.[369] Irrespective that the so paid in fee is then listed as a recognized unsecured claim (though with a very inferior ranking position)[370] and theoretically the creditors could regain it, as in most liquidation cases there is insufficient money available to pay unsecured creditors, normally these are lost.

LITHUANIA:

241. Yes. The Insolvency Act pronounces this as a general rule and says that the administrative expenses will be paid first of all from any types of funds available to the bankrupt entity – including pledged assets.[371] Then, through explicit language adds that the administrative expenses are to be deducted by the bankruptcy administrator from the proceeds of the sale of the collateral before transferring anything to the secured creditor. If the assets are not sold but are acquired by the secured parties, they have to pay the administrative expenses as well.[372]

POLAND:

242. As per the Insolvency Act the secured creditor has to cover from the proceeds of the sale of the collateral two types of costs: 1/ the costs of the disposal of the collateral; and 2/ the general costs of the insolvency proceedings. However, the latter is limited by two cumulatively applicable criteria: on the one hand, the costs deducted may not be more than one-tenth (1/10) of the proceeds generated by the sale of the collateral, and on the other hand, that amount may not exceed the amount that would be proportionate to the ratio of the value of the collateral versus the value of the entire estate.[373]

[368] *See* § 12(1) of the Hungarian Insolvency Act.
[369] *See* § 46(7) of the Hungarian Insolvency Act.
[370] *See* § 46(7) of the Hungarian Insolvency Act. For the ranking of residual category of unsecured claims – named: other claims ("*egyéb követelések*") – into which the registration fees fall, *see* § 57(1)(f).
[371] *See* Article 36.1 of the Lithuanian Enterprise Insolvency Act.
[372] *See* Article 33.6 of the Lithuanian Enterprise Insolvency Act.
[373] *See* Article 345(1) of the Polish Insolvency Act.

243. The debtor has to cover the costs of restructuring proceedings under the new 2015 Restructuring Law.[374]

Question 16. Is the secured party liable to 'set aside' any portion of the amount realised from the enforcement of security, for the benefit of (a) preferential or (b) unsecured creditors of the debtor?

HUNGARY:

244. Save the narrow exception of security-bailment, Hungarian insolvency law does not recognize private enforcement of security rights. Hence, it is the liquidator who has to set aside portions of the amount realised from the enforcement of security. Moreover, this applies only in case of floating securities, or – after 15 March 2014 when the new Civil Code came into force in this respect and discarded the earlier nominated property-encumbering (enterprise or floating) charge – when the collateral is "*identified by description*" and when the security right "*extends to all assets registrable in the register of security rights [on movables, rights and claims].*"[375]

245. In such cases, after having deducting the costs of the sale of the collateral, the liquidator may apply no more than 50% of the collected moneys *exclusively* for the payment of the secured claim (principal, contractual interest and concomitant costs); presuming the security right was constituted before the commencement of the proceedings.[376] If the collected funds are insufficient to fully pay such secured creditor, the claim for the residue will rank after administrative expenses. This is obviously still a high priority position but still it ranks after the administrative expenses.

246. The Hungarian system also provides for an idiosyncratic solution aimed at punishing insiders. Namely, these rules do not apply if the secured party was either a director, officer (as well as a close relative, life partner of these or – in case of juridical persons – was controlled by the debtor)[377] or a controlling shareholder[378] of the debtor. The security rights of these creditors will not benefit from separate enforcement. Rather, their claims will be treated as mere unsecured claims with an extremely inferior ranking position.[379]

LITHUANIA:

[374] Article 208(1) of the Restructuring Law.
[375] *See* § 49/D(2) Insolvency Act.
[376] *See* § 49/D(2) Insolvency Act.
[377] *See* § 49/D(4) Insolvency Act.
[378] *See* § 49/D(5) Insolvency Act.
[379] *See* § 57(1)(h). In fact, besides all the administrative costs (§ 57(2) – including but not limited to unpaid wages and other wage-like obligations, all costs corollary to the preservation of the estate and completion of the production of the debtor, costs of the sale of the estate's assets, costs of various liquidation-related court and administrative proceedings, costs imposed by data protection laws), all the other secured and unsecured claimants will enjoy priority.

247. This question does not arise in the context of Lithuanian insolvency law because enforcement of security rights is exclusively done by bankruptcy administrators. In other words, it is the task of the administrator to collect the administrative expenses.

248. As stated above (see previous question), the administrator will deduct the administrative expenses – as approved by the creditors' meeting – from the moneys received from the sale of the collateral before transferring any moneys to the secured party.[380] However, as the creditors' meeting is empowered to decide on the sequence and procedure for covering administrative expenses,[381]there is the possibility that the administrator will be instructed to request advances from secured creditors though no such practice seem to have emerged in the country.

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POLAND:

249. The basic principle is that moneys collected from the sale of collateral are reserved for the secured creditors; only the surplus becomes part of the estate.[382] However, through specific rules secured creditors are obliged to put aside certain percentage of the collected funds to cover the costs of enforcement and to contribute to general costs of the proceedings.[383] (See the details under Question 15 above). The novelty introduced by the amended 2015 Insolvency Act is that, as explicitly pronounced, if the collateral generates income, such income becomes part of the estate and is not reserved for the secured creditor.[384]

250. Such (or similar) situation arises only in case of enforcement of security right on an enterprise, or an organized part thereof. In such cases, namely, an evaluation has to be made not only of the value of the enterprise-collateral but also of the individualized specific assets encumbered by a mortgage, pledge or registered pledge. The function of such valuation is to determine a/ which of the securities will remain in effect after sale; b/ what their value is, and c/ the ratio of the value of the individual collateral versus the value of the enterprise.[385] Yet this is not a case of setting aside moneys for preferential or unsecured creditors.

Question 17. Can the secured party be bound against its wishes by a restructuring plan that negatively affects either the secured debt or the enforcement of the security interest?

[380] *See* Article 33.6 of the Lithuanian Enterprise Insolvency Act.
[381] *See* Article 23.5 of the Lithuanian Enterprise Insolvency Act.
[382] *See* Article 336.1 of the Polish Insolvency Act.
[383] *See* Article 345 of the Polish Insolvency Act.
[384] Article 336(3) of the amended Polish Insolvency Act.
[385] *See* Article 319(4) of the Polish Insolvency Act.

HUNGARY:

251. The Insolvency Act explicitly mentions the term 'forced agreement' ("*kényszeregyeszség*")[386] because of why it could be validly claimed that the system recognizes a version of **cramdown**. These rules apply generally and not only related to secured creditors.

252. The following features of the system are determinative here. The ***first*** – explicitly stated rule – is that the reorganization plan applies also to those *registered* creditors – both secured and unsecured – that have not consented to the plan or have failed to participate at the related proceedings (notwithstanding of having been properly summoned). The same applies to creditors with disputes claims.[387] Here, it is irrrelevant what reasons led the secured creditor reject the restructuring plan or not to participate at voting. However, through an explicit rule, these creditors are protected because the plan cannot impose on them terms and conditions that would be more onerous than the ones applicable to creditors of the same class.[388]

253. ***Secondly****,* the system tries to provide protection to all classes of creditors. As far as voting is concerned, the plan is accepted not if the majority of all the creditors votes for it but rather if the majority of each of the classes (secured and unsecured) in terms of valuce casts an affirmative vote.[389] Theoretically thus neither the secured nor the unsecured creditors can impose the plan against the wishes of the other classes. Note, however, that this applies to the class as a whole what does not exclude the possibility that some individual creditors may lose out.

254. ***Thirdly****,* besides this voting arrangement, the act adds another balancing tool to ensure that none of the classes could impose its position on the other. This tool, however, rests on pretty vague grounds given that – relying on the good faith principle – it proclaims that the restructuring plan may not contain provisions that *obviously or conspicuously* disadvantages all the creditors or only some specific classes.[390]

255. ***Fourthly****,* the decisions ideally leading to the acceptance of the restructing plan are all passed by the *majority* of the classes – both secured and unsecured classes[391] – of creditors. In other words, the position of individual secured creditors is sacrificed in the hope of an easier approval of the plan. This notwithstanding that voting census

[386] *See* § 20(2) of the Hungarian Insolvency Act.
[387] *See* § 20(2) of the Hungarian Insolvency Act.
[388] *See* § 20(2) of the Hungarian Insolvency Act.
[389] *See* § 20(1) of the Hungarian Insolvency Act.
[390] *See* § 20(1a) of the Hungarian Insolvency Act.
[391] The plan is accepted if the majority of each of the classes is obtained. In other words, the majority of unsecured creditors cannot impose on the secured creditors the plan against their wishes. *See* § 20(1) of the Hungarian Insolvency Act.

is established proportionately to the value of recognized claims: one full vote is attributed to each fifty-thousand HUF of recognized claims.[392]

256. ***Fifth,*** not only that the plan will not apply to the the individual creditor who did not participate in the conclusion of the restructuring plan because of a failure to file the claim within the statutory deadlines (i.e., non-registered creditors), but he will additionally lose his enforcement rights as well.[393] In such cases the only possibility for realization of his security right is through filing his claim in *liquidations* proceedings initiated by another creditor and only if the statute of limitations have not run out for his claim.[394] With this the system obviously aims to incentivize creditors not only to file their claims but also to participate in reorganization proceedings.

257. ***Last but not least****,* the creditor dissatisfied with the reorganization plan, may file an appeal (within 8 days from the receipt of the court's decision approving the reorganization plan or – if the decision was publicized through internet – from the date of the second such announcement).[395] In such case, the bankruptcy court will pass a decision[396] yet already primarily based on the generally applicable rules on enforceability of agreements in the Civil Code.[397]

LITHUANIA:

258. The Lithuanian Act on Enteprise Insolvency contains provisions for a loosely regulated settlement (literally: peace agreement) when the creditors agree with owners (shareholders) that the insolvency proceedings should not be completed.[398] This requires the consent of affected creditors.[399] The bankruptcy court has the task of checking whether the legally guaranteed rights and interests are dully recognized.[400] Hence, unless the secured party consents, his security interest or his enforcement rights may not be negatively affected. Lithuanian law, contains no provisions for cramdown. This includes even out-of-court settlement proceedings because they are also subject, unless otherwise explicitly stated, to the Insolvency Act.[401]

259. However, as the creditors' committee is empowered to appraise and fix the selling price of the collateral[402] and as sale is by auction, and if too high price is fixed, that may prolong the process of sale.

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[392] *See* § 18(5) of the Hungarian Insolvency Act.
[393] *See* § 20(3) of the Hungarian Insolvency Act.
[394] *See* § 20(3) of the Hungarian Insolvency Act.
[395] *See* § 21/C(3) of the Hungarian Insolvency Act.
[396] *See* § 6(7)(a) of the Hungarian Insolvency Act.
[397] *See* the decision of the Curia in the case BH2013. 131. Stating that a reorganization plan is null and void if it does not treat creditors equally. Concretely, in the case the reorganization plan gave a freedom to the debtor to unilaterally fix different dates at which various creditors would be paid.
[398] Only the relatively short Articles 28 and 29 regulate composition.
[399] *See* Article 28.2 of the Lithuanian Enterprise Insolvency Act.
[400] *See* Article 29.3 of the Lithuanian Enterprise Insolvency Act.
[401] *See* Article 13.1 of the Lithuanian Enterprise Insolvency Act.
[402] *See* Article 23.5 of the Lithuanian Enterprise Insolvency Act.

260. The procedure of company restructuring in Lithuania is regulated by the Law on Restructuring of Companies. According to this law, the restructuring plan is adopted if creditors with a value of claims that comprises 2/3 of the value of all claims approved by the court vote in favor of it.[403] The plan is binding on all creditors.

261. However, it is only a right and not an obligation of the creditor to assist the debtor regarding his debts. A creditor may, in particular, agree on postponement of payment or performance of obligations, to write off fully or partially claims, to accept performance in kind instead of payment of moneys.[404] Therefore such assistance can be included in the restructuring plan upon consent of the creditor. Otherwise, creditor claims are satisfied in accordance with procedure specified in the law. Once collateral is sold, the secured creditor receives the proceeds. For the remainder of the claim, the creditor is treated the same way as unsecured commercial creditors.

262. If the restructuring plan does not envisage the sale of collateral, than an opinion on the value of collateral by an independent appraiser must be obtained. In such case secured creditors are paid together with first ranking creditors (employees), but only the amount up to the approved value of the collateral. If that is not sufficient to cover the claim, for the remainder of the claim they are treated same as unsecured commercial creditors.[405]

POLAND:

263. As per the new 2015 Restructuring Act that is not possible.

264. This means that the basic rule is that the secured claim is not subject to the restructuring plan unless the secured party consents to this, unconditionally and irrevocably.[406] In other words, the secured creditor could have been bound against its wishes only with respect of the deficiency he could not cover from the value of the asset used as collateral; when he already is an unsecured creditor. Similarly, although an arrangement may foresee that the collateral is to be waived, changed or replaced but only if consented upon by the secured creditor.

265. If, however, the secured creditor consented to the inclusion of his secured claim in the reorganization plan, he may be bound by the restructuring plan if outvoted. This may occurr irrespective whether joint voting or voting by classes of creditors is practiced.[407] In other words, Polish law recognized a version of cramdown that was,

[403] *See* Article 14 part 3 of the Lithuanian Law on Restructuring of Companies.
[404] *See* Article 24(3) of the Lithuanian Law on Restructuring of Companies.
[405] *See* Articles 13(1), 13(3) & 13(4)) of the Lithuanian Act on Restructuring Companies.
[406] *See* Article 151(2) of the Restructuring Law.
[407] *See* Article 161 of the Restructuring Law.

however, not applicable only to secured creditors. It blurs the picture though that there are no detailed rules on the formation of classes.

Question 18. Can an under-secured creditor claim from the insolvency estate in respect of any deficiency arising as a result of the enforcement of the security?

HUNGARY

266. Yes, the right to claim deficiency from the estate is generally granted.[408] However, the position of the secured creditor differs depending on whether the collateral is "only" a specific, individualized asset, or rather a floating security, determined by description but extending substantially to all assets of the debtor.

267. Namely, if the collateral is a specific, individualized asset (right or claim), the residual claim will be treated as unsecured ("other claims" ["*egyéb követelések*"]).[409] The systems reckons with the fact that the secured creditor should be in the position to determine the right credit versus collateral value ratio. This being so as in case of such collateral, in principle the secured creditor will recover 100% of his claim (principal, interest and costs) as the liquidator is entitled to deduct only the costs of the safekeeping, preservation and sale as well 5% as his remuneration.[410]

268. The situation is different in case of global (enterprise or floating) security, where the main problem is that such all-encompassing securities hardly could be enforced without restrictions and it is also an issue whether unrestricted monopoly should be given to a single, typically strategically anyhow extremely powerful creditor. Consequently, the law affords the right of separate satisfaction – within insolvency proceedings – only up to 50% of the moneys collected. Still, these secured parties enjoy a higher ranking position in respect of deficiency claims compared to other secured parties with security rights over individual assets. whose deficiency claims are treated as mere unsecured claims preceded not just by administrative costs but also by a number of other specific classes of creditors. In respect of creditors with global security, their deficiency claims will be inferior only to the administrative expenses of the proceedings.[411]

269. As the new 2013 Civil Code discarded the nominated security device of 'property encumbering charge' (global, enterprise or floating security) the different treatment afforded to individualized and floating (all-encompassing) security by insolvency law

[408] *See* § 49/D(6) of the Hungarian Insolvency Act.
[409] *See* § 57(1)(f) of the Hungarian Insolvency Act.
[410] *See* § 49/D(1) of the Hungarian Insolvency Act.
[411] *See* § 57(1)(b) of the Hungarian Insolvency Act. In other words, while the deficiency claims based on floating securities will rank as point (b) of § 57(1), the deficiency claims of creditors enforcing on single, individualized collateral will qualify only as point (f) class in § 57(1) – under the Insolvency Act.

may lead to creditor opportunistic behavior. For example, by registering almost all – but definitively leaving out some specific economically important assets – the secured party may ensure that he could ask for separate satisfaction through sale of each of the individual assets resulting in full satisfaction instead of getting only 50% of his claims and risking non- or reduced payment for the residue.[412]

LITHUANIA:

270. There is no explicit provision on whether the secured creditor could file as an unsecured creditor for the residue in the Insolvency Act.[413] However, this follows from the language of the article devoted to enforcement of security rights, according to which "*the creditor's claims secured by pledge and/or mortgage shall be satisfied **first of all** from the proceeds obtained from the sale of the pledge assets of the enterprise or by transferring the pledged assets*. *[Emphasis added.]*"[414]

POLAND:

271. Yes. Claims secured by a mortgage, pledge, registed pledge, tax pledge or marine mortgage – "*in the amount in which they have not been satisfied from the collateral*" – are included in the plan for the distribution of the insolvency estate due to an explicit provision in the Insolvency Act.[415]

[412] *See* Andrea Csőke and László Juhász, *Az új Ptk. hatása a csődtörvényre,* [the Impact of the new Civil Code on Insolvency Law] *in:* Csőd, Felszámolás, Reorganizáció, Nos. 11-12, 2014/1-2, at 13.
[413] *See* Article 34 of the Lithuanian Enterprise Insolvency Act.
[414] *See* Article 34 of the Lithuanian Enterprise Insolvency Act.
[415] *See* Article 340(1) of the Polish Insolvency Act.

V PUBLICITY AND PRIORITY OF SECURITY RIGHTS

Question 19. To what extent must security rights over assets be publicised by registration or filing to ensure effectiveness of the security interest over parties other than the debtor and in the event of insolvency proceedings?

HUNGARY:

272. As described in more detail above under questions 6 and 7, as per the new 2013 Civil Code, the basic principle is that security (in rem) rights can be validly asserted against the world (third parties) only if registered in public registers or if perfected by transfer of possession (including constructive possession).[416] The only exceptions are the security-bailments discussed above. This used to be the rule also before 2013 yet some specific transaction types (quite important segments of the economy) have remained outside the system and registration (provision of public notice) was a requirement in their case (e.g., leasing, factoring or the so-called fiduciary securities).

273. Although the new system significantly expanded the reach of the general perfection requirement and has tried to clarify the perfection-related rules, canvassing a full picture requires adding a few qualifications.

274. ***First,*** one of the great steps ahead by the drafters of the 2013 Civil Code was the prohibition of fiduciary securities (in fact quasi-securities).[417] Parallel with that, financial leasing, recourse-factoring and transactions containing retained title (ownership) were subjected to registration with the register of security rights. The idea was, indeed, to subject all transactions that perform a security function to one of the recognized perfection methods (even at the price of prohibiting some). The issue is that some economically significant transactions have been left out of scope. It is thus questionable whether this policy has been appropriately achieved when all other leasing-forms but financial leasing or non-recourse methods of receivables financing (including factoring) have been left out?[418]

275. ***Secondly****,* it ought to be noted as well that the Hungarian system goes a step further in respect of claims (receivables) as well. Namely, while it imposes as '*the obligation*' of the debtor to inform the obligor (account debtor) about "pledging" of a claim at the time of the constitution of the security interest or issue a declaration on

[416] *See* § 5:88. As the Complex Commentary proclaims: "*[The new Civil Code makes no changes as far as the constitution of security rights is concerned] and essentially recognized two methods of perfection: transfer of possession over the asset used as collateral and registration in the appropriate register*." *See* Complex Commentary, at 423.
[417] *See* § 6:99 of the Hungarian Civil Code.
[418] *See* more on this below on question 25 on quasi-securities.

that to the secured party,[419] such notification is insufficient for perfection: the "pledging" must be registered in the register of security rights as well.[420] Note that (as mentioned above) recourse-factoring is also subject to registration with the same registry of security rights.

276. ***Thirdly***, the language and the system of the new Hungarian Civil Code might be misleading. Namely, to those familiar with UCC Article 9 and other internationally renowned systems that know for the concept of perfection by '**control**,' it might occur that the Hungarian system does not know for it. In fact, the Hungarian system knows for it – or at least for its close equivalent – just it does not speak of it as a perfection method; or method how to create a security right that could be validly asserted against third parties. Rather, under Hungarian law, control is disguised as a distinct nominated security device that was kept because of tradition. This is the already-mentioned 'security-bailment' ("*óvadék*").[421]

277. The reason because of why **security-bailment** could not be fully equated with control is that security-bailments can be perfected by two more methods. Concretely, if cash or certificated securities ("*értékpapír*" – known also as investment property) is used as collateral, perfection is by transfer of possession.[422] Strangely, dematerialized securities (investment property) could also be perfected by "transfer of possession;"[423] a highly controversal fiction of the new Code of little (if any) practical value. More importantly, however, security-bailment can be constituted on dematerialized securities and bank accounts – if the service provider with whom the account is held is also the secured creditor – purely based on the security agreement of such content.[424]

278. As there is no registration in such cases, the law requires such secured creditors to "*indicate that the account is encumbered by a security interest on each and every statements of accounts*."[425] It makes things more complicated that certain asset-types could be encumbered by both a security-bailment and a registered security interests at the same time.[426]

[419] *See* 5:89(2)(c) of the Hungarian Civil Code.
[420] As the Complex Commentary emphatically states: "*[The new Civil Code], in order to ensure the full publicity of all security rights, contrary to the [earlier] Civil Code from 1959, requires registration also of security interests on rights and claims*." This follows also from § 5:88 that recognizes only two perfection methods: transfer of possession or registration with the competent registry.
[421] *See* § 5:95 of the Hungarian Civil Code. *See* on security-bailment in more detail above under Question 6.
[422] *See* § 5:95(1)(a) of the Hungarian Civil Code.
[423] *See* § 5:95(1)(b) of the Hungarian Civil Code.
[424] *See* § 5:95(2)(b) of the Hungarian Civil Code.
[425] *See* § 5:95(3) of the Hungarian Civil Code.
[426] *See* § 5:123 of the Hungarian Civil Code on the priority between the two.

279. ***Fourthly,*** given the truly heightened importance attributed to the reform (upgrading) of secured transactions law in the post-1990 period – including the new 2013 Civil Code – it is surprising that the "pledging" of motor vehicles (obviously an important segment of the economy) has escaped proper attention. Namely, unlike Poland – where the registration of security interests on motor vehicles is ex officio reported to the body issuing certificates of title – or Lithuania, there is no such synchronization in Hungary as of yet.

280. In fact, two distinct systems of registration exist side by side for encumbering of motor vehicles: on the one hand, by registering the security right on the certification of title (i.e., the document attesting who the owner of the motor vehicle is), and on the other hand, by filing with the register of security interests on movables, rights and claims operated by the National Association of Public Notaries.

281. This dualism generates practical and legal dilemmas. For example, as the fact that the motor vehicle is serving as collateral (including subjection to a retained title) is indicated on the face of the certificate of title ("*jármű törzskönyv*"), creditors (financiers) – especially in case of newly acquired vehicles – may (and normally do) keep possession of the certification of title until repayment of the debt and do not register it. If the debtor repays the debt, the financier issues a declaration whereby it allows deletion of the inscription from the certificate of title, for the effectuation of what the municipalities where the registered residence (or seat) of the debtor is. In other words, notwithstanding that the certificate of title registry system does not prove authentically the existence of a security right on motor vehicles, they may be used to bypass the registration system. *It is an issue what happens then with the main effort of the new Civil Code system that wants to extend the requirement of publicity to all kinds of assets?*

282. It seems also that especially for older generation motor vehicles no such certificate of title were issued (or often they were lost), what does not cause problems in reality as the existence of the certification of title is not a precondition for the use of the motor vehicle.[427] Although the entry in the register of movables should enjoy priority – given that the certificate of title attests only title[428] – the consequences of a discrepancy between the data on the certificate of title and the register have not been fully worked out.

[427] *See* Article 81(2) of the Act LXXXIV of year 1999 on the Register of Data Concerning Public Traffic (*"1999. évi LXXXIV. Törvény a közúti közlekedési nyilvántartásról"*) [Hereinafter: Public Traffic Registration Act].

[428] More precisely, Article 81(4) of the Public Traffic Registration Act says only that it is presumed that the holder of the certificate of tile is the lawful owner of the motor vehicle, until the contrary is proven. In other words, entries in the register and on the face of the certificate of title do not authentically prove ownership.

283. ***Last but not least****,* the new Civil Code introduced also the concept of 'trust' modelling the newcomer legal institution specifically after its Anglo-Saxon kin. The new institution seems to have been employed in two different contexts. On the one hand, a new nominated contract – one could call it the 'trust agreement' ("*bizalmi vagyonkezelési szerződés*") – was introduced. This contract was designed to become the vehicle for inter-generational transfer of wealth and for use by financial institutions. On the other hand, the new category of 'security agent' or security trustee' ("*zálogjogosulti bizományos*")[429] was added to the chapter on security rights. The security trustee is aimed to "hold" the security in lieu of multiple secured parties (syndicated loans)[430] and as such he is taking over the rights and duties of the secured party. However, such security trustee's acts will be valid against third parties only if registered in the appropriate register.[431]Notwithstanding the obligation to register and the possibility to register only the security trustee in lieu of the (single or multiple) secured creditor(s), the security trustee is hardly another type of security yet as it entails registration it should have been mentioned here.

284. In sum, save the few exceptions mentioned, the obvious desire of the policy makers was to ensure that provision of public notice is a prerequisite for creation of all in rem security rights.[432] Although with the subjection of financial leasing, recourse-factoring and retained title (ownership) to registration, a major step has been made in that direction, dilemmas remain because of why presumably there will be a need to refine the system once again in the not so distant future. More transparent rules on "creation" of security rights might also be needed.

LITHUANIA:

285. While mortgages of immovables cannot come into existence without being registered in the appropriate public registers, in case of "pledging" of movables and rights – besides registration – transfer of possession is another recognized method of perfection. In these respects Lithuanian law is not different from other CEE systems.

286. Lithuanian law is, however, specific with respect to [financial] leasing[433] contract as the most important quasi-security. Namely, these contracts are also subject to registration in order to be valid against third parties[434] or the bankruptcy

[429] *See* § 5:96 of the Hungarian Civil Code.
[430] *See* Complex Commentary at 421.
[431] *See* § 5:96(2) of the Hungarian Civil Code. The appropriate register may be either register of immovables or the one for the concrete other asset type in question (i.e., movables, rights and claims).
[432] *See* Complex Commentary at 430.
[433] The financial leasing contract is defined as a tri-partite contract involving the financing lessor, the debtor wanting to acquire an asset and the seller of the asset. *See* 6.567(1) of the Lithuanian Civil Code. The Code allows the financing lessor to transfer most of the risks related to the defects of the asset onto the lessee.
[434] *See* Article 6.572(1) of the Lithuanian Civil Code.

administrator.[435] This applies primarily to the retained ownership of the lessor,[436] which will be valid either against third parties with adverse claims or the bankruptcy administrator if registered. Leasing contracts are, however, registered in a database different from the one on "pledged" movables and rights although both databases are maintained by the same organization, the Central Mortgage Office.[437] Installment contracts are subject to registration with the same Office yet a separate database.[438]

287. The common feature of both registration systems that neither of them is a notice-filing but rather are document-filing systems with somewhat differing yet quite cumbersome rules requiring entry of quite a long list of data.[439]

POLAND:

288. With the exception of possessory pledges, all other types of security rights must be registered. This includes immovables, movables (non-possessory security on tangible assets), rights and claims (receivables) – including enterprises (or their organized parts). If a possessory pledge, security assignment or security transfer is to be effective in insolvency, additional requirement as to form exists: the security agreement must be executed in writing with a certified date.[440]

Question 20. Can you describe briefly the nature of the filing or registration system and whether it is publicly accessible?

HUNGARY:

289. As already explained above, three registration systems exist in Hungary: the registry for mortgages on immovables, the registry for security interest on movables, rights and claims (i.e., personal property) and the few specific registries for some specific types of movables (i.e., ships, aircraft and some IP rights). Each of these systems are publicly accessible though the operation of each is radically different.

290. As described in more detail under Question 7 above, the register of immovables and the registers for specific items of movables (ships, aircraft) are document-filing systems, where entries have constitutive effects. The register for security interests on

[435] *See* Article 6.572(2) of the Lithuanian Civil Code.
[436] The text of the relevant provisions do not use identical formulations though. While Article 6.572(1) speaks specifically of the lessor's ownership rights, 6.572(2) goes broader to 'lessor's rights.'
[437] The database named the 'Register of Contracts' contains registrations related to leasing. *See* at < https://www.hipotekosistaiga.lt/index.php?1927692242 >; last visited on 5 January 2015. A different governmental resolution details the registration of leasing contracts, the Resolution No. 1158 of 2002 on the Establishment of the Register of Contracts and on the Approval of the Regulations of the Register of Contracts.
[438] *See* Articles 6.411, 6.417 and 6.572 in the Lithuanian Civil Code.
[439] *For* financial leasing *see* Resolution No. 1158 of 2002; in particular section 13.3.
[440] *See* answer under Question No. 7 above on why certified date requirement was introduced for possessory pledges in 2009.

movables, rights and claims used to be the almost complete replica of the register of immovables until 2013, when the new Civil Code introduced notice filing (known by UCC Article 9). Now, thus the entries have no constitutive force and the excerpts from them do not authentically prove the existence of a security interest.

LITHUANIA:

291. The two registers (databases) of relevance[441] are publicly accessible and are not based on notice-filing but rather the entries into these registers have constitutive force toward third parties.[442] This, in other words, means that while the security agremeent is valid between the parties from the moment of its conclusion (unless otherwise stipulated), it may be invoked against third parties only if registered in the Mortgage Register.[443]

292. A designated governmental agency, the Central Mortgage Office (established in 1997) registers all security interests. It maintains the three registers (databases) mentioned. Whereas security rights on immovables as well as movables and rights are entered into the '*Mortgage Register of the Republic of Lithuania,'* leasing contracts are subject to registration with the '*Register of Contracts*.'[444] Security interests are primarily to be registered with this body. However, as this body is linked to a host of other registers, entries are thereafter synchronized with the others. The result is that if one searches the Central Mortgage Office database for security rights over property of a company, the search will reveal all registered security interests (including those in other databases).[445]

POLAND:

293. Poland has made significant steps toward making various commercial registers available online and free of charge. Surprisingly, it is not the register of 'registered pledges' that has reached the farthest. All the registries of relevance are run under the auspices of the Ministry of Justice though the courts that are empowered to make

[441] In Lithuania mortgage of immovables and security interests on movables are registered in one database. Retained title, however, is registered separately – in the register of contracts.
[442] *See* Article 4.187 for mortgages of immovables, Article 4.213 for "pledging" of movables and rights, and finally Article 6.572(1) and (2) of the Lithuanian Civil Code for retained title in financial leasing contracts. Registration is not a pre-condition for validity of retained title agreements, but is needed for use of the agreement against third persons.
[443] *See* Article 4.187(1 & 2) of the Lithuanian Civil Code for contractual mortgages and Article 4.213 for security interests over movables and other property rights.
[444] *See* the website of the agency, with English language pages, at < https://www.hipotekosistaiga.lt/index.php?2506114761 >; last visited on 7 January 2015.
[445] According to Articles 58 and 57 of the Regulations of the Mortgage Register, Mortgage Register must within 8 working hours after registration of mortgage or security interests pass all relevant information to the following registers: 1/ register of legal persons; 2/ register of real estates (immovables); 3/ register of marine ships; 4/ register of internal water ships; 5/ register of railway rolling stock and containers; 6/ register of trademarks; 7/ register of patents; 8/ register of designs; 9/ register of tractors, self-propelled and agricultural vehicles and their trailers; 10/ register of civil aircraft; 11/ register of road vehicles; 12/ register of arms.

entries are directly responsible for those registries. These would be described briefly hereinafter.

294. The Land and Mortgage Register is a public register for immovable property containing information on owners and in rem rights (including mortgages). It is maintained pursuant to the Act on Land and Mortgage Register and on Mortgages (originally enacted in 1982). Online access is available since 1 July 2014.

295. The Register of Pledges is a public register for security interests on movables, rights and claims – including enterprises (economic units) established based on and maintained pursuant to the Act on Registered Pledges and Register of Pledges kept by district (commercial) courts.[446] Notwithstanding that the very essence of this act was the introduction of a system of registration specifically for non-possessory securities and provision of public notice that way, this register has not been made available online and accessible free of charge yet. Thus, at the moment, the person interested in obtaining information from the register must file an application, either by visiting the court maintaining the register or via Internet. In the latter case, the register will deliver a pdf file of the entry supplied with certified electronic signature of the Ministry of Justice.

296. The register is not a notice-filing system. Rather it is a document filing system[447] where entries have constitutive force and the data entered are deemed to be authentic. This means, in particular, that no person may plead ignorance of data disclosed in the register and the data is presumed to be true.[448] The following data are registered: 1/ the date of submission of the request; 2/ identification of the debtor (pledger or a third party-debtor) and creditor - i.e., name and surname (or business name), Polish identification number, place of residence (registered office), address (for foreigners, the contact address in Poland); 3/ identification of the collateral (or the method of its marking if so provided in the agreement); 4/ the maximum secured amount and its currency; 5/ the pledge enforcement method as set forth in the pledge agreement (where allowed by the Act); and the negative pledve covenant (if any).[449]

Question 21. To what extent does ‘possession’ or control of the secured assets serve as an alternative method to registration or filing in ensuring third party effectiveness of the security interest?

HUNGARY:

[446] *See* Article 36.2. of the Polish Registered Pledge Act.
[447] As per Article 39.1. of the Polish Registered Pledge Act, the registration request must be accompanied by the pledge agreement or another agreement that involves either a registered pledge or a collateral covered by a registered pledge.
[448] *See* Article 38 of the Polish Registered Pledge Act.
[449] *See* Article 40.1. of the Polish Registered Pledge Act.

297. The new Hungarian Civil Code imposes written form for all kinds of security agreements, thus it is not a distinguishing factor. As a result, perfection by transfer of possession and by registration are nothing more than alternative methods of ensuring third party effectiveness. The possibility to substitute a written form-contract by certificated securities ("*értékpapír*") that entitles its holder to the collateral conditioned on payment of the amount defined therein makes no difference.[450]

298. Where it is not fully clear whether possession or control may be equated with registration is the case of the idiosyncratic security device of security-bailment. Here, two perfection methods may come into picture: **transfer of possession** or **control**. (See on this in more detail under Question 19 above). Out of these two perfection methods, it is the control-related rules that make answering the above question uneasy. Namely, in case of perfection of security bailments by control specific formal requirements apply, i.e. conclusion of the tri-partite control agreement (i.e., inclusion also of the service-provider with whom the bank or securities account is held)[451] and the obligation to indicate on all documents data about the balance on the account.[452] As already mentioned, registration is not required in such case.[453] In sum, the Hungarian version of 'control' may also qualify as equal with registration for the purposes of ensuring effectiveness against third parties.

LITHUANIA:

299. The system treats possession of the collateral (or possession of the certificated documents of title or securities) only as one of the prerequisites of the validity of a possessory pledge. In case the collateral is transferred into the hands of the pledgee, besides transfer of possession, the pledge agreement must be concluded in written form.[454] Without the written form the transaction is rendered void.

300. Even more additional formal requirements apply in case of indirect pledges, i.e., when the collateral is transferred either to a third person or is kept in the hands of the pledgor (debtor). In such cases, besides the pledge contract, a unilateral declaration of the owner of the collateral expressing his consent to pledge the asset, a pledge deed certified by a notary and registration with the Register of Morgages is a required.[455]

301. Control is not regulated explicitly by Lithuanian law but the use of control agreements in practice is not excluded either.

[450] *See* § 5:89(6) of the Hungarian Civil Code.
[451] *See* § 5:95(2)(a) of the Hungarian Civil Code.
[452] *See* § 5:95(3) of the Hungarian Civil Code.
[453] *See* Complex Commentary at 433.
[454] *See* Article 4.209(1) of the Lithuanian Civil Code.
[455] *See* Article 4.209(2) of the Lithuanian Civil Code.

POLAND:

302. Under Polish law, conclusion of a possessory pledge contract (oral or written) and the transfer of possession on the collateral to the creditor or to a third party is sufficient only to make the contract valid between the parties.[456] To make it valid against the pledgor's (debtor's) creditors, furthermore, the contract must not only be executed in written format but the date of its execution must additionally be certified as well.[457] Due to these additional requirements in addition to transfer of possession, the transfer of possession is not a full equivalent of registration (filing). The requirement of certification of the date was introduced in 2009 (with effect from 2011) in order to prevent abuse by creation of "fiduciary" pledges just for the purpose of improving ranking in pending enforcement (or insolvency) proceedings.

Question 22. Is it possible to have more than one set of security rights (security interest) over the same asset?

HUNGARY:

303. Although little emphasized by commentators, under the new 2013 Civil Code it is clearer than earlier that the same asset can be encumbered by more than a single security interest. In fact, some institutions have been introduced exactly having in mind that the possibility to encumber the same asset by more security rights is key for the economy.

304. Perhaps the best example – besides the priority rules[458] themselves – is the introduction of the institution of 'security trustee' ("*zálogjogi bizományos*"),[459] that was conceptualized to primarily serve syndicated lending with more creditors and with more security agreements. The rules allow the security trustee to represent all the creditors. This is an ideal solution when the members of the lenders' consortium are often changing.[460] If the name of the security trustee is registered in the registers of security interests, then the true secured creditors' names cannot be indicated in the registers.[461] In such cases the security trustee is the holder of the rights and obligations of the secured parties and acts in his own name but for the benefit of the secured creditors.[462]

LITHUANIA:

[456] *See* Article 307.1. of the Polish Civil Code.
[457] *See* Article 307.3. of the Polish Civil Code.
[458] *See* §§ 5:118 – 5:125 of the Hungarian Civil Code.
[459] *See* § 5:96 of the Hungarian Civil Code. As there is no established vocabulary for this new legal institution, it ought to be added that the designation 'security agent' might also qualify.
[460] *See* Complex Commentary at 435.
[461] *See* § 5:96(4) of the Hungarian Civil Code.
[462] *See* § 5:96(5) of the Hungarian Civil Code.

305. Yes. Such an eventually is explicitly stated in the priority rules.[463] Thus, if the collateral was not handed over to the creditor based on a prior pledge agreement and the pledge agreement does not state otherwise, creation of subsequent pledge is allowed. In such cases the prior pledge remains in force.

POLAND:

306. Yes. Possibility of multiple-security interests encumbering the same assets is foreseen in the priority rules explicitly.[464] To make it valid against the pledgor's creditors the contract establishing the possessory pledge must be executed in written form with a certified date.[465] In other words, to that extent transfer of possession is not equal with perfection by registration.

307. The Registered Pledge Act refers to a control agreement – though without much detail – which must be concluded, however, only in case the registered pledge is to secure debt securities issued in a series (e.g., bonds).[466] However, such security interests must also be registered and thus the control agreement is an addition to the registration requirement.

Question 23. What are the rules for determining priority between competing security interest in the same property?

HUNGARY:

308. Hungarian law is based on a system of priority rules resting on the central 'first in time, first in rights' rule,[467] and a few specific priority-affecting provisions.

309. The 'first in time, first in rights' rule links the priority to the time of the perfection of security interests; though the official terminology uses the term 'constitution of security interests' ("*alapítás*"). Two qualifications ought to be added here. *First,* assets that substitute or supplement the asset(s) used as collateral do not affect priority, unless they are encumbered by another specific security interest.[468]*Secondly,* the fact that the assets making the collateral (movables, rights or claims) are shifting, does not affect priority either – though this rule is applicable solely in case the collateral is made of more assets registered in the register of security interests on movables, rights and claims.[469]

[463] *See* Article 4.211(1) of the Lithuanian Civil Code.
[464] *See* Article 16 of the Registered Pledge Act. *See also* Article 249 and Article 310 of the Polish Civil Code. *See also* Article 11 and Article 12 of the Polish Mortgage Act.
[465] *See* Article 307.3. of the Polish Civil Code.
[466] *See* Articles 2.4. and 4.4. of the Registered Pledge Act.
[467] *See* § 5:118 of the Hungarian Civil Code.
[468] *See* § 5:119 of the Hungarian Civil Code.
[469] *See* § 5:120 of the Hungarian Civil Code.

310. Five specific priority-affecting rules should be spoken of. For the ***first,*** the possible super-priority attributed to **acquisition finance** (purchase-money security interests), see Question 24 below.

311. The ***second rule*** simply gives full recognition to **contractual subordination** ("*ranghely-szerződés*"). It merely spells out the key subordination-related internationally accepted standards. Namely, that the ranking of security interest could be changed only with the assent of all affected parties and never at the detriment of a third party that is registered as a secured party at the time of the modification of the ranking order.[470] The senior secured creditor will keep its advanced, by-subordination-generated priority position and will not revert back to its pre-subordination priority if the junior (subordinated) security interest will cease to exist for, for example, having been paid after the subordination.[471]

312. The ***third rule*** is a prescriptive rule that merely clarifies that if two security interests were constituted on the same collateral but the earlier registered secured creditor acquires the right of disposal ("*rendelkezési jog*") only after the second security interest was registered, he will have priority.[472]

313. The ***fourth rule*** declares that if a registered security interest and a security-bailment encumbers the same asset, the priority belongs to the latter.[473]

314. The ***fifth specific priority rule*** makes **reservation of a ranking position** possible. Namely, the owner of an asset may register (in any of the registers) that he intends to exploit the asset as collateral, either by specifying the future secured creditor or without doing that.[474] However, such entries must specify the sum the future security interest is going to secure.[475] Such reserved ranking position will eventually acquire the priority position according to the time of its entry.[476]

LITHUANIA:

315. The system rests on the first in time, first in rights rule. As the system obviously reckons with the fact that time is needed for the effectuation of the registration of security rights and that registration may be refused for some reason (e.g., non-approval by the notary checking the mortgage contract), the priority rule is not linked to the time of the registration of the security right but to the time of the filing of the request to register with the registry. More precisely, if two security rights were

[470] *See* § 5:124(1) and (2) of the Hungarian Civil Code.
[471] *See* § 5:124(3) of the Hungarian Civil Code.
[472] *See* § 5:121 of the Hungarian Civil Code.
[473] *See* § 5:123 of the Hungarian Civil Code.
[474] *See* § 5:125(1) of the Hungarian Civil Code.
[475] *See* § 5:125(2) of the Hungarian Civil Code.
[476] *See* § 5:125(3) of the Hungarian Civil Code.

registered at the same time, the one for which the application had been filed earlier will enjoy priority. [477]

316. Note also that retained title in financial leasing contracts (quasi-security) is not part of this priority system.

POLAND:

317. In Poland as well, the basic priority rule is the first in time, first in rights.[478]

318. In case the same assets is encumbered by more than one registered pledges, the order of priority is determined based on the day of submission of an application for registration in the register of pledges. The *day of submission of an application* is the day when the application was delivered to the court that keeps the register of 'registered pledges.' If two applications are filed on the same day, they will rank equally.[479]

319. As opposed to that, in the land and mortgage register, *the moment of the entry* is the priority reference point. Since however, two entries cannot be made simultaneously, where applications for registration have been filed at the same time, in such a case the secured parties will have equal ranking.[480]

Question 24. Are there special rules privileging the position of an acquisition financier i.e. a secured party whose advance of funds funded the acquisition of a particular asset and who may be in a priority competition with an earlier general creditor whose security interest extends to all assets of the debtor whenever acquired?

HUNGARY:

320. Acquisition financiers (purchase-money security interest-holders) are given super-priority by the new Civil Code, though the related rules are pretty short. Both suppliers of sales- (credit for the puchase price of a new movable) and loan-credits (loan to acquire a new movable) may qualify as acquisition financiers.[481]

321. These creditors will enjoy super-priority (i.e.,will rank ahead of earlier registered security interests) if two preconditions are satisfied: *first,* such security rights must be

[477] *See* Article 4.212(2) of the Lithuanian Civil Code.
[478] *See also* Article 249 and Article 310 of the Polish Civil Code. For mortgage of immovable *see* 12.1. of the Polish Mortgage Act. For registered pledges *see* Article 15 of the Registered Pledge Act.
[479] *See* Article 16 of the Registered Pledge Act.
[480] *See* Article 12 of the Polish Mortgage Act.
[481] *See* § 5:122 of the Hungarian Civil Code.

registered in the register for security interests on movables, rights and claims, and *secondly,* all those secured creditors who have a first ranking security interest on the same collateral must be notified *in writing* on the constitution of the new security right.[482] The Comments underline that these rules aim to foster acquisition of new assets by the debtor.[483]

LITHUANIA

322. Lithuanian law does not have specific rules granting super-priority to acquisition financiers. However, the retained ownership (title) under financial leasing is recognized as full 'ownership' that is valid against third parties[484] and the bankrutpcy administrator[485] is registered with in the Register of Contracts maintained by the Mortgage Office.

POLAND

323. The Registered Pledge act contains no such rules (purchase-money superpriority). Note, however, that leasing and contracts with retained title, are not looked upon as forms of security rights. As in their case the "full" ownership ensures high level of protection equivalent, if not higher, to the super-priority of PMSIs.

324. Security transfers and assignments – if executed in proper form (notarization to certify the execution date) – have by now become the equivalents of in rem security devices rather than devices ensuring super-priority.

[482] *See* § 5:122 of the Hungarian Civil Code.
[483] *See* Complex Comments at 462.
[484] *See* Article 6.572(1) of the Lithuanian Civil Code.
[485] *See* Article 6.572(2) of the Lithuanian Civil Code.

VI QUASI-SECURITY

Question 25. Does your legal system have any rules equating the treatment, in whole or in part, of security interest and 'quasi-security' agreements i.e. agreements that in legal terms do not involve the creation of security interests but have many of the same economic consequences? Examples of quasi-security include the factoring or sale of receivables and finance leases, hire purchase agreements and retention of title clauses in sale of goods contracts.

HUNGARY:

325. In Hungary, such devices have come to be known as 'fiduciary securities;' some were products of legal innovation, others were transplants from western Europe (or a mixture). These were widely exploited devices having gained significant position in the national economy. Unfortunately, they have generated some legal problems as well, from causing major social tensions (e.g., housing mortgages combined with the option to purchase)[486] through bypassing of such fundamental principles of property law as the prohibition of *lex commissoria* (or prohibition of strict foreclosure).[487] As some of these devices have not only become popular but have satisfied as well genuine commercial needs, the reaction of the drafters of the new Civil Code was two-directional.

326. On the one hand, some of the fiduciary securities were prohibited.[488] These were contracts that secured monetary claims by transfering ownership, assigning claims or establishing the right to purchase (options). These were prohibited because "*they gave to creditors more rights [and entitlements] at the detriment of debtors than that would have been in fact necessary or legally justified*."[489] Additionally, they were often

[486] Contracts with an option to purchase were used by businesses as well. In the case BH2013. 131, for example, the parties concluded a loan contract that was first secured by a mortgage on an immovable. Later, the parties concluded also a contract designated as 'Option Contract' ("*Opciós szerződés*"). This gave the creditor the right to purchase the mortgage immovable that could be exercised by the latter upon default of the loan contract. More precisely, if the creditor would terminate the loan contract with immediate effect or if the contract would terminate for any other reason. In other words, through the combination of the mortgage and the right of option to purchase, the secured creditor could simply declare that he is "purchasing" – or becoming the owner – of the immovable encumbered by the mortgage.
[487] *See* Complex Commentary at 574.
[488] *See* § 6:99 of the Hungarian Civil Code proclaiming that "*Agreements that secure a monetary claim through transfer of ownership, right or claim, or through granting of a purchase option are null and void; with the exception of agreements allowed by the [EU] Financial Collateral Directive*."
[489] *See* Complex Commentary at 574.

infringing such debtor and other creditor-protective devices as the prohibition of the *lex commissoria.*[490]

327. On the other hand, there were also some other, quite widely used novel transactions that have rather played an economically useful function. In their case, it became clear that their subjection to registration (provision of public notice) would be desirable and sufficient to curb abuses (e.g., factoring). In other words, the new Code brought them closer to classical security devices by imposing the duty to register in the register of security rights.

328. Yet only three specific types of contracts were caught: to wit, financial leasing, recourse-factoring and contracts with retained title. For example, other types of leasing arrangements have remained intact by these changes. This is a questionable solution resting on the presumption that the so-called 'operative leasing' is equal to traditional rent (and thus there is no need even to nominate it) and on the – somewhat contradictory – postulate that "*leasing contracts are so diverse that their subjection to common rules is impossible*."[491]

329. In case of **financial leasing**[492] – the only leasing type regulated by the Code for the very first time in Hungarian legal history[493] – the system presumes that the retained ownership (title) really means retention of full ownership. This is reflected, for example, in the rules on termination of the contract: while the lessor is entitled to terminate the contract on the basis of any of the five explicitly formulated grounds,[494] the lessee can do that only for the lessor's failure to fulfill its warranty duties.[495]

[490] *See* Complex Commentary at 574.
[491] *See* Complex Commentary at 873.
[492] Financial leasing is looked upon by the Code as a financing device where the "*lessor typically provides financing for the acquisition of the object of leasing by the lessee*." *Quoted* from Complex Commentary at 873. The lessee may either automatically acquire ownership by the end of the leasing term (closed-end leasing), or he may purchase the object for the residual value (open-end leasing). *Id.*
[493] In the post-1990 phase 'leasing' became (in addition to franchise and factoring) one of the most popular imported contracts. From among the many sub-variants known in practice, the operative versus financial leasing were recognized as the main forms. In the perception of the drafters, in case of the operative leasing the parties' intention is not to acquire ownership but rather only to use the object of leasing for a specified period of time, its regulation was not opted for. Thus, in the case of operative leasing the rules on convention rent and usufruct apply mutatis mutandis. *See* Complex Commentary at 873.
[494] Based on grammatical interpretation of § 6:415(1) of the Hungarian Civil Code termination of financial leasing contracts is possible only based on the explicitly specified grounds and this is not left to be determined by the parties (for example, in a default clause). This follows also from the Complex Commentary which reads: "*[The Code, given the differences that exist between leasing and credit contracts] instead of seven provides only for five grounds for immediate termination*." *See* Complex Commentary, at 878. It is to be noted that the title of § 6:415 of the Hungarian Civil Code (Termination of the contract) does not contain the attribute of 'immediate'.
[495] *See* § 6:415(3) of the Hungarian Civil Code.

330. This includes as well the duty of the lessor to warrant that no third person has any such right on the object of leasing that would limit or prevent the lessee from its use.[496] As opposed to that, the warranty for the proper functioning ("*kellékszavatosság*") of the object of leasing is imposed on the lessor only if it participated in the selection of the object of leasing or if it has waived the warranties without the consent of the lessee.[497]

330. Similar to leasing, **factoring** is another successful transplant that has had an explonential growth in the post-1990 period in Hungary;[498] notwithstanding of what for the old Civil Code it was only an innominate contract. Today, it is utilized virtually in all segments of the economy.

331. Due to its economic importance and yet to curb the legal uncertainties surrouding factoring, the drafters of the new Civil Code chose to introduce it as a nominated, *sui generis* type of contract.[499] Interestingly, the drafters took recourse-factoring as the paradigm. As the Complex Comments say "*without recourse, the transaction cannot be differentiated from sales*."[500] As a consequence of this peculiar solution, non-recourse factoring transactions would be treated either as purchase (claim-purchase) or atypical transactions.[501] In other words, the possibility of bypassing the registration system through non-recourse factoring contracts has remained a real option and they remain quasi-securities.

332. Two factoring-related rules are important from the point of view of security rights. *First,* it is the factor's duty (obligation) to register the fact that a factoring contract has been concluded and to enter data necessary for the identification of the debtor - in the register of security interests on movables, rights and claims. [502] *Secondly,* in the lack of registration – and notwithstanding the assignment – it is presumed that the claim has not been transferred onto the factor (creditor), who as a consequence will be entitled to no more than to what the secured creditor whose security right on a claim (receivable) has not been registered in the register of security interests on movables, rights and claims. In other words, the non-registered Hungarian recourse-factoring would not be perfected but would attach and could therefore be enforced solely between the parties to the factoring contract but would not be valid against third parties.[503]

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[496] *See* § 6:411(1) of the Hungarian Civil Code.
[497] *See* § 6:411(2) of the Hungarian Civil Code. There is a qualification though in such cases. In particular, the lessee may not ask for the substitution of the leasing object. *See* § 6:411(2). This paragraph contains some further rules on warranties.
[498] According to the Complex Commentary (p. 866), in 2011 gross 888 billion HUF were factored.
[499] *See* §§ 6:405 – 6:408 of the Hungarian Civil Code.
[500] *See* Complex Commentary at 867.
[501] *See* Complex Commentary at 868.
[502] *See* § 6:406 of the Hungarian Civil Code.
[503] *See* Complex Commentary, at 839.

333. **Retained title** is regulated by the new Civil Code in the Chapter on sales contracts.[504] While ROT on immovables was subject to registration even under the old Civil Code, the great novelty is that the duty to register has been extended onto movables as well. The volte face ensued due to the realization that ROT, in fact, performs a similar function as security interests (liens).[505] As the functional equivalent of security rights, thus ROT should be treated equally especially in respect of provision of public notice on the existence of ROT. Consequently, the existence of the ROT and the identity of the debtor must be registered either in the register for security interests on movables, rights and claims, or – if a distinct register exists for certain classes of movables (e.g., ships) – in that public register.[506]

334. This equalization does not extend, however, only to the duty to register and to cast the agreement on ROT in written form.[507] Namely, on the one hand, the non-registered ROT will not prevent the good faith purchase of the asset encumbered by the ROT to acquire proper title. On the other hand, the security interest granted by the buyer for the benefit of a third-party creditor will be enforceable against the seller (protected by the ROT) notwithstanding that the debtor lacks the right of disposal.[508]

LITHUANIA:

335. Lithuanian law contains provisions for quasi-securities that are regulated by the Civil Code in a manner that is separate from mortgage and "pledge" law. These include retained title in financial leasing[509] as well as in installment sales contracts,[510] the special case of consumer hire-purchase contracts[511] and assignment of receivables (claims) as security – regulated as part of factoring law.[512] These transactions are not looked upon as security devices as a rule and thus Lithuanian scholarship does not talk of them as such.

336. Similarly to Hungarian law, validity against third parties or the bankruptcy administrator in case of retained title presumes registration in the Register of Contracts maintained by the Central Mortgage Office. As opposed to that, in case of factoring registration is not a requirement; it is rather a notification-based system. In other words, the Lithuanian system treats contracts containing retained title (including leasing) as equals only with respect to the duty to provide public notice.

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[504] *See* § 6:216 of the Hungarian Civil Code.
[505] *See* Complex Commentary at 684.
[506] *See* § 6:216(4) of the Hungarian Civil Code.
[507] *See* § 6:216(2) of the Hungarian Civil Code.
[508] *See* § 6:216(4) of the Hungarian Civil Code.
[509] *See* Article 6.572(1) and (2) of the Lithuanian Civil Code. Art. 6.567 is a more general article, providing definition of leasing.
[510] *See* Article 6.441(1) of the Lithuanian Civil Code.
[511] *See* Article 6.361 of the Lithuanian Civil Code.
[512] *See* Article 6.903(2) of the Lithuanian Civil Code.

337. Consumer hire-purchase contracts are subject to distinctive regulation under Lithuanian law and deserve a brief mention. The single applicable provision states only that if the ownership is retained in case of consumer purchase-sales contracts the parties may agree that until payment of full purchase price of the contract the buyer will be "only" a lessee.

POLAND:

338. Polish law knows also some quasi-securities. These include not only leasing and retained title but also the somewhat idiosyncratic security transfers ("*przewlaszczenie na zabezpieczenie"*) and security assignments ("*przelew na zabezpieczenie"*).

339. **Leasing** is subject to a regime distinct from security laws, regulated by a separate title in the Civil Code.[513] In fact, Polish law does not look upon leasing as a form of security but rather only as a newcomer nominated contract where the emphasis is on letting the lessee use, or use and collect profits of object of leasing.[514] The parties may agree that the lessee may acquire title to the object of leasing, however, that is not looked upon by the system as a normal but rather as an optional yet tolerated feature of the contract.[515] This is reflected also in the Insolvency Act, which foresees, for example, that in case of lessee's insolvency the leasing contract will not expire yet the insolvency practitioner may terminate the contract upon consent of the judge.[516]

340. **Retained ownership** is likewise distinct from security rights and is perceived to be part of sales law. The validity of ROT towards the buyer's creditors is conditioned by the Civil Code on written form with a certified (authenticated) date. Dates in official documents, or in documents issued by a governmental body (including local governments) or notaries will qualify as containing certificated dates.[517]If executed with certified dates, the ROT will survive insolvency[518] and the seller may claim exclusion of the asset from the bankruptcy estate.

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[513] *See* Book Three on Obligations, Title XVII[1] on the Contract of Leasing, Articles all numbered as 709[1] through 709[18] (altogether 18 new sections) yet which were all added as amendments.
[514] *See* Article 709[1] of the Civil Code containing the definition of leasing.
[515] *See* Article 709[16] of the Polish Civil Code specifying that if transfer of ownership was agreed upon, the lessee may demand the transfer within a month from the lapse of the agreed upon time.
[516] *See* Article 114 of the Polish Insolvency Act.
[517] *See* Article 81 of the Polish Civil Code. Polish case law differentiates additionally between *data certa sensu stricto* (narrower, strict sense) and *data certa sensu largo* (broader meaning). While in the first case the certification is focused exactly on the date of the execution of an act, in the latter cases the documents primarily certify some other facts yet the same document certifies also the dates on which those acts were performed. The *data certa* requirement primarily aims to prevent antedating of documents. For a Supreme Court case involving a security transfer and a discussion on what satisfies in that context the *data certa* requirement *see* Krzysztof Kaźmierczyk & Filip Kijowski, *Enforcement of Contracts in Poland, in:* Stefan Messmann & Tibor Tajti (eds.), t*he Case Law of Central and Eastern Europe – Enforcement of Contracts* (European University Press, Bochum – Germany, 2009), at 633-638 [hereinafter: Kaźmiercyzk & Kijowski, Enforcement of Contracts in Poland].
[518] *See* Article 101 of the Polish Insolvency Act. The Insolvency Act refers to these as "claims secured by transfer of ownership of property, claim or another right."

341. As opossed to leasing and retained title, **security transfers and assignments** have been for most of the post-1990 period rivals of registered pledges (especially in car finance). They were case-law-created fiduciary securities that, however, were not subjected to registration or any other way of provision of public notice.[519]

342. These securities survive the opening of insolvency proceedings provided the agreement was executed in writing with *data certa, i.e.,* authenticated date of the execution of the agreement.[520] They are still known in Poland though the law applicable to them has changed; in particular with the 2009 amendment of the Insolvency Act. While prior to the amendments the creditor could claim exclusion of the property or rights transferred or assigned to him by way of these fiduciary security from the bankruptcy estate, since the 2009 amendments they are treated in insolvency in the same way as pledges.[521]

[519] *See* Spagnole article at 283 and Kaźmierczyk & Kijowski, Enforcement of Contracts in Poland, at 633.
[520] *See* Kaźmierczyk & Kijowski, Enforcement of Contracts in Poland, at 634.
[521] *See* the new Article 70^1 as well as Article 336.2. of the Polish Insolvency Act.

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VII AVOIDANCE OF TRANSACTIONS

Question 26. Are there rules in your legal system that operate once a debtor enters insolvency proceedings and that provide for the invalidation of transactions entered into by the debtor prior to the commencement of the insolvency proceedings?

HUNGARY:

343. The liquidator (acting on behalf of the debtor) or the creditor may proceed, either based on the Civil Code (the *Actio Pauliana*) [522]or based on the Insolvency Act to invalidate such transactions.[523] As per the latter, the reasons for invalidation are: 1/ fraudulent transfers ("*csalárd ügyletek*"),[524] 2/ gratuitous or conspicuously undervalue bilateral transactions ("*ingyenes vagy feltűnően aránytalan visszterhes jogügyletek*"),[525] and 3/ preferential treatment of a creditor ("*hitelező előnyben részesítése*").[526]

344. The Insolvency Act differentiates additionally a sub-type of the last item – provision of preferential *services (performance)* to a specific creditor ("*szolgáltatás visszakövetelése egy hitelező előnyben részesítése miatt*").[527] The rationale for this is that a preference may consist also of *performing* a contract before that would be due (especially if performance would be due after opening of the insolvency proceedings). Put simply, the Hungarian lawmaker found it important to stress this by casting it into a separate provision.

345. These suits are known under the heading of 'avoidance litigation' ("*megtámadási perek*"). As no empirical data seem to exist on which avenue is more frequently exploited and why, one may only presume rather than firmly claim that the tools offered by insolvency law are more regularly resorted to. No empirical analyses exist on the basis an evaluation could be made about the efficiency of the laws.

LITHUANIA:

346. Lithuanian law knows two types of avoidance avenues, the one initiated by the bankruptcy court – the sui generis institution of fraudulent bankruptcy[528] – in which case the time period for review of transactions is if five years. The other is part of the

[522] *See* §6:120 of the new Civil Code.
[523] *See* Hungarian Insolvency Handbook, at 541.
[524] *See* § 40(1)(a) of the Hungarian Insolvency Act.
[525] *See* § 40(1)(b) of the Hungarian Insolvency Act.
[526] *See* § 40(1)(c) of the Hungarian Insolvency Act.
[527] *See* § 40(2) of the Hungarian Insolvency Act.
[528] *See* Article 20 of the Lithuanian Insolvency Act.

statutory duties of the administrator who has to check transactions concluded 36 months before the start of the insolvency proceedings.[529]

347. Lithuanian law knows also the Actio Pauliana.[530]

POLAND:

348. Besides the Actio Pauliana that is available to creditors *outside*[531] insolvency based on the Civil Code,[532] the amended Insolvency Act contains a number of avoidance rules of relevance only to liquidations. The basic rules additionally apply to both corporate and individual debtors and are applicable to:

1. gratuitous and grossly undervalue transactions (including court settlements, waiver of claims);[533]
2. granting of a security or payment of an immature debt;[534]
3. non-gratuitous transactions with connected parties;[535]
4. security assignment of future receivables made without certified date;[536]
5. excessive remuneration paid to a director or officer of the bankrupt corporate;[537]
6. securing the debt of a third party at no or extremely low consideration (benefit) for the bankrupt; and[538]
7. contractual penalties in situations where the non-pecuniary obligation secured by the penalty has been performed to material extent or the penalty is manifestly high.[539]

349. The novelties and changes introduced by the amended Insolvency Act are the following.

First, a new avoidance rule foresees that the assignment of future receivables is ineffective in insolvency if it comes into existence after opening of insolvency proceedings unless the receivable assignment agreement was executed no later than 6 months prior to the filing of the bankruptcy petition in written form with certified date (*data certa*).[540]

Second, the rules on avoidance of transactions with connected persons i/ have been expanded to include also unmarried yet cohabitating persons as well as companies with a single shareholder; ii/ the rules on avoidance of transactions with connected

[529] *See* Article 11.5(8) of the Lithuanian Insolvency Act.
[530] *See* Article 6.66 of the Lithuanian Civil Code.
[531] Under Polish law, Actio Pauliana is very rarely available after declaration of insolvency. This would be possible only if the avoidance rules would not provide protection in a particular case but Actio Pauliana would do. See also Article 131 of the Insolvency Act and section 357 of this report.
[532] Articles 527-534 of the Polish Civil Code.
[533] *See* Article 127(1)-(2) of the Polish Insolvency Act.
[534] *See* Article 127(3) of the Polish Insolvency Act.
[535] *See* Article 128(1) of the Polish Insolvency Act.
[536] *See* Article 128a of the Polish Insolvency Act.
[537] *See* Article 129(1) of the Polish Insolvency Act.
[538] *See* Article 130(1) of the Polish Insolvency Act.
[539] *See* Article 130a of the Polish Insolvency Act
[540] Article 128a(1)(2) of the Polish Insolvency Act.

persons will not operate based on the law but will require decision of the bankruptcy judge who may issue such decision at its own discretion or on the application of the insolvency practitioner; and iii/ the burden of proving that the transactions is not harming the interests of the creditors is on the connected person. However, if he proves that the transaction causes no damages to creditors, it cannot be declared void by the court.[541]
Third, the rules allowing for challenge of the bankrupt's directors excessive remuneration were extended also to the so-called shadow directors, which may be either employees performing managerial activities, or persons providing managerial or supervisory services.[542]
Last but not least, a rule aimed at faster recovery of assets from avoidable transactions was introduced. According to this, if the transfer of such property is avoided, there is no more need to lodge a claim against the suspected tranferee but the decision declaring the transaction void itself will qualify as an enforcement title against such person.[543]

350. Under the 2015 Restructuring Act the following avoidance rules apply: 1/ gratuitous and grossly undervalue transactions (including waivers and settlements);[544] 2/ granting of a security at no consideration or if the value of the collateral exceeds by more than half the secured claim;[545] and 3/ excessive remuneration paid to a director or to an executive.[546]

Question 27. Do these transactional avoidance rules catch security and quasi-security type transactions?

HUNGARY:

351. Granting of a security to a creditor in the suspect period of 90 days preceding the arrival of the request for liquidation to the court – when the creditor had security whatsoever – would qualify as a preference. The same regime applies also to modification of an existing contract for the benefit of a creditor or otherwise providing preferential treatment to a creditor otherwise. [547]

352. The language of the avoidance provisions in the Insolvency Act are otherwise neutral and talk about the possibility to attack "*a contract or a legal declaration*" (*[az adósnak] a szerződését vagy más jognyilatkozatát*) of the debtor. Therefore, quasi-

[541] Article 128 of the Polish Insolvency Act.
[542] Article 129(1) of the Polish Insolvency Act.
[543] Article 134 of the Polish Insolvency Act.
[544] Article 304(1)(2) of the Polish Restructuring Law.
[545] Article 304(3)(4) of the Polish Restructuring Law.
[546] Article 305 of the Polish Restructuring Law.
[547] *See* § 40(1)(c) of the Hungarian Insolvency Act.

security agreements may also qualify, just as all other contracts or declarations; it is rather the intention and/or the effects on the debtor's estate that matter.[548]

LITHUANIA:

353. Both provisions (avenues for invalidation) are neutral and talk of 'transactions' rather than being limited to security rights. Thus, in principle, they cover both security and quasi-securities.

POLAND:

354. Secured transactions; i.e., to granting of *in rem* security (mortgage, pledge, registered pledge, or maritime pledge) may be avoided based on a special provision in the Insolvency Act.[549] These, however, apply only to liquidations under the Polish Insolvency Act.

355. The regime applicable to fiduciary transfers as quasi-securities is essentially the same but whether fiduciary transfers are to be treated as 'securities' equal to mortgages and pledges for the purposes of avoidance law or rather as general transactions, is not easy to determine. There is no explicit formula for determining whether a transaction involving transfer of a movable or a claim qualify or involves a security transfer or assignment.

356. The qualification is of importance because the suspect period for 'securities' is shorter than for other [general] transactions (6 months versus 1 year).[550]

357. Moreover, transactions that serve as security may be challenged only on the basis of a particular provision that contains a 6 months suspect period. As the Supreme Court ruled in a case, in order to determine whether such transactions could qualify as a security for the purposes of the avoidance rules, the interpretation of the parties' agreement is needed to determine the intent and thus the true nature of the contract (e.g., whether receivables were sold or rather used only as collateral). It also ruled that whenever the Insolvency Act is to be applied, the application of the Civil Code's rule on Actio Pauliana is excluded.[551]

Question 28. If so, describe briefly these rules highlighting in particular (a) the rationale for the rules; (b) the conditions for the

[548] *See* § 40(1)(a) of the Hungarian Insolvency Act.
[549] *See* Article 130(1) of the Polish Insolvency Act.
[550] The period was extended from two to six months by amendment to Article 127(3) of the Polish Insolvency Law introduced by 2015 Restructuring Act.
[551] For an analysis of the case III CZP 104/2005 with excerpts from the judgment in English and Polish *see* Kaźmierczyk & Kijowski, Enforcement of Contracts in Poland, at 638-645.

application of the rules; (c) the length of the 'suspect period'; (d) whether the rules apply to transactions with a cross-border element; (e) whether the rules operate more stringently in respect of transactions that favour parties who are connected to the debtor and (f) any defences that may be availed of by a counterparty to the transaction (i.e., the defendant in an avoidance action).

HUNGARY:

The rationale of the rules:

358. The Insolvency Act contains, neither a detailed preamble, nor is there an official comment of the Insolvency Act.[552] Hence, the rationale of the Hungarian avoidance rules does not seem to be different from the ones underlying the avoidance rules of most other European insolvency systems.

359. This in particular means the following:

(1) In case of fraudulent transfers, the law allows for avoidance of transactions because, on the one hand, the debtor's intention was to defraud a creditor or creditors, and on the other hand, the party with whom the debtor concluded such transactions knew, or should have known, about the debtor's fraudulent intent.[553] Here, the system does not want to reward fraud, in addition to aiming at providing adequate and equal protection to all creditors.

(2) The protection of the estate and the equal protection of creditors underlies as well the rules allowing for avoidance of gratuitous and conspicuously undervalue transactions. The same principle applies to preferential treatment of a creditor.

The conditions for the application of the rules:

360. *First,* only the creditors and the liquidator – acting on behalf of the debtor – have the right to file a claim for avoidance of a transaction with the competent court.[554] Additionally, the administrator – being often in a better position to track avoidable transactions – has the duty to inform the creditors' committee, their representative, or the creditors (if no committee is formed) about the problematic transaction(s) *without*

[552] The short preamble of the Hungarian act posits the reorganization of the debtor through agreement with its creditors as the first goal of the system. Yet – as opposed to the Polish one – it does not proclaim that ensuring maximal satisfaction of creditors' claims is also a goal. *See* the one-sentence-long preamble in the Hungarian Insolvency Act.

[553] *See* § 40(1)(a) of the Hungarian Insolvency Act.

[554] *See* § 40(1) of the Hungarian Insolvency Act. For the rules on jurisdiction *see* § 6(1). For conducting main or ancillary cross-border insolvency proceedings as per Regulation 1346/2000 against a business enterprise not registered in Hungary the Metropolitan Court of Budapest (http://fovarositorvenyszek.birosag.hu/english) has exclusive jurisdiction according to § 6(2).

*delay a*nd he has to transfer the underlying proofs as well.[555] Apart from that, it is not clear what the rational of the administrator's duty to inform is.

361. *Secondly,* if a creditor or the administrator is attacking a contract *only* based on the Civil Code, the generally applicable rules on jurisdiction and statute of limitations apply. As opposed to that, if a contract is sought to be avoided on the basis, at least partly, of the Insolvency Act, the claim has to be filed with the insolvency court.[556]

362. *Thirdly,* the avoidance claims can be filed with the competent court within **90 days** from learning about problematic transaction. However, under no circumstances can the claim be filed after the expiry of **one year** from the date of the publication of the court order opening the liquidation proceedings.[557]

363. *Fourthly,* if the attack is successful and the transaction is avoided, the Civil Code's provisions on void contracts ("*érvénytelenség*") are to be applied.[558] In particular, the creditor or administrator may request restitution and the deletion of avoided rights that have been entered on public registers.[559]

364. *Last but not least,* as the assets of the debtor are to be disposed of by the administrator exclusively through public sales (normally through public bids or invitations for tender offers) and he is expected to achieve the highest possible price, it is primarily the administrator who is liable to carrying out and for the result of disposals. This means also that the administrator and the purchaser are jointly and separately liable vis-à-vis the insolvent debtor (enterprise) if they were acting in collusion to sell an asset at undervalue.[560]

The length of the 'suspect period':

365. The Insolvency Act makes a distinction between different suspect periods depending on the type of the avoidable transaction.

366. (i) In case of fraudulent transfers, the time is **five years** preceding the making of the request to the court for the opening of liquidation proceedings.[561]

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[555] *See* § 40(5) of the Hungarian Insolvency Act.
[556] *See* Hungarian Insolvency Handbook at 551. *See* § 6(1) for the jurisdictions of courts.
[557] *See* § 40(1) of the Hungarian Insolvency Act.
[558] *See* § 40(1a) of the Hungarian Insolvency Act. *See* § 6:108 et seq. on the consequences of voidness in the new 2013 Civil Code.
[559] *See* § 40(1a) of the Hungarian Insolvency Act.
[560] *See* the high court decision BH2011. 227, which proclaimed that court practice accepts as the biggest possible price the one achieved at a public bid or tender unless there are some other data or circumstances that make that suspicious. In other words, the fact that the asset was sold at a public auction may not be sufficient but the achieved price and other circumstances of a case should also be taken into account when deciding (also) on the possible liability of the liquidator.
[561] *See* § 40(1)(a).

367. (ii) In case of gratuitous and conspicuously undervalue bilateral transactions the suspect period is **two years** preceding the request to the court for opening of liquidation proceedings.[562]

368. (iii) In case of transactions providing a preference to a specific creditor the time is **ninety days before the** receipt of the request by the court for the opening of liquidation proceedings.

369. (iv) *Finally,* if a creditor was provided a preferential service (performance) or a service (performance) was out of the ordinary, the suspect period is **sixty days before the receipt** of the request for the opening of liquidation proceedings. In such case, the liquidator may request, on behalf of the debtor, to return the services (performance); like return of the prematurely paid debt.[563]

Applicability of the rules to transactions with a cross-border element:

370. As there are no territorial limitations on the operation of the avoidance provisions of the Insolvency Act, in principle, they apply also to transactions with a cross-border element.

The applicability of the rules on debtor's insiders:

371. The Insolvency Act contains explicit rules applicable to transactions with insiders in the context of avoidance litigation. Transactions concluded with the following three categories of parties may qualify as insiders: *first,* business enterprises ("*gazdálkodó szervezet*")[564] in which the debtor has a majority control, *secondly,* the member or chief officer of a business enterprise ("*gazdálkodó szervezet tagja vagy vezető tisztségviselője*"),[565] and *thirdly* business enterprises that – even though not linked directly or indirectly – are controlled by the same person or business enterprise.[566] These presume fraudulent intent where the transaction was made for no consideration

[562] *See* § 40(1)(b) of the Hungarian Insolvency Act.
[563] *See* § 40(2) of the Hungarian Insolvency Act.
[564] For the definition of business enterprise s*ee* § 3(1)(a) of the Hungarian Insolvency Act, which includes a wide range of business, professional (e.g., law firm) and non-profit vehicles – with or without a juridical entity status – that have the center of their main interest (COMI) in the European Union, from all Hungarian company forms, cooperatives, to sole proprietorships and associations and foundations.
[565] For the definition of 'chief officer of a business enterprise' ("*gazdálkodó szervezet vezetője*") *see* § 3(1)(d), which limits this concept to the *registered* officers of an enterprise. In case of foreign enterprises this would be the person registered in Hungarian registers as the person being entitled to make legal acts on behalf of the entity. If there is no such designated person, then it is presumed that the person entitled to represent the entity before governmental bodies or to conclude contracts and other private legal acts will qualify.
[566] *See* § 40(3) of the Hungarian Insolvency Act.

or where the transaction is challenged as being a conspicuously undervalue bilateral transactions.[567]

The defences available to defendants in avoidance actions:

372. The Insolvency Act explicitly excludes the applicability of the avoidance rules in two specific situations: 1/ close-out netting ("*pozíciólezáró nettósítás*"), and 2/ if the collateral is substituted by another asset of equal value or if an additional security is granted.[568] Otherwise, the generally applicable rules may be resorted to.

LITHUANIA:

Rationale of the Rules:

373. As far as the administrator's duty to review and avoid some transactions is concerned, this is a normal corollary of modern insolvency systems.[569] What is unusual is the broad – if not vague – criteria for determining what transactions should be avoided. In particular, the rationale of avoiding of *all* transactions that might prevent settlement with creditors is questionable.

374. The intention to sanction parties who have profited from fraudulent bankruptcies[570] is self-explanatory but the general (if not vague) nature of the criteria for avoidance somewhat obscures this rationale.

The Conditions for the Application of the Rules:

375. The provisions are as follows:

- *first,* administrator has the statutory time period of six months from the receipt of the underlying documents to review them; unless extended by the bankruptcy court for additional six months;
- *secondly,* he has to review transactions entered into by the bankrupt within 36 months before the initiation of the bankruptcy proceedings;
- *thirdly,* he is to start court proceedings for the invalidation of three classes of transactions: 1/ those that are contrary to the debtor-enterprise's activities; 2/ those that would prevent settlement with creditors and finally 3/ those that led to fraudulent bankruptcy.

376. In case of **fraudulent bankruptcies**, the steps leading to invalidation of fraudulent transactions are the following:

- *first,* the bankruptcy court has to determine during the bankruptcy proceedings that the debtor was intentionally bankrupted;

[567] *See* § 40(3) of the Hungarian Insolvency Act.
[568] *See* § 40(5) of the Hungarian Insolvency Act.
[569] *See* Article 11.5(8) of the Lithuanian Insolvency Act.
[570] *See* Article 20 of the Lithuanian Insolvency Act.

- *secondly,* then the administrator will have to review all transactions made within 5 years before the initiation of the bankruptcy proceedings;
- *thirdly,* the administrator has to review and initiate invalidation of those transactions that are either contrary to the interests of the debtor and/or could lead to inability to settle with creditors.[571]

The Length of the Suspect Period;

377. It is a general duty of the administrator to examine all transactions entered into by the bankrupt debtor within **36 months** before the date of the initiation of bankruptcy proceedings. What makes the Lithuanian system peculiar is that the suspect period is qualified by the addition of the phrase 'at least 36 months.' This, in other words, means that the administrator must check transactions for at least 36 months but he also has the right to check and attack those concluded even earlier. The administrator is constrained in that respect by the rule that he has only six months available as a rule. As this limited period of time may be prolonged only once and only for another six months, in case of large corporations it is questionable whether the time frame is sufficient.

378. As opposed to that, if the bankruptcy court finds the case to be one of fraudulent bankruptcy[572] – the administrator is obliged to review all transactions made within **5 years** before the opening of insolvency proceedings.[573]

Application to Transactions with Cross-Border Element:

379. In the lack of specific rules on the applicability of these rules to transactions with cross-border elements, one has to draw the conclusion that EU Regulation 1346/2000 and Lithuanian conflicts of law rules would apply.

Stringency of the Rules towards Parties Connected to the Debtor:

380. Although the Lithuanian Insolvency Act imposes quite meaningful obligations and even liability for damages for failure to participate in the proceedings, there are no explicit avoidance rules specifically targeting only parties connected to the debtor.

Defenses of the Counterparty to the Transaction:

381. Lithuanian Insolvency Act does not specify any particular defense mechanism that would be available to counterparties to suspect transactions.

POLAND:

Rationale of the Rules:

382. Under the Insolvency Act (liquidation) the rationale of the avoidance rules is the satisfaction of the claims to the maximum possible extent.[574] Consequently, if a

[571] *See* Article 20 of the Lithuanian Insolvency Act.
[572] Fraudulent bankruptcy is defined by Article 2.1. (12) of the Lithuanian Insolvency Act as "*deliberate bringing of the enterprise to bankruptcy*."
[573] *See* Article 20 of the Lithuanian Insolvency Act.
[574] *See* Article 2 of the Polish Insolvency Act.

transaction is declared ineffective, all what has been received by the party to the transaction must be transferred or credited to the bankruptcy estate. Under the new 2015 Restructuring Act the avoidance rules, however, serve besides this purpose also the restoration of the debtor's capacity to service its debts.[575] Note here, however, that the avoidance rules under the Restructuring Act apply only to rehabilitation proceedings and not to the other three new restructuring proceedings.

383. Case law: As pronounced by the Polish Supreme Court, a set-off declared by the bankrupt debtor within one year before declaration of opening of liquidation proceedings is ineffective if the counter-party knew for the existence of grounds for declaration of bankruptcy.[576]

384. The avoidance rules do not apply to financial collateral.[577]

The Conditions for the Application of the Rules:

A. Common Rules:

385. Three commonalities exist for each type of avoidable transactions: 1/ the legal effect of voidability is *ineffectiveness* (invalidity) vis-à-vis the bankruptcy estate, 2/ in each of the cases the benchmark date for calculation of the suspect period is "*the day of submission of a petition for bankruptcy*;" and 3/ the petition to declare a transaction ineffective may be brought within **two years** from the declaration of insolvency unless the claim expired earlier based on the Civil Code or was null and void (ineffective).[578]

B. Specific Rules:

386. Gratuitous and grossly undervalue transactions:

A. Insolvency Act:

The following rules apply:

a/ a transaction is deemed to be grossly undervalue if "*the value of the benefit provided by the bankrupt grossly exceeds the value of the benefit received by the bankrupt or reserved for the bankrupt or a third person*;" and

b/ the rules do not extend to security established in association with forward financial transactions, lending of financial instruments or sale of financial instruments with repurchase obligation.[579]

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[575] Statement of reasons attached to the Restructuring Law proposal (bill), page 58.

[576] Resolution of the Supreme court dated 4 September 2013 in case III CZP 26/13.

[577] Article 135(2) of the Polish Insolvency Act and Article 309(2) of the Restructuring Act. The text of the Articles is identical.

[578] Judgment of the Appeal Court in Gdańsk dated 29 April 2015 in case V ACa 859/14. The case concerned a donation of a flat made by a father to his daughter (article 127(1) case). While the donation was made on 22.03.2010, insolvency was declared 21.06.2010. Action based on article 127(1) was brought on 17.02.2014 (after two years). The court held that both articles 127 and 128 provide for ineffectiveness of a legal transaction *ex lege* (no court decision is necessary).

[579] *See* Article 127(4) of the Polish Insolvency Act.

c/ the rules extend also to court settlements, waiver of claims and acknowledgement of a claim;

B. Restructuring Act:
a/ legal transactions executed by the debtor within one year before the day of submission of a petition for opening of the rehabilitation proceedings may be attacked;
b/ if they were performed gratuitously or non-gratuitously but the value of the benefit provided by the debtor significantly exceeds the value of the benefit received by the debtor or reserved for the debtor or a third person;[580]
c/ the same rule applies to gratuitous or undervalue court settlements, acknowledgement of a complaint or writing off a claim.[581]

387. Non-gratuitous transactions with connected persons: *As under the Restructuring Act there are no avoidance rules involving connected persons*, only the list from the Insolvency Act can be provided. According to this, the list of connected persons includes:
(i). Individual bankrupts: a/ spouse, relative or relative by affinity in the direct line; b/ relative or relative by affinity in the collateral line up to the second degree inclusive; and c/ adoptee or adoptive parent, and c/ as added by the 2015 amended Insolvency Act persons living in a common household (cohabitation) [see also Question 26 above].

(ii) Companies or other legal persons as bankrupts: a/ partners, sole shareholders or representatives (officers), or their spouses; b/ affiliated entities, their partners or representatives, or their spouses; c/ transactions between parent and subsidiary, as well as d/ as added by the 2015 amended Insolvency Act: single shareholder companies [see also Question 26 above].

(iii) Case law: neither employees,[582] nor shareholders[583] (unless in the shoes of directors or officers) qualify as connected persons. As far as the former is concerned, the exemption applies if made as part of a regular employment.

388. Last but not least, the list of connected persons listed for individual bankrupts applies mutatis mutandis here as well. [584]

389. Excessive remuneration paid to an officer of the bankrupt corporate:
A. Insolvency Act:
More preconditions apply:

[580] Article 304(1) of the Polish Restructuring Act.
[581] Article 304(2) of the Polish Restructuring Act.
[582] Judgment of the Supreme Court dated 4 September 2014 in case I PK 23/14.
[583] Judgment of the Appeal Court in Gdańsk dated 28 June 2013 in case V ACa 330/13.
[584] *See* Article 128(1)-(3) of the Polish Insolvency Act.

a/ remuneration is to be paid based on an employment or service contract or resolution of an organ of the bankrupt concluded before declaration of bankruptcy;
b/ the excessiveness of the remuneration is measured against two cumulatively applicable criteria: (i) the average remuneration payable for the same type of work or service and (ii) the amount of work done;
c/ the proceedings may be started by the judge decide ex officio or at the request of the receiver;
d/ a court decision is passed in the matter: (i) after having heard the receiver and the bankrupt's representative, whereby (ii) a portion of the remuneration will be declared ineffective.[585]

B. Restructuring Act:
The following terms and conditions apply:
a/ the persons caught are debtor's representatives (directors and officers) or employees performing managerial activities, persons providing services of management or supervision of debtor's enterprise based, either on employment or service contracts, or resolution of debtor's board;
b/ the time span in the purview of the system is three months before the day of opening of rehabilitation proceedings,
c/ remunerations paid to these persons will be avoidable if excessively high compared to average remuneration for the same type of work or services and not justified by the amount of labour;
d/ the restructuring judge shall determine, ex officio or at the request of the administrator, that a certain portion of the remuneration due for a certain period before the day of opening of rehabilitation proceedings, is ineffective with respect to the restructuring estate, even if the remuneration has already been paid.[586]

390. Securing the debt of a third party at no or extremely low consideration (benefit) for the bankrupt.
A. Insolvency Act:
The following conditions apply:
first, this provision is triggered only at the request of the receiver;
secondly, only specific types of security transactions may be attached (i.e., mortgage, pledge, registered pledge and maritime pledge);
thirdly, a court decision is passed; and
fourthly, the provisions apply if (i) the security was given by the bankrupt to a third party for which it did not receive any consideration (benefit), or (ii) a security was

[585] *See* Article 129 of the Polish Insolvency Act.
[586] Article 305 of the Polish Restructuring Law.

established for a consideration (benefit) "*that is exceedingly low compared to the value of the [collateral];"*
*finally, a*s already stated above, if the security was given for the benefit of a connected person, the collateral value versus benefit for the bankrupt ratio is not of relevance as in such case the system presumes that the transaction is ineffective.[587]

B. Restructuring Act:
A security interest granted by the debtor within one year before the day of submission of a petition for opening of the rehabilitation proceedings is ineffective if the debtor is not receiving a commensurate benefit directly.[588]

The Length of the Suspect Period:
391. The length of the suspect period differs for each type of the avoidance rules.

A. Insolvency Act:
392. In case of gratuitous and grossly undervalue transactions (including court settlements, waiver of claims) the suspect period is **one year** before the day of submission of a petition for bankruptcy. [589]

393. In case of granting of a security or payment of an immature debt the suspect period is **six months** before the day of submission of a petition for bankruptcy.[590]

394. **Six months** before the day of submission of a petition for bankruptcy is the time in the case of non-gratuitous transactions with connected parties.[591]

395. The same **six months** applies also to excessive remuneration paid to a director or officer of the bankrupt corporate.[592]

396. Finally, securing the debt of a third party at no or extremely low consideration (benefit) for the bankrupt will be ineffective vis-à-vis bankruptcy estate if made **one year** before filing for bankruptcy.[593]

B. Restructuring Act:
397. In case of gratuitous and grossly undervalue transactions (including waivers and settlements) the suspect period is **one year** before the day of submission of a petition for opening of rehabilitation proceedings. [594]

[587] *See* Article 130 of the Polish Insolvency Act.
[588] Article 304(3) of the Polish Restructuring Act.
[589] *See* Article 127(1) of the Polish Insolvency Act.
[590] *See* Article 127(3) of the Polish Insolvency Act.
[591] *See* Article 128(1) of the Polish Insolvency Act.
[592] *See* Article 129(1) of the Polish Insolvency Act.
[593] *See* Article 130(1) of the Polish Insolvency Act.
[594] *See* Article 304(1)(2 of the Polish Restructuring Act.

398. **One year** before the day of submission of a petition for opening of rehabilitation proceedings is the time in the case of granting of a security at no consideration or if the value of the collateral exceeds by more than half the secured claim.[595]

399. **Three months** applies also to excessive remuneration paid to a director or to an executive.[596]

Application to Transactions with Cross-Border Element:

400. The basic rule is that the Polish Insolvency Act (including therefore the avoidance rules) does not apply if it contradicts either an international treaty to which Poland is a party or EU legislation.[597] As the Polish Insolvency Act, in principle, cannot contradict EU law, the Polish avoidance rules should be applied whenever Polish law is the applicable one. This applies primarily when the main proceedings are conducted in Poland. The same applies also to the Restructuring Act.

401. The Polish Insolvency Act, however, has some specific rules affecting the applicability of Polish avoidance rules even in case when the main proceedings are in another Member State of the EU. These are:

(i) The basic principle is that for assets and debts located in Poland, Polish law applies.[598] This basically means the application of Polish avoidance rules for assets located in Poland.[599]

(ii) If a foreign insolvency proceeding was recognized as the **main proceeding**, the foreign representative may intervene in any proceedings to which the bankrupt is a party. Thus, he may bring also actions to declare ineffective transactions detrimental to creditors.[600] If a foreign representative was appointed in **secondary** bankruptcy proceedings, the right to intervene can be exercised solely in respect to the assets involved in those proceedings.[601]

(iii) If secondary bankruptcy proceedings are instituted in Poland ***after*** recognition of foreign bankruptcy proceedings, the administration of the bankrupt's assets located in the Republic of Poland, previously performed by a foreign representative shall be

[595] *See* Article 304(3)(4) of the Polish Restructuring Act.
[596] *See* Article 305(1) of the Polish Restructuring Act.
[597] *See* Article 378(1) of the Polish Insolvency Act.
[598] *See* Article 403(1) of the Polish Insolvency Act.
[599] *See* Article 403(2) of the Polish Insolvency Act.
[600] *See* Article 400(2) of the Polish Insolvency Act.
[601] *See* Article 400(3) of the Polish Insolvency Act.

continued by a receiver or administrator appointed in the secondary bankruptcy proceedings.[602]

Stringency of the Rules towards Parties Connected to the Debtor:

402. The Restructuring Act introduced no avoidance rules on connected parties. As opposed to that the Insolvency Act not only has such rules but they are more stringent if connected parties are at stake. T**wo specific provisions** are dedicated to these transactions:1/ non-gratuitous transactions with connected parties, and 2/ disproportionately high remunerations paid to corporate officers (see Question 27 above). Additionally, the law presumes that the transaction is avoidable if security was granted to a connected party.[603]

Defenses of the Counterparty to the Transaction:

A. Insolvency Act:

403. Gratuitous and grossly undervalue transactions: this rule is a non-rebuttable presumption of the system.[604] This means that if a transaction was performed "*gratuitously or non-gratuitously but the value of the benefit provided by the bankrupt grossly exceeds the value of the benefit received by the bankrupt or reserved for the bankrupt or a third person*,"[605] it is deemed that such transactions will be ineffective vis-à-vis the estate*.* The law foresees no right of objection or appeal.

404. Granting of a security or payment of an immature debt: the rule is a rebuttable presumption. The counter-party may petition the bankruptcy court to declare the transaction valid if he could prove that he was not aware of the fact that the grounds for declaration of insolvency were present at the time when the security was granted or the payment made. [606] As opposed to the former rule, non-gratuitous transactions with connected parties are *non*-rebuttable presumptions of the system.[607]

405. Excessive remuneration paid to an officer (representative) of the bankrupt corporate: The decision of the court is appealable.[608]

406. Securing the debt of a third party at no or extremely low consideration (benefit) for the bankrupt. The decision of the bankruptcy judge may be appealed.[609]

B. Restructuring Act:

[602] *See* Article 410(1) of the Polish Insolvency Act.
[603] *See* Article 130(3) of the Polish Insolvency Act.
[604] *See* Article 127(1) of the Polish Insolvency Act.
[605] *Id.*
[606] *See* Article 127(2) of the Polish Insolvency Act.
[607] *See* Article 128(1) of the Polish Insolvency Act.
[608] *See* Article 129(4) of the Polish Insolvency Act.
[609] *See* Article 130(4) of the Polish Insolvency Act.

407. To reiterate, avoidance rules apply **only** in the context of **rehabilitation proceedings**. Hence, note that the next few sections will apply only to them.

408. Gratuitous and grossly undervalue transactions (including waivers and settlements): this rule is a non-rebuttable presumption of the system.[610] Such transactions will be ineffective vis-à-vis the rehabilitation estate by operation of law and the law foresees no right of objection or appeal.

409. Granting of a security at no consideration or if the value of the collateral exceeds by more than half the secured claim: this rule is a non-rebuttable presumption and the law foresees no right of objection or appeal.[611].

410. Excessive remuneration paid to a director or to an executive: The decision of the court is appealable.[612]

[610] *See* Article 304(1) of the Polish Restructuring Law.
[611] *See* Article 304(3)(4) of the Polish Restructuring Law.
[612] *See* Article 305(5) of the Polish Restructuring Law.

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VIII: EXPERIENCES WITH THE EU CROSS-BORDER INSOLVENCY LEGISLATION

A. ARTICLE 5 AND RIGHTS IN REM (SECURITY RIGHTS)

Question 29. Have you come across any difficulties in relation to the operation of Article 5 of the Regulation on rights in rem (security rights)?

HUNGARY:

411. Based on the few reported cases and the Hungarian scholarship, two difficulties could be identified. However, as these difficulties are either highlighted in only a couple rather than a number of court cases, or are theoretical rather than practical problems (figuring only in scholarly debates), one should not draw too far-reaching conclusions based on them.

Case Law:

412. As illustrated by a case decided upon by the Curia (Supreme Court) in 2013,[613] lower level courts in the case had problem with understanding and thus applying Article 5 of the Regulation. At stake was a security-bailment on company shares (and the price received for them) constituted based on Hungarian law. The security was granted by the Austrian debtor against whom the main insolvency proceedings were in process in Austria. The first and second instance Hungarian courts ruled that based on Article 4(2)(f) of the Regulation the security cannot be enforced in Hungary but only within the main insolvency proceedings and based on Austrian law.

406. The Supreme Court (Curia), as opposed to the lower level courts, ruled that 1/ the secured party's claim should be adjudicated based on Article 5 of the Regulation, meaning that 2/ the main proceedings ongoing in Austria do not affect the constitution, validity and effects of the Hungarian security. Consequently, 3/ "*the secured party may enforce his security right as if the main insolvency proceedings would not have been initiated, as if the debtor would not be subject to an insolvency proceeding.*" Likewise, 4/ obstacles imposed by Austrian law (as the law of main proceedings) that may restrict enforcement of the Hungarian security (e.g., stay according to Austrian law) do not effect enforcement of the security right according to Hungarian law. Thus, 5/ whether the mentioned Hungarian security-bailment came into existence and how it should be enforced is to be determined based on Hungarian private law. Last but not least, 6/ the only point on which Austrian law is determinative is whether the defendant in the Hungarian proceedings aimed at enforcement of the security-bailment should be represented in person or by the Austrian insolvency administrator. As according to Austrian law the debtor has no right of disposal during the insolvency proceedings, the party to such litigation could be only the Austrian insolvency administrator.

Scholarly debates

[613] *See* EBH2013.G.4. The Curia is the highest court instated in Hungary and is in charge also with the harmonization of the law. For related English language pages *see* <http://kuria-birosag.hu/en/uniformity-decisions-jurisprudence-analysis>.

413. Two issues appear to be contentious in the scholarly debates. One of the dilemmas is caused, on one hand, by the requirement of Hungarian insolvency law that makes enforcement of security rights (or generally all creditors' claims) contingent on acquiring the status of a 'creditor,'[614] and on the other hand, under Hungarian insolvency law the collateral can be sold only by the insolvency administrator (save the security-bailment).

414. The dilemma is what happens if the main proceedings are opened in Hungary and how these features of Hungarian insolvency law affect enforcement in another Member State where it is not a requirement to become a recognized creditor or where private sale of the collateral (i.e., not exclusively by the administrator) is part of the legal system. According to a leading Hungarian commentator, private enforcement on the basis of another national law would be possible but the creditor would have to become a registered creditor as required by Hungarian law.[615]

[614] As explained above, in order to be enlisted as a creditor, a claim must be filed with and be recognized by the insolvency administrator and the prescribed registration fee must be paid in. For reorganizations s*ee* § 12(1) and for liquidations *see* § 46(5),(6) and (7) of the Hungarian Insolvency Act.
[615] *See* Andrea Csőke, *A határokon átnyúló fizetésképtelenségi eljárások* (HVG-Orac, 2008), at 149-153.

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IX CONCLUSIONS

415. Admittedly, the above analysis of only three CEE jurisdictions yields no complete picture of the entire region. Nevertheless, since similar in-depth reforms have taken place in most of the other countries in this part of Europe, moreover more often than not in the same direction as well, conclusions may legitimately be drawn not only in respect of the three jurisdictions under consideration, but more generally in respect of other countries in the region.

416. In order to answer our central query ***whether European harmonization of insolvency (substantive) and the law relating to security rights is appropriate and desirable*** **from the perspective of CEE – in particular from the perspective of Hungary, Lithuania and Poland –** the focus should be on the following main issues: 1/ the quality and nature of the legal framework; 2/ the effiency of the system (the operation of the registry system and of the enforcement system); 3/ the technical and technological bases of the registration system(s), and 4/ the prevailing social, polical and economic circumstances (in particular, the importance of credit, security and access to finance, reform fatigue, and willingness to learn from the experiences of others).

A The Legal Environment (the Quality of Security and Insolvency Laws):

417. As far as security laws are concerned – especially reform of personal property security laws (i.e., security interests on movables, rights and claims) – it is common that in all systems the reform and upgrading of the system was the centre of interest in the post-1990 period. This includes in particular, the following.

418. A major mindshift occurred in the matter of 25 years. In this process a mindset for which credit and security were inherently (and ideologically) bad was gradually replaced with another one for which credit is the alpha and omega of economic activities and the token of economic well-being. This claim stands notwithstanding that problems with overindebtedness have surfaced as well.

419. As part of this process, these systems have embraced the philosophy that in rem securities should be publicized (i.e., public notice must be provided to the outside world or a legally sanctioned substitute method must be employed). This is stark contradiction with, for example, German and Austrian laws.

420. Moreover, such often neglected yet important changes have occurred, like:
a/ the possibility to encumber virtually all kinds of transferable assets has become reality;
b/ the domestication of floating-types of enterprise (global) securities has also been concluded; and

c/ to a great extent due to the introduction of global securities, these systems have in the meantime been transformed from the era of 'single-security per asset' to systems where encumbering of the same assets with more securities is normal.

421. Next to security laws, insolvency laws were also the focus of post-1990 reforms in each of the targeted countries. Perhaps the achievements are less conspicuous compared to secured transactions law yet the task of insolvency lawyers was tougher because they were commissioned with multiple tasks. The expectation was not only to draft modern insolvency acts – after four-and-a half decades of legal vacuum – but also to reconcile the new system with the newly introduced common-law inspired secured transactions laws as well as to catch up with new challenges. The forging of a legal framework that would incentivize rescue of enterprizes instead of driving them out of the market through compulsory liquidation was obviously the toughest one; in respect of what the results are modest at most.

B The Efficiency of the System:

422. Each of the countries have taken steps to increase the efficiency of the operation of their newly introduced secured transactions (movables, rights and claims as collateral only) systems. These efforts were directed to make the process of the creation of security rights as easy, cheap and fast as possible and, secondly, to increase efficienies in the enforcement of security interests. Both strands of efforts required rethinking and giving up some parts of inherited venerable legal principles or doctrines. In case of mortgages on immovables these efforts were directed rather only to improving the work of the registers.

423. Each of the systems have through subsequent amendments tried either to bypass or at least to minimize the involvement of courts in the process of creation of security rights. While in Poland we can talk only of reduction of the involvement of courts, in Hungary and Lithuania the task was given over completely to public notaries. The new 2013 Hungarian Civil Code went a step further by introducing the system of notice-filing thereby reducing the role of notaries.

424. After the initial reluctance to give way to various methods of out-of-court enforcement of security rights, each of the systems has opened the doors to some forms of self-help or private enforcement.[616] While self-help *repossession* is still illegal, sale of the collateral by the parties (without involvement of the court) and strict foreclosure (i.e., acquiring of the collateral upon default by the secured creditor) has become tolerated in some form. The most far reaching change is the possibility of private enforcement of Polish global (enterprise) securities; which seemed to have

[616] For the overview of related developments in some European jurisdictions *see* Catalin Gabriel Stanescu, *Self-Help, Private Debt Collection and the Concomitant Risks* (Springer, 2015).

remained only a not-widely-exploited possibility in Hungary so far. Thus, while in the UK enforcement of floating charges privately through receivers has been cut back radically, the same practice has developed in some parts of CEE. All this was driven by the realization that efficient enforcement is a measure of the success of the new secured transactions systems.

425. The evidence in respect of the new insolvency system is less promising. While typically empirical research is lacking and thus one may not be in the position to point to publicly available quality data, the large number of amendments of the new Insolvency Acts[617] should be a good, though indirect, indicator of the frequency and gravity of problems these systems have witnessed in that respect. It is common to the region that the bankruptcy stigma index is high everywhere and this is that particular factor that is the most important obstacle to introduction of a rescue culture; a problem well-known to western systems as well. Although avoidance litigation is intesifying, it is still plagued with uncertainities and inefficiencies and would require more attention in the future.

C The Technical and Technological Bases of the new Systems:

426. Each of the countries under consideration have introduced new registries, typically first only for *securities on movables*. Later, these were expanded to reach also rights and claims (receivables); though in respect of these types of assets used as collateral the divergences are still significant. Most of the registries have by now become computerized and accessible via Internet; though not necessarily open to the wider public and searchable free of charge. Moreover, in some, the registries have become interlinked and entries have been synchronized. This may not necessarily be the case even in the most developed western countries.

427. Selected data related to *insolvency* have become registrable in publicly accessible computerized systems linked to Internet as well.[618] This is still in process and one should not be completely satisfied with the achievements.

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[617] The new [post-1990] Hungarian Insolvency Act (enacted in 1991, stepped into force on the 1 January 1992) has been amended in the mean-time 16 times: by five major and 11 minor amendments. *See* Hungarian Insolvency Handbook at 38-40.

[618] In Hungary, insolvency-related information are available through the website providing information on companies operated by an office under auspices of the Ministry of Justice at <http://www.e-cegjegyzek.hu/index.html>. In January 2015, only Hungarian language pages seem to be available only.

In Lithuania the register for juridical persons contains such information at < http://www.jar.lt >; last visited on 7 Jan. 2015.

Insolvency-related information are obtainable in Poland through the National Court Register at < http://bip.ms.gov.pl/pl/rejestry-i-ewidencje/ >. It ought to be added, however, that a new Central Insolvency and Restructuring Registry (*Centralny Rejestr Restrukturyzacji i Upadłości*) has been introduced by the 2015 Restructuring Act with its operations foreseen to start on 1 February 2018. As the other online registers, it will be operated by the Ministry of Justice and made available free of charge. It will make provision for: (i) publication of decisions and other documents related to insolvency and

428. Access to data on cross-border insolvencies is still problematic and problems persist on domestic level as well. For example, in Poland while the Land and Mortgage Register became searchable online and free of charge from 1 July 2014, that is still not the case with the Register of Pledges that was introduced by a law often considered to be the most progressive in the realms of security law. Nevertheless, one may validly claim that these countries possess solid foundations as far as the technical and technological bases are concerned to get linked to a common European system.

D The Social, Political and Economic Climate:

429. It is far from being irrelevant what the attitude of various stake-holders is and generally whether a society is open to learn from the good or bad experiences of others. As it is well-known from the many publications on legal reforms, transplantation and modernization (no matter how labelled), many factors come into picture during those processes. The issue is not only about the fear from the risks (known and unknown) corollary to novel legal institutions but also how to find the right balance between the tested venerable foundations of the old system and the new, foreign and thus unpredictable. What matters is that the reformed CEE countries have gained lots of experiences with handling such problems potentially exploitable by countries that have or are about to embard on reform of their systems – as is the tendecy nowadays in Africa (e.g., Malawi, Nigeria, Sierra Leone or Kenya).

430. From an economic point of view it matters also that due to the reforms, stakeholders, businesspersons and a significant part of the citizenry have realized the key role that credit and credit securities play. If one evaluted what an economics or law graduate at the end of the 1980s knew about these topics on average in CEE and compared this with the knowledge of current graduates, the change would be conspicuous and signify the changes that have occurred in the meantime. These and a host of other changes are as important developments as the introduction of modern laws.

E The Final Verdict:

431. On the basis of the above, one should not deny that the new systems do work in the analyzed CEE jurisdictions quite well, notwithstanding the gaps, dilemmas and occasional backpedalling. In many respects, these systems come closer to the unitary

restructuring proceedings; (ii) making publicly available data included in the said decisions; (ii) filing of applications and other documents; (iii) service of process (delivery of documents in proceedings); (iv) making available official forms of applications; and (v) containing list and addresses of relevant insolvency courts and insolvency practitioners. It will also include information on the main and secondary proceedings referred to in the Insolvency Regulation].

The Croatian website is also maintained by the Ministry of Justice at < https://sudreg.pravosudje.hr/registar >; last visited on 7 Jan. 2015. In Romania insolvency-related information are available via < http://www.buletinulinsolventei.ro >; last visited on 7 Jan. 2015.

model and Book IX of the DCFR than that of some of the economically more developed systems of the EU.

432. In brief, should European harmonization occur, for example, along the model enshrined in Book IX of the DCFR, Hungary, Lithuania and Poland would be in a pretty good position to relatively easily align themselves with it. If another model would be opted for (e.g., the existing German system of latent security interests) that may cause serious problems in this country as that would require discarding all the achievements made as part of the secured transactions reforms in the post-1990 period. This claim stands irrespective of the fact that each of these laws contains a number of idiosyncratic solutions.

433. Overall, the achievements of the CEE countries is fruitful soil not only for comparative lawyers but also for those looking for a common model for Europe.

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