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Guide for taking charges in Hungary



European Bank
for Reconstruction and Development

Guide for taking charges in Hungary

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and the European Bank for Reconstruction and
Development**

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Introduction

In 1996, Hungary was among the first countries in the region to reform the Civil Code provisions related to secured transactions (charges) over movable and immovable property. The country established a flexible, simple and reliable regime, which has been a source of inspiration throughout the region. The reforms in 2000 further enhanced that regime.

This guide aims to give the practitioner, be it businessman, banker or adviser, a brief overview of the law governing secured transactions in Hungary and to provide answers to the practical questions that are likely to arise for those involved with the giving or taking of a charge to secure credit.

A charge is a right that a person (a ‘chargor’) gives a creditor (a ‘chargeholder’) in his assets to secure payment of a claim due to the creditor. The claim may be for repayment of a loan or trade debts arising in a business, or any other claim for money. If the claim is not paid, the assets given as security may be realised to satisfy it. The effect of a charge is to give the chargeholder a right in the charged assets, in addition to his personal claim against the debtor.

An effective legal framework for the granting of secured credit is generally regarded as an essential aspect of a modern market economy. It facilitates the granting of credit, thus stimulating economic activity and at the same time permitting a more efficient use of assets. The purpose of security is to reduce the risk attached to giving credit, by increasing the chances of the lender recovering the amounts owed by the debtor. As a result, the availability of credit is increased, its cost is reduced and the other conditions applicable to credit (for example the duration) are improved.

An explanation of terms used

As far as possible this guide avoids the use of technical language but it may help the reader to explain, at the outset, certain terms used in this guide:

Charge

A right in assets to secure payment of a claim for money.

Charge agreement

An agreement which establishes a charge.

Charged assets

Assets over which a charge is given (same as *charged property* or *collateral*).

Charged property

Property over which a charge is given (same as *charged assets* or *collateral*).

Chargeholder

A person to whom a charge is given to secure payment of his claim (same as *secured creditor*).

Charges Register

The register of charges operated by the Hungarian Chamber of Notaries.

Chargor

A person who gives a charge over his assets to secure payment of his debt or the debt of another debtor.

Collateral

Assets or property over which a charge is given (same as *charged assets* or *charged property*).

Enforcement

The process by which the rights of a chargeholder are exercised.

Enterprise charge

A charge covering the entirety of the assets of a business or part of a business that can operate as a separate economic unit (enterprise).

Framework charge

A charge securing a fluctuating debt.

Possessory charge

A charge where the chargeholder (or a designated third party) takes possession of the charged assets.

Realisation

The sale of the charged assets on enforcement.

Registered charge

A charge which is registered in a public registry, allowing the chargor to retain the right to possession of the charged assets (non-possessory charge).

Secured claim

The claim of the chargeholder that is secured by the charge (same as *secured debt*).

Secured creditor

The creditor whose claim is secured by a charge (same as *chargeholder*).

Secured debt

The debt due to the chargeholder that is secured by the charge (same as *secured claim*).

Security

An umbrella expression used to cover rights given to a creditor to reinforce or 'secure' his right to payment.

Specific register

A register in which certain types of assets are recorded, for example the Land Register, Aircraft Register, etc.

Key features

The principles underlying the regime for charges in Hungary include:

- Any legal or physical person can give a charge over its assets in favour of any other legal or physical person.
- The charge can be taken over any single or collective asset or right that is capable of being transferred. These include movable tangible assets, land and buildings, rights and receivables. (Note that under Hungarian law, intangible property does not qualify as movable.) The charge can also be taken over a group of assets which is constantly changing and assets that the chargor will acquire in the future.
- All types of claim may be secured, and may be denominated in any currency, be of fixed or varying amount and include claims that will arise in the future.
- If parties agree to create a registered charge, the debtor may retain possession and continue to use the assets taken as security. Land, buildings and other immovable assets may only be charged by registered charge.
- The law allows considerable contractual flexibility, with broad scope for the debtor and creditor to determine the terms of the security in a way, which fits with what they agree between themselves.
- The Charges Register permits immediate registration of charges over movable assets at any notary office. Any person may inspect information on the Register at a notary office.
- The creditor gains a first right in the charged assets, subject to any prior charge given to another creditor. Priority between registered charges is determined by the order of their registration.
- If the debtor fails to pay the secured debt when due, the secured creditor has the right to take possession and to sell the assets given as security and to use the proceeds to repay the debt. The process for enforcement allows for sale by auction or private sale, without the necessity of involving the courts.

Which laws?

Charges are primarily regulated by sections 251-269 of Act IV of 1959 of the Hungarian Republic (Civil Code).

Further important provisions can be found in the following pieces of legislation:

- Sections 47-48 of Law Decree 11 of 1960 on the Implementation of the Civil Code, as amended by Para 3 Section 2 of Act CXXXVII of 2000 on the Modification of Legal Regulations on Taking Charges
- Act CXLI of 1997 on the Real Property Registry
- Sections 114, 114/A, 138/A, 138/B, 169, 170, 170/A of Act LIII of 1994 on Judicial Enforcement
- Decree No 11/2001 (IX.1.) IM of the Ministry of Justice on the Detailed Rules of the Charges Register
- Decree No 12/2003 (I. 30.) of the Government on the Sale of Charged Property through Non-judicial Enforcement
- Sections 38, 49/D, 56, 57, 58 of Act IL of 1991 on Bankruptcy Proceedings, Liquidation Proceedings and Voluntary Dissolution.

1. FIRST STEPS: IDENTIFYING THE ELEMENTS OF A CHARGE

1.1 Who is involved?

1.1.1 Who can grant a charge?

Anyone can grant a charge over his assets, as long as he has the capacity to transfer those assets. Restrictions on the ability of some entities (e.g. local government authorities) to transfer their assets also affect their right to grant security.

1.1.2 Who can receive a charge?

Anyone can receive a charge to secure debts due to him. The most usual chargeholders are banks and credit institutions, but any person who gives credit to another may receive a charge. Companies frequently receive charges to secure claims against other companies arising in the course of their business. A charge can be granted to local and foreign creditors alike.

1.2 Identifying the property involved: What assets can be charged?

The subject of a charge may be any tangible thing, any transferable right or claim. This basically means that a very wide range of assets can be charged.

Security may also be granted over future assets and a group of assets which is constantly changing, such as inventory, stocks of raw materials or an entire enterprise.

Movable and intangible property is often a significant component of a company's assets and it can represent substantial wealth of the business. Examples include stocks of raw materials, work in progress, inventory of finished products, claims against customers for goods or services supplied, equipment and machinery used in the business, trademarks and patents. The law provides a viable regime for taking security over such assets, which often makes a charge over them almost as attractive as the more traditional charge over immovable assets.

1.2.1 Things - Tangible movable assets

Any type of tangible movable asset can be charged. This can include a piece of equipment, a stock of goods, a diamond, a computer, etc. Often tangible movable assets are described generally, since such assets in many cases are difficult to identify individually (raw materials, stocks of goods, etc.).

Special rules apply to the charging of certain movable assets which are recorded in specific registries, e.g. ships and aircraft (see 3.3.2).

1.2.2 Land - Immovable assets

Immovable assets may also be given as security, such as a plot of land, a building or any object that is fixed to the ground. The process for contracting the charge is similar but, as with other registered assets, the formalities to establish such security are different (see 3.3.4).

1.2.3 Intangible assets

A charge may also be granted over intangible assets such as claims for money (receivables) and economic rights arising from intellectual property rights (e.g. patents, rights to software). Receivables as charged assets are attractive as they can represent a substantial part of a company's assets, which can be efficiently liquidated and which have limited risk of depreciation.

In a business where there is a predictable flow of payments from customers who have been accorded time for payment, a charge over the pool of receivables from customers and over the bank account into which those receivables are paid may provide valuable security.

A building supplies company gives its regular customers 60-day payment terms. As security for its bank overdraft it gives a charge over (i) the receivables from its customers, and (ii) the bank account into which customers make payment.

In relation to charges over receivables and bank accounts (see 4.1.6 and 4.1.7).

1.2.4 What assets cannot be charged?

To be charged, an asset must be freely transferable. Even if the transferability of an asset is limited, the charge is still valid. For example, the current restriction on foreigners buying agricultural land does not prevent the creation of a charge for the benefit of a foreigner. The restriction, however, will affect the enforcement of the charge since land may only be sold to Hungarians. There are certain cases when it is possible to prohibit contractually the creation of a charge and to register such prohibition in the land registry (but not in the Charges Register). This makes ineffective any charge created subsequently (e.g. a seller may do so for the period the purchaser owes the purchase price).

Intellectual property rights are a combination of personal and economic rights; only the latter are transferable, and hence chargeable.

It is not clear whether securities can be the subject of a non-possessory charge (see 3.3.3).

1.2.5 *Can future property be charged?*

It is possible to charge not only assets owned by the chargor at the time of the charge agreement, but also assets that he may acquire in the future. These may be assets that exist at the time of the charge agreement or assets that only come into existence subsequently (equipment to be acquired at a later date, raw materials or other goods to be purchased in the future, future claims against customers).

Although the charge is only created in law at the time when the chargor acquires the assets, all the formalities are completed in advance and the charge comes into existence automatically on acquisition. For questions of priority (see 4.4).

Often, future assets will be generally described, since a specific description at the time of the agreement may be difficult or even impossible (see 1.2.7). It should be noted that a charge over immovable assets or over assets which are registered in specific registries (e.g. intellectual property rights) cannot be taken for after acquired assets since it has to be registered against the specific assets.

To secure a loan, a bank requests a charge over production line machinery, together with any additions or extensions that may be added in the future.
To secure a loan to a building company, a lending institution takes a charge over all amounts due to the builder under a given construction contract, together with all future amounts that may become due from the customer to the builder relating to the construction project.

Practice note: It is important that the contract includes an adequate definition of the future assets to be included. A charge over production line machinery, for example, may not cover additions or extensions unless this is clearly stated.

1.2.6 *Can property already charged to someone else be charged again?*

It is possible to charge the same assets to different persons, as part of different transactions. Only one possessory charge, however, can exist over an asset at any one time. The first chargeholder will have first priority and the charge granted subsequently will have only a second priority right over the assets. Sometimes the agreement between the chargeholder and chargor prohibits the creation of further charges. This is referred to as a "negative pledge clause". In such cases, the creation of subsequent charges is a breach of agreement and may have contractual consequences. The charge created subsequently, however, will still be valid (see 4.1.9).

1.2.7 *Can a pool of assets be charged?*

It is possible to charge assets described generally without having to identify them individually, for instance 'all machines deposited in a [given] warehouse', or 'all books in a library'. That 'pool' over which the charge is granted may be *static* or *increasing*. It may also be a *fluctuating* pool of assets where the individual assets that make up the pool are constantly changing.

1.2.8 Can an enterprise be charged?

It is possible to charge the entire assets of a company or a part of a business that can operate as a separate economic unit (see section 6).

1.2.9 What elements are automatically included in the charged property (e.g., fruits, additions, attachments)?

Fruits (that is, what the asset produces) will only be included if the parties have so agreed. As a general rule fruits will cease to be covered by a charge when they become detached from the charged asset. Additions and attachments will be included in the charge from the moment they are added or attached.

A charge over a cow will include its calf up to the moment of birth. A charge over a computer will include a new modem from the moment it is fixed into the computer.

Practice note: This rule may be modified by contractual agreement between the parties. Where fruits or additions are anticipated it may be advisable to provide for them expressly in the charge agreement.

1.2.10 If the chargor sells the charged assets, does the charge extend to the proceeds of sale?

The charge extends to the proceeds of sale only if the parties expressly so agree. The only case where such an extension is automatically provided by law is when the charged assets are sold in the interest of prevention of damage to the assets. A charge over proceeds of sale can be of limited value because of difficulties in identifying and tracing proceeds.

Practice note: Where the parties agree that the charge should extend to proceeds, it may be advisable to create a charge over the claim for the price payable by the purchaser as a charge over a receivable and/or a charge over the bank account into which the price is payable (see 1.2.3).

1.2.11 Does the charge extend to insurance rights and/or proceeds?

Insurance proceeds arising from the destruction or loss of value of the charged assets are automatically covered by the charge.

Practice note: It is not clear how the right to insurance proceeds under the law works in practice. It may be preferable for the chargeholder to include expressly all rights under the insurance policy in the description of the charged assets rather than relying on the law. The chargeholder should be shown as payee in the insurance policy.

1.3 The claim that needs securing

1.3.1 What claims can be secured by a charge?

Any monetary claim or debt can be secured by a charge provided that it can be enforced by judicial proceedings. The secured debt may be denominated in any currency, may be of a

fixed or varying amount (subject to a maximum) and may include claims that are conditional or will arise in the future. The law is not restricted to bank lending but covers credit given by any person. The debt may be from a customer to his supplier, from one group company to another, from one member of a family to another, etc.

1.3.2 *Can a charge secure a future claim?*

A claim which is not yet in existence, or which is subject to a condition, may be secured. The maximum amount of the claim, however, must be shown on the Register, where applicable (see section 3). In practice, the creation of the charge is often a condition precedent to the disbursement of a loan, in which case the charge secures a future claim.

On 1 February a bank enters into a loan agreement with a manufacturing company, agreeing to lend HUF 50 million subject to receiving:

- (a) a charge over its raw materials, work in progress, inventory and receivables from customers, and
- (b) specified financial information and a certificate from the company's auditors.

The charge is created, i.e. registered, on 5 February, the financial information and auditors' certificate is delivered on 20 February and the loan is advanced on 25 February. Between 5 and 25 February, the charge has secured a future claim.

1.3.3 *Can a charge secure a fluctuating claim (e.g. a bank overdraft or a trading account)?*

When parties are in a continuous commercial relationship (supplier-purchaser, bank-customer, etc.) they may want to secure all claims arising out of this relationship, e.g. the regular supply of goods to a customer or an overdraft on a bank account. The secured debt will fluctuate (increase and decrease) in its amount during the life of the charge as new debts are incurred and as payments are made. At any particular time, the secured debt will be the amount then outstanding from the customer or on the overdraft.

It is possible to give a charge to secure such a debt by including on the Register a description of their commercial relationship and the maximum principal amount secured by the charge. This is called a "framework charge" (*Keretbiztosítéki jelzálogjog*).

A charge may be created to secure, for example:

- all amounts advanced from time to time under a loan facility up to a maximum outstanding at any one time of HUF 10 million, or
- all amounts which may be due from a customer to his bank (whether for loans, overdraft, foreign exchange or any other transactions) up to a maximum at any one time of HUF 40 million, or
- all amounts which may be due at any time from a customer to a supplier up to a maximum of HUF 5 million.

1.3.4 *Can a charge secure a claim expressed in a foreign currency?*

It is possible to express the claim in a foreign currency. There is a specific field in the registration statement that requires the claim's currency to be expressed.

1.3.5 *What is included in the secured claim? Interest? Costs? Damages?*

The charge covers interest, costs of enforcement of the claim and of the charge, and necessary expenses incurred in connection with the charged asset.

For a registered charge, the incidental claims have to be indicated in the Register. This may be done, however, by referencing the charge agreement without indicating the actual amounts.

2. CREATION OF A CHARGE

2.1 How to create a charge?

To create a charge, other than a statutory charge (see 4.4.4), there needs to be an agreement (the charge agreement as distinguished from the loan or credit agreement, although this could be included in the same document) and, in most cases, some form of publicity (see section 3). Failure to comply with any of the formalities can result in the charge being invalid.

2.1.1 *What form should the charge agreement take? Written agreement? Notarial deed?*

In all cases, including possessory charges, the charge agreement should be in writing. Whether a notarial deed is required depends on the nature of the assets charged and on the type of charge that is to be created.

A notarial deed is required for:

- a registered charge on movable tangible assets (goods, machinery, equipment etc.)
- an enterprise charge (see section 6)
- a charge on aircraft or ships.

A notarial deed is **not** required for:

- a charge on immovables (land, buildings etc.) - the document must only be countersigned by an attorney in law
- a possessory charge
- a charge on rights and receivables, including intellectual property rights.

Practice note: Where a charge covers a mixture of assets, for example, all the inventory of finished products of the debtor together with the receivables due from customers to whom those products are sold, it is possible to create a charge. This can be in a single document which must be a notarial deed (because the charge covers goods) or in two separate documents, a notarial deed for the inventory and a private agreement for the receivables.

It is often preferable to have a notarial deed, even where it is not a requirement, in order to facilitate enforcement (see 5.3.1 and 5.4.4).

2.1.2 *What must the agreement contain?*

Where the charge is registered in the Charges Register (see 3.2), the charge agreement serves as the basis of the entry in the Register and, therefore, the notarial deed should contain the information that has to be registered (see 3.2.3).

In other cases, there are no particular requirements as to the contents of the charge agreement, except that as a minimum the charge agreement should include:

- the identification of the parties
- a description of the charged assets
- a description of the secured claim.

The Parties

The parties will be referred to in the charge agreement by their name (first name and surname when physical persons, registered name and identification data when legal persons), and address. In case of a legal person, the role and powers of the representative will also be mentioned.

Charged asset(s)

The charge agreement may describe the charged asset(s):

- individually, by reference to specific characteristics of the charged asset (serial number, precise description and location, etc). This is mandatory for immovables and other registered assets, and where the charge covers a single asset the nature of which allows specific description.
- generally, by describing the general characteristics (type, amount, location, etc).

Practice note: The description must be adequate to identify the individual assets that are covered by the charge, and to alert third parties that the assets are subject to a charge. A vague or ambiguous general description may make it more difficult for the chargeholder subsequently to enforce the charge against a third party who has obtained the charged asset (see 4.1.11).

Secured debt

The secured debt should be described by:

- the nature of the debt, for example by reference to the underlying transaction – loan, credit line, etc – or to the contract under which the debt arises
- its currency and principal amount or maximum principal amount, together with a description of interest costs and other additional amounts that are covered
- its due date, and
- identification of the debtor in case it is different from the chargor.

The agreement should also contain the contractual terms agreed between the chargor and chargeholder regarding the charge. In particular, there must be a clause by which the parties expressly consent that the described asset will serve to secure the described debt.

2.2 What are the costs of creating a charge? How long does it take?

The principal costs are the notarial fee for the notarial deed and the registration fee. Notarial fees on the charging instrument are calculated on a degressive scale depending on the amount secured.

Secured debt amount in HUF	Notarial fee in HUF	Notarial fee in Euros*
1-10,000,000	81,700	297
10,000,001 - 200,000,000	81,700 plus 0.25 per cent of the debt over 10,000,000 81,700 – 556,700	297-2,025
> 200,000,001	556,700	2,025
* For information only, based on exchange rate €1 = HUF 275		

In some circumstances the normal fee can be halved or doubled. Notarial fees might be doubled when (1) the transaction is large, complex and hard to settle; (2) the public notary needs to act out of business hours or out of the office; (3) it is necessary to prepare the deed in a foreign language.

The notarial fee might be halved if (1) the deed is prepared on the basis of the draft provided by the parties without altering the draft; or (2) it is justified in all the circumstances.

The registration fees are set out in 3.2.5. Additional costs may be incurred by the parties, for example for professional advisers.

Creating a charge is essentially a simple process. In most cases, the preparation of the charge agreement should be quick. Additional time may be incurred, however, due to the complexity of the transaction or the difficulty of negotiations. Once the charge agreement is completed in notarial form, registration at the Charges Register should take a matter of minutes. (This may be different for immovables, see 3.3.4).

2.3 Is there a risk of the charge being declared invalid if the chargor becomes insolvent soon after its creation?

The charge will not be invalid simply because it was created close to the commencement of insolvency proceedings. If, however, the charge was created less than a year before the opening of liquidation proceedings, the insolvency administrator or any creditor may challenge its validity. They will need to prove that the security was taken for no consideration or to reduce the property of the chargor or to deceive other creditors. In addition, the priority ranking of the chargeholder's claim is different according to whether the charge was created more or less than one year prior to the commencement of the liquidation procedures (see 4.4.7).

3. PUBLICITY: INFORMING OTHER PERSONS OF THE EXISTENCE OF THE CHARGE

Once the parties have entered into a charge agreement, they are contractually committed to each other. However, in most cases the charge is not created until other necessary formalities, principally designed to “publicise” the existence of the charge, have been fulfilled. The two basic forms of publicity are taking possession and registration.

Where the chargeholder takes possession of the charged assets (a possessory charge), the assets have to be handed over to the chargeholder or a third party. Where the charge requires registration it has to be registered in the relevant registry.

An exception to the need for publicity exists in the case of charges on rights and receivables which do not require registration (except in the case of registered intellectual property rights) and where transfer of possession is not possible. However, the charge cannot be enforced until the obligor of the charged right or receivable is notified of the charge (see 4.1.6 and 5.4.6). Another exception is the case when the charge is created by virtue of the law (see 4.4.4).

3.1 Which charges have to be registered and where?

Publicity through registration is a condition of validity for the following types of charges:

- charges over tangible movable assets: at the Charges Register
- charges over immovable assets: at the Land Register (Cadastre)
- charges over trademark, patent, design and related rights: at the Industrial Property Registry kept by the Hungarian Patent Office
- charges over ships or aircraft: at the Ships or Aircraft Registries kept by the Central Traffic Supervision/Air Traffic Authority.

Although a registry for motor vehicles is held at the local municipalities, this is not a title registry and charges do not have to be registered there. Motor vehicles are charged in the same way as other movable tangible assets, by registering the charge in the Charges Register.

Practice note: A person who purchases a second-hand car should check the Charges Register unless he purchases through a dealer (see 4.1.11).

3.2 The Charges Register: How does registration work?

3.2.1 Where is it registered?

The Charges Register (*zálogjogi nyilvántartás, ZONY*) is maintained by the Hungarian Chamber of Notaries (*Magyar Országos Közjegyzői Kamara*) and entries can be made by any notary. The initial registration of the charge will probably be made by the notary who draws up the notarial deed of charge. Subsequent registration of amendments may be made in the office of any notary, during office hours (8:00 a.m. to 4:00 p.m.). The Register consists of a single centralised database, which can be inspected by any member of the public at any notary’s office.

3.2.2 *What is the procedure to obtain registration?*

Before signing the charge deed, the notary establishes whether there is already an entry under the name of the chargor in the Register. If there is not, the notary will create one. Then the notary makes a reservation in the Register, which prevents any other party from registering a charge against the chargor. This reservation cannot be maintained beyond the end of the working day when it is initiated. This reservation can also be made at terminals which are “read only” (see 3.2.8): this means that a notary could establish a charge agreement within the offices of a bank, make a reservation on the chargor’s entry from the bank if it possesses a read-only terminal, and then return to his office to perform the registration, since that is only permitted at a notary’s office.

Any entry of the charge is registered on the basis of a request by the chargor (unless the charge is created by court order or another administrative ruling). The application is prepared by the notary on a standard, computer-based form detailing the charging instrument and the information provided by the parties. The chargor signs a print-out of the registration application before registration occurs.

Once the print-out is signed, the notary transmits the information to the central system of the Charges Register by electronic means. When the registration is completed (it normally only takes a few minutes), the notary issues a print-out of the entry of the charge in the Register in the form of a certificate. Every party to the notarial deed receives a certificate of registration.

The notary need only check the identity of the parties who are present and that the required information for registration has been provided. Due diligence on the charged assets, the secured debt and any other matters must be performed by the parties.

Practice note: The creditor must check carefully that the information registered is correct. Any defect in the validity of the charge cannot be made good by registration (see 3.2.10).

If the secured debt is shown in the Register as €10,000, but in the charge agreement as €5,000, the charge will only secure €5,000. However, only the sum indicated in the Register, will be secured, even if the charge agreement shows a larger sum.

If the charged assets are described in the Register as all the machinery at X and Y location, but the charge agreement only refers to X location, the machinery at Y location will not be charged. Similarly if the charged assets are described in the charge agreement as all the machinery at X and Y location, but the Register only refers to X location, the machinery at Y location will not be charged.

If the chargor does not own the charged assets as described in the Register, the charge will not be valid (but see 1.2.5 for future charge).

3.2.3 *What information has to be registered?*

The law describes precisely what information must be registered:

Parties: Personal details of the parties (chargor and debtor if different from the chargor, and chargeholder):

- in the case of natural persons: surname and given name, previous name, date of birth and – if they consent to it – address
- in the case of a legal entity (e.g. limited liability company (*korlátolt felelősségű társaság*), company limited by shares (*részvénytársaság*)) or business association without legal entity (e.g. partnerships): name, registered office, identification data (number of incorporation, failing which, a tax number)
- in the case of other organisations: identification data.

Charged assets: The description of the charged assets can be exactly the same as the description in the charge agreement (see 2.1.2) or a shortened version. Alternately, it may be a reference to the document or the annex of the document which serves as a base for the charge, in which case the assets' nature (the name used in everyday or in commercial practice) must also be indicated in the Charges Register. The field in the Register for description of assets is limited to one page (A4), so concision is required.

In the field of “charged assets”, the Register can mention: “All the company's computers located at the headquarters and all offices and branches”.

It can also read: “all the machinery and equipment, present and future, of the company as described in the charging agreement of X February 200X”.

Practice note: The description of the charged assets should enable a third party to identify what is, and what is not, covered by the charge.

Secured debt

- basis of the secured claim (e.g. loan agreement, supply agreement)
- currency
- due date
- amount and/or its maximum amount
- the incidentals to the secured debt, such as interest and costs; these do not have to be quantified and may be covered by reference to the charge agreement.

The following additional information is also registered:

- the name, address and registration number of the notary carrying out the registration
- the type of charge
 - registered charge over tangible assets
 - registered independent charge over tangible assets
 - enterprise charge
 - independent enterprise charge
 - registered framework charge
 - registered framework enterprise charge
 (For framework charges see 1.3.3, for independent charges see section 7 and for enterprise charges see section 6.)
- the day and time at which the charge was registered, which is entered automatically by the system.

Subsequent to the initial registration, further information must be registered including:

- amendments to the information shown on the Register
- termination of the charge
- maintenance of priority of a deleted charge (see 4.4.6), and/or agreed changes in priority (see 4.4.2)
- transfer of the secured claim
- date, reference number and issuing authority of judicial or administrative proceedings aimed at the enforcement of the charge and/or concerning the charge.

3.2.4 How long does it take?

Once the charge agreement is completed in notarial form, registration should take a matter of minutes.

3.2.5 How much does it cost?

The basic registration fee for a new entry, changes to an existing entry and deletion is HUF 5,000 (approximately €18). This is paid in addition to the fee for incorporating the charge agreement into a notarial form (see 2.2). In some circumstances the notary may claim an additional fee to recover expenses.

3.2.6 Can registration be refused? If yes, on what grounds?

Registration can only be refused if there is not a notarial deed, the information for registration is incomplete or the fee is not paid.

3.2.7 What information in the Register can be searched? And by who?

Anybody may have access to all information included in the Register by searching under the name of the chargor and may take notes or obtain a print-out.

3.2.8 How can searches be made?

Searches can be made at any notary's office. Some banks and other organisations have direct read-only access to the registration system, which enables them to make their own searches.

Practice note: The search engine is relatively sophisticated, so it is possible to conduct a search with only very basic information about the chargor (such as the first few letters of their surname). The system will display all the entries that match these first letters. However, it is preferable to search based on the chargor's date of birth, or identification data for legal persons, in order to avoid the risk of spelling discrepancies in the chargor's name.

3.2.9 How long does the search take and how much does it cost?

Once the search criteria are entered into the search terminal, the search result is almost immediate. The basic search fee is HUF 1,000 (approximately €4).

3.2.10 To what extent can a third party rely on the registered information?

The Charges Register provides evidence that the charge agreement was entered into by the parties before the notary. A third party may not rely on any other information in the Register, but should verify it for himself. However, a third party can rely on the absence of information in the Register. A registered charge cannot be created without registration. Therefore, if no charge is shown in the Register, a third party can assume that no registered charge exists (in certain cases there may be a statutory charge over the asset - see 4.4.4).

3.3 Non-possessory charge over registered assets: How does registration work?

Some assets are registered in specific registries, and a charge over them will need to be specifically registered in the respective registry.

3.3.1 Patents, licences, registered trademarks, and other intellectual property rights

Trademarks, patents, design rights, and related rights are registered in registers kept by the Hungarian Patent Office. A written registration request must be presented with the charge agreement attached. Registration can be refused if there is a formal defect or if it is evident from the charge agreement that it is not valid. The Patent Office has a 30 day deadline for completing the registration process. The registration fee for a new entry, changes to an existing entry and deletion is HUF 10,000 (approximately €36).

3.3.2 Ships and aircraft

A charge over a ship or an aircraft is created by registration of the charge in the Ship or Aircraft Registries kept by Central Traffic Supervision/Air Traffic Authority. The charge agreement must be prepared in the form of a notarial deed. In the case of ships, there is a 30 day deadline for completing the registration process. The registration fee for a new entry, changes to an existing entry and deletion is HUF 10,700 (approximately €39). In the case of aircraft, the deadline is the same. The registration fees for a new entry and changes to an existing entry are HUF 53,000 (approximately €193) and deletion is HUF 17,600 (approximately €64). In the case of ships, registration in the Charges Register may also be required.

3.3.3 Shares and securities

The law is not clear on whether securities can serve as a non-possessory charge. Therefore, it is preferable to create a charge over securities by way of depositing it with the chargeholder or with a third party (security deposit). In the case of dematerialised securities, the chargor would instruct its brokerage firm to place the securities in a closed sub-account.

Shares in some companies (*korlátolt felelőséű társaság, közhasznú társaság*) legally qualify as mere rights and the trading of these shares are restricted. (Such shares are usually referred to as quotas or participations.) A charge can be created on such quotas merely by concluding a charge agreement without registration. The charge will not, however, be enforceable until it has been notified to the company.

Practice note: Where a security deposit agreement *is* used, the chargeholder can enforce the agreement by taking hold of the deposited securities to satisfy his secured claim without court involvement. In practice, the chargeholder would either acquire title over the securities or sell them to a third party. The arrangement is a special form of charge (*óvadék*).

3.3.4 *Charge over land and other immovable assets: How does registration work?*

Immovable assets are registered in the Land Registry kept by the Land Bureaux. All details of the immovable asset are registered, including charges. The registration shall be requested by the chargeholder (in case the charge agreement does not provide otherwise), within 30 days from the conclusion of the charge agreement. If delayed, the chargeholder shall pay a late fee (with a maximum of HUF 200,000). The registration fee is 5 per cent of the amount of the secured claim, with a maximum of HUF 10,000 (€ 36). The fee for the deletion of the charge is HUF 2,000 (€ 72).

It may take considerable time to obtain registration of the charge, but the request for registration is immediately indicated in the registry to protect the creditor's interest and to alert third parties. A person may also, up to one year in advance, register his intention to create a charge over his property, up to a specified amount (see 4.4.6).

It is possible for notaries and lawyers, if requested by a party, to request an excerpt from the Land Registry: the notary or the lawyer has to enter the parcel number and request the excerpt to the Charges Register. The Register's control centre then requests the excerpt from the Land Bureaux by electronic means and forwards it to the notary's personal folder in the Register's system. The notary may then print it out and hand it over to the interested party. This procedure takes about 5-10 minutes.

3.4 Possessory charges on movable tangible assets: How does possession work?

Transfer of possession is a condition of validity of the charge. It can be made to the chargeholder or to a third person who acts as custodian and has possession on behalf of the chargeholder. The role of the custodian and the terms on which he acts are a matter for agreement between the parties.

There is a specific legal regime for goods deposited in public warehouses, which is widely used for security purposes. On deposit of the goods (for a set period of time, not exceeding one year), a two-part receipt is issued: a goods receipt and a lien receipt. The latter is endorsed in favour of the creditor and the goods may not be reclaimed until both parts of the receipt are handed over to the warehouse.

For further information on a possessory charge, see also 4.5.3.

4. THE LIFE OF A CHARGE

The right created by a charge is only exercised in the exceptional circumstance of the debtor failing to pay. Unless and until that happens, the charge remains dormant. This section examines the transactions and events that may take place in the mean time, which may nonetheless be affected by the existence of the charge.

4.1 The charged assets

4.1.1 *Can the chargor use/consume the charged assets?*

When the chargor remains in possession of the charged assets, he is entitled to make normal use of them subject to maintaining them in good condition. This probably extends to consumption of the assets (e.g. as part of a manufacturing process) where that would be normal use. In such a case, the obligation to maintain the collateral means that the chargor will have, unless otherwise agreed, to replace the consumed assets with new ones so that a given amount is always there. The parties may make their own agreement as to the use of the assets.

Practice Note: Where the chargor expects to consume the charged assets (for example, in the case of raw materials used in a manufacturing process), it is preferable for this right to be expressly stated in the charge agreement.

For the right to sell the charged assets, see 4.1.10.

4.1.2 *What are the duties to maintain the charged assets?*

In the case of a registered charge, the chargor is responsible for maintaining the charged asset in good condition. If the deterioration of the state of the charged asset jeopardises the ability to realise on enforcement, the chargeholder may request the restoration of the charged asset. Where the chargeholder is in possession of the charged assets, he may not use them (unless otherwise agreed), but he is entitled and obliged to collect their natural proceeds.

4.1.3 *In what circumstances is the chargor obliged to substitute new assets?*

In the event of deterioration, loss or destruction, the chargeholder may, subject to the terms of the charge agreement, request the chargor to provide additional assets to be charged, unless the chargeholder himself was responsible for the damage.

Practice note: If substitution of the charged asset is likely at some point during the life of the charge, it is preferable for the parties to describe the charged assets in a manner which is sufficiently broad to include the substituted (future) asset.

A company has charged all its production machinery used in a specified manufacturing process. At some point, part of this machinery needs replacing. As the description of the charged assets also refers to all machinery that the company may acquire in replacement of its production machinery, the new part will automatically be covered under the original charge.

4.1.4 *In what circumstances can the chargor elect to substitute new assets?*

The chargor cannot unilaterally elect to substitute new assets. In agreement with the chargeholder, he may do so if the description of the assets is wide enough to cover the assets to be substituted. If it is not, a new charge has to be created.

There is an exception for possessory charges: where there is a danger of deterioration of the state of the charged asset or significant loss of its value is feared, the chargor may request the return of the charged asset while offering other appropriate security.

4.1.5 Does the chargor have to insure the charged assets?

The law does not put the chargor under any obligation to insure the charged assets, but this will often be required contractually.

4.1.6 What are the specific requirements of a charge over claims or receivables?

When a charge is taken over claims that the chargor has against a third person, for example receivables, the question arises whether that third person (the “obligor”) needs to be informed of the charge. Notice to the obligor is not a requirement for the existence of the charge, but it is a requirement for its enforcement (see 5.4.6). Subject to any agreement between chargor and chargeholder, notice may be given at any time.

Where performance of the charged claim consists of payment of a sum of money, the effects of the notice are as provided in the charge agreement. If the charge agreement does not make any provision, the effects are as follows:

- Before the charge has become enforceable, the obligor must perform to the chargor and the chargeholder jointly. If required by the chargor or the chargeholder, performance could be by deposit with the court for the benefit of both of them.
- When the charge is enforced, the obligor must perform only to the chargeholder, unless the claim was assigned to a third party as part of the enforcement process.

During the life of the charge, the chargor is not entitled to make any declaration terminating or changing adversely the charged rights or receivables without the consent of the chargeholder. On charges over bank accounts, see 4.1.7.

Practice note: It is preferable to include in the charge agreement provisions covering:

- when and how the obligor can be informed of the charge
- how the obligor is to make payment after notice has been given
- how the chargeholder shall account to the chargor for payments received.

A company may give a charge to its bank over receivables payable by its customers. The charge is established by the charge agreement. The bank may be prepared to allow customers to continue paying directly to the company if the charge agreement:

- (i) provides a satisfactory mechanism for notice to be given to the customers at any time the bank feels appropriate
- (ii) provides that after such notice payment should be made by customers directly to the bank.

4.1.7 How does a charge over a bank account work?

When a bank account is charged, the charged asset is the claim of the customer against his bank. The charge may be set up in a way which allows the continued operation of the account, permitting the customer to withdraw and transfer funds on the account. Meanwhile the chargeholder will have the right to suspend these operations under pre-defined conditions. In practice, the chargeholder will notify the bank of the existence of the charge at the time of its creation. At the same time, the chargeholder will deliver an authorisation to the bank from the chargor, to act in accordance with a “prompt collection order” delivered by the chargeholder upon occurrence of pre-defined conditions. Usually a minimum balance is set which must be kept in the account by the chargor.

4.1.8 Can subsequent charges be granted over the previously charged property?

An asset may indeed be charged several times to different chargeholders to secure different debts (see 1.2.6).

A manufacturing company gives credit to a customer secured by a charge over a new machine it has supplied. The customer later grants a second charge to its bank over all its machinery and equipment to secure a working capital loan.

4.1.9 What if there is a negative pledge clause?

Parties may include in the charge agreement an obligation on the chargor not to create further charges over the same (or other) charged property. This is valid as between the parties but will not be effective against third parties.

In an agreement with a manufacturing company (see 4.1.8), the customer undertakes not to create any further charges over the machine. The later charge to the bank is valid, but the customer will be liable to the manufacturing company for breach of its agreement.

See also 1.2.4 regarding prohibitions that can be registered at the Land Register.

4.1.10 Can the chargor sell the charged assets?

There is nothing in the law which prevents the charged assets being sold. Parties may include in the charge agreement a prohibition on sale of the charged property. This is valid as between the parties, but will not be effective against third parties. If the charge agreement is silent on this issue, then the sale is permitted but a separate question arises of whether the purchaser acquires subject to the charge (see 4.1.11). As an exception, such prohibition would be effective in the case of an immovable asset, if it was in favour of an unpaid vendor and was registered in the Land Registry.

4.1.11 What happens if the charged asset is sold to a third party?

The charge creates a proprietary right over the asset and, subject to exceptions discussed below, this continues notwithstanding any change of ownership of the assets. Thus, if the owner of the charged assets sells those assets to a third party, the acquirer of the charged assets acquires them subject to the charge. The acquirer does not, however, become liable for the secured debt: the chargeholder's right is limited to his right to enforce against the charged asset to obtain satisfaction of the secured debt. The acquirer's right to recover from the original chargor will depend on the terms on which he acquired the asset.

The customer sells the machine to another company (see 4.1.8). Later it fails to repay the credit to the manufacturing company when due. The manufacturing company has the same rights to enforce the charge against the purchasing company as it would have had against the customer.

The entry for the charge in the Charges Register must be amended and an entry must be made against the name of the acquirer as chargor. The duty of the registration of the amendment is on "the person causing any change and the person interested in the occurrence of a change". Therefore, the original and the new chargor (provided he is aware of the existence of the charge) and the chargeholder would seem to be jointly responsible. Practically, it means that either of them may submit a registration request. However, the parties are required to cooperate in fulfilling this obligation by providing each other with the necessary statements. They should request registration of the amendment in the Charges Register within 15 days from the date of the transfer or 15 days from the date where they become aware of the transfer.

Practice note: When acquiring assets, which could be subject to a registered charge, it is important to check for any charges in the relevant registry, unless one is certain to fall within the exceptions below.

In the case of registered assets, for example land, the position is different as the change of ownership of charged assets will always be registered in the relevant registry (e.g. Land Register) and no additional registration is required in respect of the charge.

Exceptions

There are four cases where the charged asset is transferred free from the charge:

- the charged asset is sold in trade activity to a buyer in good faith (for example a purchase in a retail shop)
- the charged asset is sold in the ordinary course of business activity to a buyer in good faith (for example a wholesale purchase of an article that is produced by the seller)
- the asset, which is a usual thing of every day life, is acquired by a buyer in good faith against countervalue (this covers transactions of small value that usually occur between neighbours, colleagues or friends)
- the asset was part of a pool that is charged by an enterprise charge (see section 6).

A dealer in agricultural equipment gives a charge over all its stock to its bank. A farmer who purchases a tractor from the dealer will acquire it free of charge. In order to finance the purchase, the farmer takes a loan from his bank, secured by a first ranking charge on the same tractor. The farmer then sells the tractor to his neighbour. The neighbour will acquire the tractor subject to the charge in favour of the farmer's bank as, unlike the agricultural equipment dealer, the farmer is not in the business of selling tractors nor is the tractor "a usual thing of everyday life".

4.2 Can the secured debt be transferred?

Secured debt can be transferred in the same way as any other debt. Unless the parties otherwise agree, the charge will follow the debt and the transferee will become a secured creditor of the debtor in the place of the transferor. The entry in the Charges Register should be amended to reflect the transfer. The only consequence of not amending is that the new chargeholder may be prevented from enforcing since he would not appear as "chargeholder" on the Register. This can always be remedied, however at the time of enforcement. If the chargeholder transfers the secured debt without the charge, the debt becomes unsecured and the charge terminates since it cannot exist independently from the debt (see, however, section 7 on independent charge).

Practice note: The person to whom a secured debt is transferred should ensure that he is registered as the new chargeholder. In order to avoid any difficulty in obtaining registration, he should require the transferring chargeholder to make the change in the Register at the time of the transfer.

4.3 The Register

4.3.1 *Do the parties need to renew the registration?*

Registration is valid until the charge terminates and there is no need to renew.

4.3.2 *Does additional information need to be included in the Register?*

Subsequent to the initial registration, amendments and some new information must be registered. In particular, identification of the new chargor (see 4.1.11) and new chargeholder (see 4.2), termination of a charge (see 4.5), transformation of an enterprise charge (see 6.3), commencement of a judicial enforcement procedure (see 5.2.3), as well as any changes in the registered details of the parties must all be registered. Upholding of a priority order (see 4.4.6) or swap of positions (see 4.4.2) must also be registered to be effective against third parties.

The duty of the registration of the amendment is jointly on "the person causing any change and the person interested in the occurrence of a change". They must request registration of the amendment in the Charges Register within 15 days from the date of the change or from the date of becoming aware of it.

A distinction must be made between amendments that in effect result in a new charge (for instance, modification of the charged assets increasing the scope of assets) and amendments to the initial registration that do not result in a new charge (change of identity of the parties).

A person gives a charge over ten paintings. Six months later he changes address and registers his new address in the Charges Register. He then extends the charge to cover five further paintings he has acquired. This cannot be registered as an amendment to the charge, since in reality it is a new charge over the five paintings and must be registered as such.

Practice note: If the charged assets in the original charge had been described as the ten paintings plus any further paintings that the chargor may acquire, the five paintings would have been included in the original description of the charged assets and so no new registration would have been required.

4.4 How is the priority of a chargeholder determined?

4.4.1 *Vis-à-vis other chargeholders*

If several charges were created over the same assets, chargeholders are entitled to satisfaction in the order in which the charges were created. For registered charges, it is the time of registration that determines priority. For possessory charges, it is the time of giving possession (or the date of the charge agreement if the chargeholder was already in possession of the assets). For charges over rights and receivables, it is the time of the charge agreement (not the time of giving notice to the obligor of the charged debt).

The priority for charges over after-acquired assets (see 1.2.5) is from the time of registration (but see 4.4.5) or, in the case of rights and receivables, the time of creation, that is, the time when the chargor acquires the right or receivable.

If three charges are created over the same future receivable, they will all be ‘created’ at the same time (when the receivable comes into existence) and will therefore rank *pari passu*.

4.4.2 *Where there is agreement for change of priority or subordination*

In the case of registered charges, chargeholders can agree amongst themselves to a different order of priority and have the changed order registered. The agreement is only effective upon registration, and has no effect against a chargeholder who is not party to the agreement if it has a negative impact on the enforcement of his claim.

4.4.3 *Vis-à-vis other enforcing creditors*

An unsecured creditor may start judicial enforcement against a debtor’s assets for payment of his claim. This procedure may cover the charged assets. Should the charged asset be affected, the chargeholder may join in the judicial enforcement procedure. In this case, he does not lose his priority, but he is prevented from exercising his rights of non-judicial enforcement (see 5.2.4) as of the day of sequestration of the charged asset. The chargeholder will have a prior right in the proceeds of sale from the judicial enforcement.

4.4.4 *Vis-à-vis creditors benefiting from statutory charges*

Creditors with statutory charges may exercise a preferential right to the extent of their claim which relates to the asset (regardless of the time when the charge was created).

This may be relevant, for example, to warehouse keepers, carriers and forwarders vis-à-vis the assets in their possession.

4.4.5 Charges over the charged assets created by previous owners

If the charged asset acquired by the chargor is already subject to a charge, the charge created by the previous owner will have priority over any charge created by the chargor. The chargor can only grant a charge on the title he acquires. If he acquires the asset subject to a charge, then he can only give it as security subject to that charge.

In October 2001, a farmer gave his bank a charge over all his present and future farm equipment and machinery. In January 2002, he acquired a tractor from his neighbour; the tractor is already subject to a charge given by the neighbour to a finance company in November 2001. The charge in favour of the neighbour's finance company (although given after the farmer's charge to the bank) will have priority over the bank's charge.

Note that in practice a charged asset may often be transferred free from the charge (see 4.1.11).

4.4.6 Special rights to ranking

A person may also, up to one year in advance, register his intention to create a charge over his real property (immovable) up to a specified amount (see 3.3.4). The priority rank of the pre-registered charge will be defined by the date of the pre-registration.

Upon termination of a registered charge over either movable or immovable property, the chargor may grant a new charge over the same assets ("involving no greater encumbrance"). This charge can have the same priority as the terminated charge, and can also retain this priority position for one year from the deletion of the registered charge.

Practice note: When taking a charge over assets which are already charged, or which have been subject to a charge within the previous year, there is a danger that the prior or former charge will be renewed. It is preferable to obtain a renunciation from the chargor of his right to do this.

4.4.7 Insolvency

Where the chargor is insolvent, the chargeholder retains his priority right for 50 per cent of the price received on the sale of the charged asset by the liquidator, after expenses. For any balance of debt, but only up to the sale proceeds of the charged asset, the chargeholder ranks second behind all the costs of the liquidation. (These include costs of cessation of the debtor's business, expenses of the sale of assets and enforcement of claims, judicial and administration costs and the liquidator's fee.) This applies to charges created in good faith and for consideration a year or more before the starting date of the liquidation proceedings. For charges created in good faith and for consideration less than one year before the start of liquidation, the whole of the chargeholder's claim up to the sale proceeds ranks behind the liquidation costs (see also 2.3). Any claim in excess of the sale proceeds is unsecured.

4.4.8 *Are there any specific preferential rights granted to third parties that the chargeholder should be aware of?*

In case of immovables, ships and aircraft the claims secured by a charge shall be satisfied only following claims for:

- child support
- other support
- employee's wages and other employment-related benefits.

The above preferences apply only when enforcement is led by the court, the claims are enforced against the same collateral and the proceeds of the enforcement are insufficient to cover all claims.

4.5 **Can a charge be terminated without the express consent of the parties?**

4.5.1 *When the charged property ceases to exist? Loses value?*

If all things, rights and assets encumbered by the charge are destroyed, the charge will automatically terminate. However, if the chargor is responsible for the destruction or loss of value, the chargeholder may require the chargor to provide an appropriate new charged asset or additional assets adding value to the extent of the loss. Such extension of the charge to the new assets may require registration. The insurance proceeds paid to compensate for the destruction of the charged asset and/or its loss of value are substituted for or added to the charged assets. If the charged asset is sold to prevent damage, the purchase price is automatically substituted for the charged asset. See also 4.1.5.

Practice note: The charge agreement may provide what will happen when the charged assets are damaged or destroyed, for example immediate acceleration of the secured claim or replacement with additional security.

4.5.2 *When the charged property ceases to be identifiable or separable or becomes incorporated with other property which is not charged?*

Charged assets may be merged or incorporated into other assets and, thus, cease to be identifiable or separate. This is the case when raw materials are used in a manufacturing process and become merged or incorporated to new goods. For example, steel becomes part of a car, yarn becomes part of clothing, etc. In such a case, Hungarian law does not provide clear guidance and it may be advisable for the parties to cover the position in their charge agreement. For instance, parties could provide that the charge ceases over any assets when they are incorporated or merged, and, if they so agree, add an additional charge over work-in-progress.

<p>A charge is granted over stocks of steel, which are to be melted and incorporated into some other material as part of the manufacturing process. The parties to the charge may agree that the security will also cover the products which are produced with the steel up to completion of the manufacturing process, or up to sale to customers.</p>

4.5.3 *For a possessory charge, when the chargeholder ceases to have possession?*

The charge ceases if the chargeholder returns the charged asset to its owner or if the chargeholder loses possession of the charged asset and within one year neither regains possession nor applies to court for this purpose.

Practice note: A possessory charge may remain in existence for up to one year from the time when the chargeholder loses the possession or longer where there are court proceedings.

4.5.4 *When the secured debt ceases to exist or is transferred without the charge?*

The charge shall cease to exist if the debt ceases to exist or becomes time barred, unless another person (e.g. a guarantor) has satisfied the secured debt. In this case, the charge may continue to secure the recourse claim of the person who has made payment. If the debt is transferred without the charge (see 4.2), the charge will also cease. The parties may agree that they terminate the secured debt and transform the existing charge to an independent charge (see section 7).

4.6 **Can the chargor and chargeholder agree to terminate the charge? Can the chargeholder waive his right to the charge?**

Yes, but it will only be effective towards third parties if the charge is deregistered or dispossessed. If the chargeholder assigns the secured claim without de-registration of the charge, the new creditor will be able to enforce it against the charged asset and the debtor will not be able to successfully object such enforcement. The debtor will only be able to sue the original creditor for breach of contract.

5. ENFORCING THE SECURITY

Enforcement is the ultimate stage of the security right. The charge gives the chargeholder the right to seek satisfaction from the charged asset if the chargor fails to perform his obligations. Although the majority of charges will never reach this stage, particular attention has to be paid to what happens on enforcement as the entire value of the charge depends upon it. In normal commercial practice, both parties should want enforcement to be fair, quick and efficient.

5.1 **When can the chargeholder enforce the charge?**

5.1.1 *When the secured debt is due and unpaid?*

Not paying the secured claim when due constitutes the most obvious failure of the chargor to perform his obligations.

Practice note: The trigger for the chargeholder's right to enforce is the debtor's failure to pay. It is, therefore, preferable for the time of payment to be defined without ambiguity.

5.1.2 *When the chargor becomes insolvent/bankrupt?*

If the chargor becomes insolvent, the chargeholder will not be allowed to enforce his right according to the charge agreement from the commencement of the liquidation. The chargeholder will be entitled to file his claim with the administrator who will confirm the existence of the debt and also the priority arising from the charge (see 5.5.1 and 4.4.7).

5.1.3 *When the chargor breaches other obligations to the chargeholder?*

The trigger for enforcement is failure to pay. Other failures by the debtor or chargor, for example failure to maintain the charged assets, will not automatically give a right to enforce. However, the law does provide a right for the chargeholder to enforce if the chargor does not comply with its obligations to restore or replace the charged asset or provide additional security (see 4.1.2 and 4.1.3).

It is usual to provide contractually for the creditor to be able to claim immediate payment if certain 'events of default' occur. In that way, the chargeholder can choose to 'accelerate' the debt if the chargor is in breach, and can then commence enforcement if there is a failure to pay the debt that has become due.

Practice note: The charge agreement or the credit agreement should define the procedures on default and the rights of acceleration.

5.2 **What are the basic procedures for enforcement?**

5.2.1 *How is enforcement commenced?*

When the parties have not entered into any agreement concerning enforcement, enforcement is via court procedure and commencement is by appropriate application to the court.

If enforcement is to take place in the manner agreed in the charge agreement (i.e. not through court procedure), or a subsequent agreement entered into prior to the commencement of enforcement, the chargeholder must give the chargor a preliminary notice of his intention to enforce under the terms of the agreement. The notice must specify:

- the charge agreement and, unless the charge agreement provides for the sale, the subsequent agreement
- the charged assets to be sold
- the amount of the claim together with its incidentals
- the date and triggering event (e.g. non-payment) or circumstance of the right of satisfaction.

5.2.2 *Is it necessary to involve the court?*

If there is an agreement between the parties that provides for out of court enforcement, and realisation is in the manner agreed between the parties, it is not necessary to involve the court.

5.2.3 Is enforcement publicised?

When enforcement is through court procedure, the date of commencement of the proceedings must be registered in the Charges Register (see 3.2.3) or, in the case of immovables, the Land Register.

5.2.4 What are the methods of realisation?

A charge can be realised by sale pursuant to the charge agreement (or other agreement between the parties entered into prior to the right to enforce arising) or by court procedure.

Where the sale is pursuant to an agreement, it may (subject to the terms of the agreement) be:

- a joint sale by the chargor and the chargeholder
- sale by the chargeholder acting alone (This is only possible if his business includes providing loans against security – e.g. the chargeholder is a credit institution – or if the charged assets have an officially registered market price – e.g. commodities traded on the commodity exchange.)
- sale by a person appointed by the chargeholder, who is professionally or officially dealing with providing loans against security and/or organising auctions.

The agreement must fix the lowest sales price or its method of calculation and must set the maximum period to complete the sale from the commencement of enforcement. For details of the procedures, see 5.4.

5.2.5 When can realisation commence?

Realisation by an agreed sale procedure cannot begin until 30 days after the delivery of the preliminary notice (see 5.2.1). The exception is perishable, goods where the chargeholder may choose an earlier date for sale.

5.2.6 How are the realisation proceeds distributed?

When realisation is by sale pursuant to an agreement, the chargeholder must give the chargor (and any other chargeholder joined to the sale) a written account of the sale (including details of all proceeds and costs), the secured claims satisfied from the charged asset and any remaining proceeds or assets that must be returned to the chargor. Unless objection is made within eight days, the chargeholder distributes in accordance with that account. On a court sale, distribution is made by the court.

5.2.7 How long should it take and what should it cost?

Out-of-court enforcement will take a minimum of 30 days from the delivery of the preliminary notice of enforcement. In practice, it is likely to take 60-90 days where there is a ready market for the charged assets.

Judicial enforcement is likely to take about six months for movables and rights and six to nine months for real property. The time can be considerably longer, however, in complex cases or where enforcement is contested (it may also be shorter in cases where the creditor is well prepared).

With regards the costs, court enforcement involves a number of fees. These fees are in addition to the parties' own costs (such as the fees of professional advisers) and any taxes payable on transfer of the charged assets. The costs include court fees (between 1 and 3 per cent with a maximum of HUF 150,000 (€ 545) in the lower courts and HUF 450,000 (€ 1635) in the higher courts) and bailiff fees that consist of a flat fee and a success fee. The flat fee is HUF 31,000 in cases where the value of the claim is HUF 1 million, HUF 111,000 in cases where the value of the claim is HUF 5 million and HUF 161,000 in cases where the value of the claim is HUF 10 million. Beyond HUF 161,000, fees are 0.5 per cent of the claim over 10 million. The success fee is HUF 500,000 in cases where the collected amount is HUF 5 million, HUF 900,000 in case the collected amount is HUF 10 million, beyond that is HUF 900,000 plus 5 per cent of the collected amount over 10 million.

In addition to the parties' own costs, an auction or a sale by a person who is professionally or officially dealing with providing loans against security will always involve the fees and costs of the auctioneer or the person who is acting in a professional or official capacity.

5.3 Are the charged assets protected during enforcement?

5.3.1 Can the chargeholder take possession of the assets?

Where enforcement is by a sale pursuant to an agreement, the chargeholder can require, either in the preliminary notice (see 5.2.1) or thereafter, that the chargor hands over the charged assets and provides everything that is necessary to sell them.

In the case of a joint sale, the chargor will hand over the asset only if provided in the agreement for joint sale. If not, the chargor must give the chargeholder the necessary information about the charged asset for the purpose of the sale and should allow potential buyers to inspect the charged property.

If more than one chargeholder gives notice to enforce over the same assets, the chargor is obliged to hand the charged property over to the chargeholder whose demand notice was received first (unless otherwise instructed by all chargeholders concerned). On charges involving several chargeholders, see 5.5.2.

However, if the chargor refuses to cooperate, the chargeholder would have to go to court to enforce the right to possession. The court will order enforcement on the basis of either a notarial deed that evidences the chargeholder's claim, or a final court decision establishing the chargeholder's right to enforce.

5.3.2 What happens with claims and rights?

Where the charged assets are rights and claims, the chargor must hand to the chargeholder the originals of the documents that constitute or evidence the right/claim. Alternately, these documents are necessary for exercising the right or enforcing the claim and inform the obligor

of the charge (if not already done). Should the chargeholder inform the obligor directly of the existence of the charge over the claim, the obligor can request the chargeholder to certify the existence of the charge by presenting the charge instrument or a notarised document evidencing the charge.

5.3.3 How can the chargeholder prevent loss, damage or deterioration of the charged assets during this period?

The chargor remains under the same duties to maintain the charged assets as before enforcement (see 4.1.2). In principle, they should not sell or hand the charged asset over to anyone other than the chargeholder or the person appointed to sell the charged asset.

Practice note: As the law is not completely clear on this point, it is preferable for the chargeholder to include in the notice to the chargor a prohibition on any disposal of the charged assets.

The best means of obtaining additional protection is to take possession (see 5.3.1). A chargeholder might also seek protection of the charged assets by a court injunction, if the circumstances merit it.

5.4 What are the methods of realisation of the charged property?

5.4.1 Sale by the chargeholder pursuant to an agreement - how does it work?

If the charged asset has an officially registered market price or the chargeholder is in the business of providing loans against security, the parties can agree (see 5.2.4) that the chargeholder may himself sell the charged asset.

At least 15 days prior to the sale, the chargeholder must inform the chargor in writing on the chosen method, place and time of the sale (which can be the same document as the preliminary notice, see 5.2.1). Thereafter, he must make an inventory of the charged assets in his possession and maintain a sale journal setting out the steps taken in relation to the sale. The journal is to be kept open to inspection by the chargor.

The chargeholder must act with the diligence that is generally expected in the given situation and must sell the property for a fair price available in the then prevailing market conditions. Where the sale is not in the ordinary course of trade, potentially interested buyers must be informed of the sale and have the opportunity to make competitive offers. The chargor must put the chargeholder in a position to be able to sell the charged asset in accordance with the agreement and the law and must refrain from any conduct that prevents the chargeholder from exercising his rights.

If the charged property is not sold within the time limit or under the other conditions of the agreement with the chargor, the sale is deemed to have failed. The parties may agree on a new deadline, failing which the agreement for sale lapses. The chargeholder must return the charged asset to the chargor unless he promptly initiates a court enforcement procedure.

5.4.2 Sale by another person pursuant to an agreement: How does it work?

The parties can agree (see 5.2.4) that the chargeholder may instruct another person to sell the charged asset. That person must be professionally or officially dealing with providing loans against security and/or organising auctions.

The rules for the conduct of the sale are the same as for the sale by the chargeholder himself (see 5.4.1). If the sale notice is sent to the chargor by the third party appointed for the sale, a copy of the deed on his appointment has to be attached to the notice.

5.4.3 Joint sale pursuant to an agreement: How does it work?

The parties can agree (see 5.2.4) that they may jointly sell the charged asset. In this case, the chargeholder may not take any measure without the consent of the chargor. The rules for the conduct of the sale are the same as for the sale by the chargeholder himself (see 5.4.1) unless the parties otherwise agree. The chargor must cooperate with the chargeholder to achieve a successful sale.

5.4.4 Court enforcement: How does it work?

When parties have not entered into an agreement for sale of the charged assets on enforcement, realisation is led by a court. If the charge agreement is a notarised document (see 2.1.1) containing certain data prescribed by law and the secured debt is recorded in a notarised document, the court will order the enforcement procedure at the request of the chargeholder without hearing the chargor. Otherwise, a court decision ordering the debtor to pay the claim is necessary before the enforcement procedure itself can start.

Sale at public auction is the general mode of realisation on judicial enforcement. The auction is led by a public executor (bailiff) who has power to seize the charged assets and then organise a public sale at auction.

Practice note: The chargeholder can opt for realisation through court procedure regardless of any agreement for other means of sale. However, it may be possible to exclude this right in the charge agreement.

5.4.5 Can the chargeholder acquire the assets himself?

An agreement allowing the chargeholder to acquire the charged assets on enforcement is null and void if made prior to the triggering of the right of enforcement. This is with the exception of “*óvadék*” (security deposit agreement - see 3.3.3), where it is normal practice that the chargeholder enforces his claim by directly acquiring ownership of the charged securities. After the triggering of the right of enforcement, the chargor can agree on a sale to the chargeholder.

5.4.6 How does realisation take place over claims for money (receivables, bank accounts, etc)?

In principle, the method of realisation for claims of the chargor against a sub-debtor is the same as for any other asset. In addition, the claims can be sold pursuant to an agreement or

through court procedure. In practice, this may often be unsatisfactory, particularly where the claims are close to maturity. Alternatively, the chargeholder may wait for the claims to be paid by the sub-debtor. If the sub-debtor has been notified of the charge, he is obliged from the time of commencement of enforcement to pay solely to the chargeholder (unless otherwise provided). In that case, the chargeholder is entitled to satisfy his claim out of the money so received.

Enforcement of a charge over a bank account (see 4.1.7) is made by the chargeholder delivering an instruction (often in the form of a "prompt collection order") to the bank holding the account. The bank will then debit the account by the amount of the enforced claim and transfer the amount to the chargeholder.

5.5 What else is relevant to enforcement?

5.5.1 What happens if the chargor is insolvent?

From the commencement of the liquidation, the chargeholder ceases to have the right to enforce. The charged assets are sold as part of the liquidation proceedings but the chargeholder has a prior right to the proceeds of the sale (see 4.4.7). Moreover, any enforcement proceedings underway when a bankruptcy declaration is made would automatically be discontinued. (See also 2.3 on invalidity of the charge in insolvency).

5.5.2 Where there are several chargeholders, what are their respective rights?

Where there is more than one charge over the same charged asset, the position depends on whether realisation is pursuant to an agreement or through the court.

1) Realisation pursuant to an agreement

The chargeholder must give notice of the sale, and of taking possession (where applicable), to all other chargeholders authorised to sell, informing them that they may join the sale within a specified period (no less than eight days) after receiving the notice. Once another chargeholder has informed the chargeholder conducting the sale of his intention to join, they can take common decisions as to how the sale is to be conducted. In addition, they can appoint a new chargeholder for keeping possession of and selling the charged property, and can amend the place, the time, the method and other conditions of the sale. They are jointly and severally bound to inform the chargor of all procedural steps.

Upon the sale of the assets, the claims of all chargeholders who joined in the sale will be paid in accordance with the priority and to the extent of these claims. However, the assets will be sold subject to the charge of any other chargeholders who did not join in the sale.

Practice note: Where there is more than one chargeholder, it is in practice necessary to have an agreement between all of them as to the sale. Failing which, it may be more appropriate to initiate court enforcement procedure. The enforcing chargeholder should carefully appraise the rights of other chargeholders before commencing enforcement.

2) Realisation through the court

Following seizure of the charged assets, the bailiff must give notice of the seizure to everyone presumed to have a charge over the assets, advising them of their right to apply to the court

for a permission to join in the enforcement procedure. Chargeholders have eight working days to submit a request to the relevant court. The court will then only consider whether the chargeholder's claim is enforceable (irrespective of whether it is due or not) and undisputed by the chargor (which is usually deemed to be the case if the charge agreement is incorporated in a notarised deed). If these conditions are fulfilled, the chargeholder will join in the enforcement procedure and have the same rights and liabilities as the chargeholder who started enforcement, irrespective of the priority of their claims. However, the court will distribute the sales proceeds in accordance with the priority of creditors' claims.

5.5.3 Will the purchaser on enforcement be protected?

Where realisation is pursuant to an agreement, the law provides that the person authorised to sell the charged asset has the right to transfer ownership on behalf, and in the name of, the chargor. This would seem to protect a purchaser acting in good faith from any challenge by the chargor. But he will not be protected from third party claims (e.g. in cases where the chargor is not the owner of the collateral) unless the sale was conducted by a professional auctioneer or dealer.

Where realisation is through the court the purchaser obtains good title.

6. THE SPECIFIC CASE OF ENTERPRISE CHARGE

6.1 What is an enterprise charge?

It is possible to grant security over an "enterprise", that is the entirety of the assets of a business or a part of a business that can operate as a separate economic unit. Creating a charge over an enterprise does not require all the assets constituting the enterprise or the unit to be separately defined. The assets of the enterprise, including those acquired by the chargor during the life of the charge will automatically be included in the security. Conversely, the charge ceases over assets that leave the enterprise so that business activity can continue normally. An enterprise charge is a charge over a 'living' body, with the potential and the risk this represents. On enforcement it gives the chargeholder the right, in principle, to realise the enterprise as a going concern or to realise the assets of the enterprise separately.

Practice note: The charge agreement must clearly indicate that the charge is over an enterprise and define the business or the part of the business that is subject to the charge.

An enterprise charge is subject to the same rules as a registered charge and, in addition, certain special rules which are described in this section.

6.2 How is an enterprise charge created and publicised?

Enterprise charges are created in the same way as other registered charges and are registered at the Charges Register. Registration is not required in the Land Registry or other specific registries to make the charge over these assets valid (but as to priority, see 6.4).

6.3 How can an enterprise charge be transformed into a charge over the assets of the enterprise?

Upon enforcement, or if the value of the enterprise decreases to the extent that it jeopardises realisation on enforcement, the chargeholder may transform the enterprise charge into a charge over the individual assets of the enterprise (as opposed to a charge over the enterprise as a whole). Transformation is achieved by the chargeholder by:

- notifying the chargor
- registering the transformation in the Charges Register
- registering in the relevant specific registries the charges over the assets of the enterprise that are created by the transformation.

The chargor also notifies the chargeholder of decreased value of the enterprise, where relevant.

Practice note: The parties may agree in advance what constitutes decreased value and, more generally, may agree on the ways in which the chargeholder will monitor the enterprise.

Upon transformation, the chargeholder holds a registered charge over the tangible movable and intangible assets of the enterprise and is thus protected against subsequent acquirers, subject to the normal exceptions (see 4.1.11).

6.4 What is the priority of the enterprise charge?

In principle, the enterprise charge (and the charge created by the transformation of an enterprise charge, see 6.3) gives the chargeholder priority ahead of other subsequent charges. This is with effect from the date of registration of the enterprise charge in the Charges Registry. This priority ranking does not apply *vis-à-vis* the following charges:

- charges over assets which are registered (even subsequently) in other specific registries. In these cases, the parties often create, in addition to the enterprise charge, a separate registered charge over the most valuable registered assets (e.g. real estate, ships) included in the enterprise. Priority over these assets will then depend on the time of registration of the separate charge into these specific registries.
- charges over rights or receivables created in good faith in the context of trade relationships between the chargor and the chargeholder.

If any of the charged assets was acquired by the chargor already subject to a charge, the charge created by the previous owner will have priority over the enterprise charge (see 4.4.5).

6.5 Enforcement

Enforcement of an enterprise charge can take place either by maintaining the unity of the enterprise and selling it as a whole (a going concern), or by the “transformation” of the enterprise charge into a charge over the assets that are included in the enterprise at the time of enforcement, and realising those assets in the same way as any other charge (see 5.4). There are currently no special rules regulating sale of an enterprise as a going concern, but a new law is being proposed to cover this. Until this law becomes effective, this route of enforcement does not seem feasible.

7. THE INDEPENDENT CHARGE

While ordinary charges cannot exist without an underlying claim that is explicitly designated in the charge instrument, an independent charge secures an abstract claim, without being linked to any separate claim between the chargor and the chargeholder. The holder of an independent charge has no personal claim against the chargor, merely an abstract right against the charged asset. He cannot, therefore, enforce the claim from any other asset of the chargor. An independent charge, however, is in many ways a somewhat stronger security than an ordinary charge. This is because it does not depend on any underlying claim and also because it can be transferred by itself. It is not affected by any defect in the claim it is intended to secure. In commercial practice, an independent charge is created with the intention of securing a loan or other underlying transaction, although it is not formally linked to the loan or other transaction in law. To enter into such an arrangement, an element of trust has to be present between the parties. The independent charge may be either registered or possessory.

7.1. Creation of the independent charge

For the creation of the independent charge, the rules relating to registered charges and possessory charges apply respectively. The charge agreement shall specify the amount up to which the chargeholder is entitled to seek satisfaction from the charged asset. The agreement usually also specifies a termination period, but does not specify any underlying claim that it is intended in practice to secure. Ordinary charges may be converted into an independent charge (and vice versa) without changing the priority if so agreed by the parties.

7.2. Enforcement of the independent charge

Since the charge is independent, enforcement does not depend in principle on whether the separate claim which the independent charge is intended to secure exists or not, or is due or not. As a consequence, there is no need on enforcement to produce any evidence concerning the existence or validity of any separate claim. The independent charge itself entitles the chargeholder to enforce against the charged assets up to the amount for which it was granted.

The chargor can raise objections on the basis of the underlying transaction *vis-à-vis* the original chargeholder or a subsequent chargeholder who is aware of a deficiency in the underlying transaction. To this extent, they may not rely on the independence of the charge. It is only subsequent transferees, without knowledge of the underlying transaction, who can benefit fully from the independent nature of the charge. To commence enforcement, it is enough to simply terminate the independent charge and give six months' notice of the enforcement (unless the parties have agreed on a shorter or longer notice period or have defined a fixed termination date).

The chargeholder may seek satisfaction only from the charged asset encumbered by the independent charge.

7.3. Transfer of the independent charge

The main benefit of an independent charge is that it is transferable. In case the charge is transferred, the chargor may only raise objections against the new chargeholder based on the separate claim if the new chargeholder acquired the independent charge without consideration, or if he was aware of the deficiency of the separate claim.