

Authorisation guidelines

(Capital market)

April 2010

**Detailed rules of the authorisation procedures
conducted pursuant to Act CXXXVIII of 2007 on
Investment Firms and Commodity Dealers, and the
Regulations governing their Activities (Investment
Services Act)**

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Authorisation guidelines for the authorisation procedures conducted pursuant to Act CXXXVIII of 2007 on Investment Firms and Commodity Dealers, and the Regulations governing their Activities

By issuing these Guidelines, the Hungarian Financial Supervisory Authority (HFSA) intends to provide assistance to the submission of applications for authorisation procedures, explaining the general conditions of the most frequent types of authorisations. However, the information is not necessarily exhaustive; in individual cases procedures different from those laid down in the Guidelines may be followed, naturally in compliance with the effective legal regulations.

Authorisation of the Activities of Investment Enterprises

General Rules

Pursuant to Article 7 Paragraph (1) of the Investment Services Act, unless otherwise provided for in this Act, only investment enterprises and credit institutions may engage in activities to provide investment services. As a consequence of Article 3 Paragraph (2) of the Investment Services Act, as a main rule, credit institutions engaged in activities to provide investment services or supplementary investment services are governed by the provisions specified for investment enterprises.

Pursuant to Article 7 Paragraph (3), investment enterprises with their registered address (headquarters) located in a third country may conduct their activities in Hungary through a branch office.

Pursuant to Article 7 Paragraph (4) an investment enterprise with its registered address located in another state of the EEA may perform cross-border activities in the territory of the Republic of Hungary.

We hereby draw your attention that in absence of a relevant express provision in the Investment Services Act, the establishment of an investment enterprise does not require a license of foundation, and a license is only required for the activities to be conducted by it, and thus the incorporation procedure in relation to the founding of the firm may be completed even before the operating license is issued, provided of course that the investment enterprise may not commence the activity subject to authorisation by the authority until the operating license has been issued.

Activities Permitted for Investment Enterprises

Article 5 Paragraph (1) lists the investment service activities that may be performed in the framework of regular business activities with regard to the financial instruments listed under Article 6. These are as follows:

- a)* Acceptance and transmission of orders;
- b)* Execution of orders for the benefit of customers;
- c)* Trading on own account;
- d)* Portfolio management;
- e)* Investment advice;
- f)* Placement of a financial instrument (security or other financial instrument) with a commitment to purchase the instrument (underwriting guarantee);
- g)* Placing of a financial instrument without a commitment to purchase the instrument (financial instrument); and
- h)* Operation of a Multilateral Trading Facility.

Article 5 Paragraph (2) designates the following supplementary services:

- a)* Safe custody and record-keeping of the financial instrument and management of the related customer account;
- b)* Custodian services and management of the related securities account, record-keeping of printed securities and management of the customer account;
- c)* Investment lending;
- d)* Consulting and services related to capital structure, business strategy and issues related thereto, and related to mergers and acquisitions;
- e)* Trading on own accounting currency and foreign exchange, related to activities to provide investment services;
- f)* Investment analysis and financial analysis;
- g)* Services related to underwriting guarantees;
- h)* An activity to provide investment services or supplementary services in relation to underlying instruments of derivative transactions listed under Article 6 Sections e)-g), j) and k).

It is an important rule, pursuant to Article 8 Paragraph (4), that a license to provide supplementary services may not be obtained on its own without a license to engage in activities to provide investment services, except if the applicant is a clearing house or a central depository as defined under the Capital Market Act.

The range of financial instruments is presented under Article 6:

- a) Transferable securities;
- b) Money market instruments;
- c) Securities issued by collective investment schemes;
- d) Options, futures, swaps, forward interest-rate agreements, and any other derivatives contracts, instruments, financial indices or measures related to securities, foreign exchange, interest rates or yields that may be settled with physical delivery or in cash;
- e) Options, futures, swaps, forward interest-rate agreements, and any other derivatives contracts or instruments related to commodities, that shall be settled in cash, or may be settled in cash at the option of one or more of the parties to the transaction, otherwise than by reason of the date of maturity or other termination event;
- f) Options, futures, swaps, forward interest-rate agreements, and any other derivatives contracts or instruments related to commodities, to be settled with physical delivery, provided that the instrument is traded on a regulated market or on a Multilateral Trading Facility;
- g) Other options, listed and over the counter futures, swaps and any other derivatives contracts related to commodities and not included under Section f) above, that can be settled with physical delivery and serve a non trading purpose, if cleared using a recognised clearing house or if subject to obligations to regularly supply additional payments;
- h) Derivatives contracts with the purpose to transfer credit risk;
- i) Financial contracts concerning margins;
- j) Options, futures, swaps, forward interest rate agreements or any other derivatives contracts or instruments related to a climatic or meteorological variable, freight, emission of an air pollutant or a greenhouse gas, inflation rate or some other official economic statistic, that shall be settled in cash or may be settled in cash at the option of one or more of the parties to the transaction, otherwise than by reason of a default;
- k) Any other derivatives contract or instrument related to an instrument, right, obligation, index or measure not listed under Sections a)-j), that has the characteristics of one of the other derivative instruments, including the characteristic that it is traded on some regulated market or on a Multilateral Trading Facility, is cleared and settled using a recognised clearing house, or is subject to an obligation to regularly supply additional payments, and if it is a derivatives contract as specified under Article 39 of Commission Regulation (EC) No. 1287/2006.

Pursuant to Article 8 Paragraph (5), in addition to being engaged in providing investment services and supplementary services, an investment enterprise may engage exclusively in the following:

- a) The activity specified under Article 9 Paragraph (1), i.e., activities permitted for service providers active on the commodity exchange;
- b) Management of share registers;
- c) Activities as a shareholder nominee;
- d) Agency activity as specified under the Act CXII of 1996 on Credit Institutions and Financial Enterprises (ACIFE), with an operating license, issued pursuant to the ACIFE, to intermediate financial services;
- e) Intermediation of insurance as specified under the Act LX of 2003 on Insurance Institutions and the Insurance Business;
- f) Securities lending;
- g) Marketing of data and information about financial instruments.

We note that the above legislature does not apply to credit institutions.

Organisational rules and subscribed capital

Pursuant to Article 16 Paragraph (1) an investment enterprise may operate in the form of a company limited by shares or in the form of a branch office.

Pursuant to Article 16 Paragraph (2), investment enterprises operating in the form of a business organisation are governed by the provisions of the Act IV of 2006 on Companies, while the branch offices of foreign enterprises are governed by the provisions of the Act CXXXII of 1997 on Hungarian Branch and Representative Offices of Foreign Enterprises, with the differences contained in this Act.

Article 13 Paragraph (1) stipulates that in order to commence activities an investment enterprise shall have an initial capital in the amount of at least seven hundred thirty thousand Euros, with the exceptions as set forth under Paragraphs (2)-(3).

Pursuant to Article 13 Paragraph (2), if an investment enterprise obtains license to engage exclusively in the provision of investment services to accept and forward orders, to execute orders for customers, and to provide portfolio management services (either jointly or individually), and

- a) If it is entitled to manage the financial instruments and the monetary assets of its customers, then it shall have an initial capital in the amount of at least one hundred twenty five thousand Euros; and
- b) If it is not entitled to manage the financial instruments and the monetary assets of its customers, then it shall have an initial capital in the amount of at least fifty thousand Euros.

While pursuant to Article 13 Paragraph (3) if an investment enterprise obtains a license to provide investment services to accept and forward orders or to provide investment consulting services, and if it is not entitled to manage the financial instruments and monetary assets of its customers, than it shall have an initial capital in the amount of at least fifty thousand Euros or it shall have professional liability insurance covering the territory of the EEA states providing cover of at least one million Euros for each claim event and at least one million five hundred thousand Euros in total per annum.

The rules for the payment of the subscribed capital of an investment enterprise are contained under Article 15 Paragraphs (1)-(6).

(1) With consideration to the contents of Paragraph (2) the subscribed capital of an investment enterprise may only be supplied in the form of a monetary contribution.

(2) It will be considered as equivalent to monetary contribution as specified under Paragraph (1), if the subscribed capital is increased using the assets of the investment enterprise in addition to its subscribed capital, and also if the amount of the subscribed capital is determined in the course of a fusion, acquisition or a merger.

(3) The subscribed capital of an investment enterprise may be payed exclusively in a credit institution that does not participate in its founding and in which no founder holds an ownership stake, and which does not hold an ownership stake in a founder.

(4) In the case of investment enterprises operating in the form of a branch office, with the exception listed under Paragraph (5), the subscribed capital is to mean the endowment capital.

(5) The endowment capital requirement shall not be applied to a branch office of an investment enterprise that has its registered address in another EEA state.

It is to be noted that the endowment capital requirement is to be applied for branch offices of credit institution governed by the ACIFE.

(6) The amounts specified under Article 13 in Euros are to be converted into Hungarian Forints using the official exchange rate published by the Magyar Nemzeti Bank (National Bank of Hungary) that is

- a) Valid for the last day of the month preceding the founding, for the amount of the initial capital; and
- b) Valid for the last days of the calendar year preceding the year in question, for the amount of the liability insurance.

Naturally, credit institutions also engaged in activities to provide investment services are governed by the organisational rules and by the special rules set forth in the ACIFE with regard to their subscribed capital.

General Requirements related to Investment Enterprises

Pursuant to Article 17 Paragraph (1), investment enterprises shall set up their individual organisational units within their organisations and the rules governing their operation and conduct to ensure that the organisational structure thus created, and its operation – in accordance with the size of the investment enterprise and the nature and the complexity of its activities –

- a) Enable the investment enterprise to perform its activities and to meet its duties independently, including also a clear and consistent separation of the necessary competencies;
- b) Ensure that the managers of the individual organisational units are not subordinated, superordinated or reporting to each other, in order to thereby reduce the possibilities for the fusion of personal interests that could lead to abuses;
- c) Enable access to information only to those entitled, in order to thereby reduce the possibilities for the abuse of the inside information that is generated in the administration of the business;
- d) Are transparent;
- e) Reinforce process-integrated control and enable objective monitoring in its course.

Pursuant to Article 17 Paragraph (2), an investment enterprise subject to consolidated supervision under the Capital Market Act, shall also comply with the provisions of this Article and Article 100 in consolidation with the credit institution or investment enterprise under its controlling influence.

Pursuant to Article 18 Paragraph (2) the accounting, record-keeping and information technology systems of the investment enterprise shall be suitable a) for the determination of its prevailing financial condition at any point in time, b) for the determination of the holdings and the amounts of the financial instruments and monetary assets transferred by the customer and due to the customer at any point in time, and c) for compliance with the data disclosure requirements as specified in the legal regulations.

Documents to be submitted as attachments to an application for an operating license

Pursuant to Article 28 Paragraphs (1)-(5) an investment enterprise – and a credit institution that intends to engage in activities to provide investment services – shall attach the following documents to its application for the issuance of an operating license:

- Its articles of association or the amendment of its articles of association;
- A copy of its share register;

- Proof of payment of the initial capital in the amount as specified and a declaration together with the corresponding documentary proof, stating that the amount required for the payment of the initial capital originates from the personal lawful income of the person participating in the founding, or the contract for the liability insurance;
- Designation of the activity that the applicant intends to pursue and the organisational and operational rules that should also contain the applicant's systems for decision making and governance;
- A declaration stating that the investment enterprise shall be managed from a central office to be established in the territory of the Republic of Hungary;
- In the case of several sites, a description of the material and technical conditions at the site where it intends to conduct its activities;
- Names, registered offices and scopes of activities of the business associations in which the applicant holds shares, indicating also the percentage of ownership;
- A description of its accounting policies and accounting system;
- Its draft rules for business records;
- Its draft rules for its audit arrangement;
- Its business plan (to include a textual analysis of the results that the firm intends to achieve from the given activity on the market in the coming three years, indicating its planned revenues and expenses, all of which should be supported with numeric data);
- A detailed description of compliance with the material and technical conditions as specified in this Act and in separate statutory regulations;
- Copies of documents that provide proof of its compliance with the organisational conditions as specified in this Act;
- Copies of documents that provide proof of its compliance with the personal conditions as specified in this Act and in a separate statutory regulation (the separate statutory regulation has not yet been completed);
- The draft general terms and conditions of contract for the activity to be pursued, the draft business rules, the draft rules for the prevention of money laundering, the draft rules for the management of cash and valuables, the draft implementation policies and the draft policies concerning incompatibility;
- Proof of payment of the administrative service fee as specified in a separate statutory regulation;
- A certified statement by the auditor confirming that the information technology system of the investment enterprise is suitable for compliance with the requirements specified under Article 18 Paragraph (2);
- The draft rules for the monitoring, measurement, verification and management of risks;

- The draft rules for the management of the trading book;
- For investment enterprises subject to supervision on a consolidated basis or subject to supplementary supervision, a presentation of the system for the transfer of information related to supervision on a consolidated basis or to supplementary supervision and declarations from the persons closely related to the investment enterprise stating that they will disclose all data, facts and information that may be necessary for supervision on a consolidated basis or for supplementary supervision;
- Declarations from persons closely related to the investment enterprise, stating that they consent to their personal details that have been provided to the investment enterprise to be managed and forwarded for the purposes of compliance with supervision on a consolidated basis or supplementary supervision as specified in this Act;
- Identification details for persons closely related to the parent company of an investment enterprise subject to supervision on a consolidated basis or subject to supplementary supervision;
- A confirmation from the Investor Protection Fund of the submission of the application to join the Fund and of the payment of the accession fee, if a license is requested for an insured activity and if a statutory regulation stipulates that the investment enterprise shall join the Fund.

Pursuant to Article 28 Paragraph (2), for an application for the authorisation of custodian activities the applicant shall attach, in addition to the documents listed under Paragraph (1), its draft rules for security, custodian services and safe custody.

Pursuant to Article 28 Paragraph (3), for an application for the authorisation of investment lending activities, the applicant shall attach, in addition to the documents listed under Paragraph (1), proof that it has joined the Central Credit Information System.

With regard to foreign applicants further rules are stipulated under Article 28 Paragraphs (4)-(5). Thus, in an application for the authorisation of investment enterprise activities, in addition to the documents listed under Paragraphs (1)-(3), a foreign applicant a) shall also indicate the locations where it pursues the activities and b) shall also designate the decision making powers of the persons in executive positions and of the body, without the approval of which the individual decisions shall be invalid;

Furthermore, a foreign applicant shall attach to its application for the authorisation of activities to provide investment services, a certified statement from the supervisory authority having jurisdiction over its registered address, stating that there are no grounds for the exclusion of a person in an executive position, who is not a Hungarian citizen, from filling the position or from discharging the duties associated therewith.

When submitting the application, the owners of an investment enterprise shall consider the rules of the Investment Services Act governing the acquisition of qualified influence, and in particular the provisions of Article 37 Paragraph (3) pursuant to which: "For a person to hold a qualified influence in an investment enterprise,

- a) His/her influence on the investment enterprise may not threaten the independent, reliable and prudent governance of the investment enterprise by its owners;
- b) His/her business activities and the nature of his/her contacts or the structure of his/her indirect or direct ownership interests in other enterprises may not hinder the supervisory activities;
- c) He/she should be of good business reputation."

Since the acquisition of qualified influence in an investment enterprise is subject to prior supervisory authorisation, an application shall also include as attachments the documents listed in the Authorisation Guidelines under the section titled "Authorisation of the acquisition of qualified influence in an investment enterprise."

When **expanding the scope of activities** of an investment enterprise, the application for the authorisation shall be submitted together with the documents specified under Article 28 Paragraph (1) of the Investment Services Act that have not yet been submitted earlier.

Special Statutory Conditions for the Authorisation of a Multilateral Trading Facility

Pursuant to Article 142 Paragraph (1) of the Investment Services Act, an investment enterprise or a regulated market (hereinafter jointly referred to as a market operator) are entitled to engage in activities to provide investment services and to operate a Multilateral Trading Facility as designated under Article 5 Paragraph (1) Section h).

Pursuant to Article 144 Paragraph (1), (1) A market operator has a system, procedure and organisational solution for trading and record-keeping that ensure a) discrimination-free access to the trading system; b) a fair, reliable and transparent system for making offers and efficient pricing; c) compliance with the rules specified under this Act for trading and participation in trading; and d) the secure and efficient clearing and settlement of the transactions completed.

Pursuant to Article 147, in addition to the documents included under Article 28, the applicant shall attach the following documents to an application for the authorisation of this activity:

- a) The draft bye-law(s) as specified under Article 150 Paragraph (1): The market operator prepares bye-law on the rules for participation in trading, which shall contain at the least the conditions for discrimination-free access to the trading system, the rights and the obligations of the members with the right to trade in the system, the rules for trading and for closing deals, including rules and procedures for the suspension of trading and the method of pricing;
- b) The conditions, upon compliance with which, a specific financial instrument may be traded on the Multilateral Trading Facility;
- c) Description of the range of publicly accessible information related to the Multilateral Trading Facility and to trading, and of the means of its publication;

- d)* The procedures for verifying the conditions that members of the Multilateral Trading Facility shall meet;
- e)* Description of the procedure to prevent and identify insider trading and market manipulation;
- f)* Presentation of the procedure to eliminate conflicts of interest that may emerge in the course of the operation of the Multilateral Trading Facility and the execution of the orders of the customers of the investment enterprise that operates the Multilateral Trading Facility;
- g)* The name of the manager of operations;
- h)* Designation and detailed description of the tangible and technical assets necessary to transact trading and that are available or are to be purchased;
- i)* The certificates that guarantee the security and reliability of the system, the continuity of business, and the confidential and comprehensive management of the data;
- j)* The disaster recovery plan prepared for system breakdown events;
- k)* The method for the clearing and settlement of the transactions completed;
- l)* A copy of the agreement signed in order to ensure the clearing and settlement of the transactions completed on the Multilateral Trading Facility;
- m)* The contract for the liability insurance as specified under Article 144 Paragraph (4), with liability insurance cover in the amount of at least one hundred million Hungarian Forints for each claim event and at least one hundred fifty million Hungarian Forints in total per annum for damages in connection with the operation of the trading facility;
- n)* The draft contract to be entered into between the operator of the Multilateral Trading Facility and its members; and
- o)* The procedures for the contents of the information to be provided to the members of the Multilateral Trading Facility and for the method by which the information is to be forwarded.

Personal conditions

For investment enterprises the Investment Services Act specifies persons in an executive position (Article 4 Paragraph (2) Section 70), the person performing the executive management of an investment enterprise operating in the form of a company limited by shares (Article 22 Paragraph (1)), the most senior manager in charge of the activities to provide investment services (Article 22 Paragraph (3)), the head of internal audit (Article 19 Paragraph (2)), the manager in charge of compliance with statutory regulations (Article 21) and the auditor (Article 97).

In the case of a credit institution the applicant shall have a person in charge of its activities to provide investment services (Article 22 Paragraph (4)).

Person in an executive position:

A person in an executive position with an investment enterprise shall submit a declaration stating that he/she is not subject to any of the grounds for incompatibility as listed under Article 25 Paragraph (1) of the Investment Services Act.

Pursuant to Article 25 Paragraph (1) a person in an executive position with an investment enterprise or a service provider active on the commodity exchange, or a close relative of such a person may not be:

- a) A natural person holding an indirect or direct share in another investment enterprise;
- b) A person in an executive position with an organisation that holds an indirect or direct share in another investment enterprise;
- c) A person in an executive position with or employed by another investment enterprise;
- d) A person in an executive position with or employed by the issuer of a security listed on a regulated market, not including the investment enterprise itself.

The above legislature is not applicable to persons in an executive position with a credit institution or to their close relatives.

Person (at least two) in charge of the executive management of an investment enterprise shall submit the following:

- An original official certificate of criminal history as proof of a clean criminal record;
- Employer's letter(s) of reference as proof of at least three years of relevant professional experience;
- Employer's letter of reference as proof of employment.

(Article 22 Paragraph (1))

A person in charge of the activities of a credit institution to provide investment services shall submit the following:

- An original official certificate of criminal history as proof of a clean criminal record;
- Employer's letter(s) of reference as proof of at least three years of relevant professional experience;
- Negative statement concerning the incompatibility set forth under Article 25 Paragraph (2) of the Investment Services Act (the manager of or the person with decision making powers responsible for the management of an organisational unit created to perform this activity at a credit institution holding a license to engage in activities to provide investment services, may not be employed in an identical position with another

organisational unit of the credit institution or with another credit institution or investment enterprise).

(Article 22 Paragraph (4))

Pursuant to Article 24 Paragraph (1) acceptable professional experience may include time spent with

- a) an investment enterprise;
- b) a financial institution;
- c) a stock exchange or a commodity exchange;
- d) an organisation performing the activities of a clearing house;
- e) an investment fund manager;
- f) a venture capital fund manager;
- g) the Magyar Nemzeti Bank (National Bank of Hungary);
- h) the Government Debt Management Agency Private Company Limited by Shares (ÁKK Zrt) or the Treasury;
- i) an administrative authority;
- j) a service provider active on the commodity exchange;
- k) the Central Clearing House and Depository; or
- l) a Central Contracting Party

as an officer, civil servant or employee in an investment or financial field of specialty.

Article 24 Paragraph (2) states that professional experience obtained abroad shall be eligible for consideration if the professional experience was obtained at an institution equivalent to an institution specified under Paragraph (1) or at an international financial institution.

At least one person in an executive position with an investment enterprise operating in the form of a branch office:

shall submit copies, certified by a notary public, of personal identification documents providing proof of Hungarian citizenship, of resident status, and of permanent residence in Hungary of at least one year (Article 22 Paragraph (2)).

Head of internal audit:

Pursuant to Article 19 Paragraph (2) an investment enterprise shall notify the HFSA of the identity of the person heading its internal audit function.

Manager in charge of compliance with statutory regulations:

Pursuant to Article 21 Paragraph (4) an investment enterprise shall notify the HFSA of the identity of its person in charge of compliance with statutory regulations.

Auditor

The applicant shall submit the contract signed with the auditor and a declaration stating that the auditor appointed by the applicant meets the conditions specified under Article 97 Paragraph (1) of the Investment Services Act;

Pursuant to Article 97 Paragraph (1), to discharge the duties of the auditor, the investment enterprise shall appoint an auditor who or which holds a valid auditor's license and who or which complies with the provisions of the Act IV of 2006 on Companies and

- a) Is certified to audit financial institutions or investment enterprises;
- b) Has no indirect or direct ownership in the investment enterprise;
- c) Has no close relative with an indirect or direct ownership in the investment enterprise;
- d) Has no outstanding debt owed to the investment enterprise;
- e) Has no close relative with outstanding debt owed to the investment enterprise; and
- f) An owner that holds a qualified influence in the investment enterprise has no indirect or direct ownership in the audit firm.

Authorisation of the Operations of Service Providers Active on the Commodity Exchange

Activities Permitted for Service Providers Active on the Commodity Exchange

Pursuant to Article 9 Paragraph (1), as part of its regular business activities a service provider active on the commodity exchange may engage in the following activities for instruments listed under Article 9 Paragraph (2):

- a) Acceptance and forwarding of orders;
- b) Execution of orders for the benefit of the customer;
- c) Trading on own account;
- d) Agency activity as specified under the ACIFE, with an operating license, issued pursuant to the ACIFE, to intermediate financial services;

- e) Intermediation of insurance as specified under the Act LX of 2003 on Insurance Institutions and the Insurance Business;
- f) Intermediation of investment services and supplementary services as a dependent agent;

Services on the commodity exchange may be provided for:

- a) Commodities, including warehouse receipts, their certificate of title parts, negotiable valuable rights and interests and related derivative instruments;
- b) Emission units of greenhouse gases, emission rights of air pollutants, and related options, futures and other derivative transactions; and
- c) Financial instruments specified under Article 6 Sections e)-g) (and listed in the section about the authorisation of the investment enterprise).

Organisational rules and subscribed capital

Services related to the commodity exchange as specified under Article 10 Paragraph (1) may be provided by service providers active on the commodity exchange or by investment enterprises. If an investment enterprise intends to provide services on the commodity exchange, then with regard to the conditions of authorisation the contents of the previous part shall apply.

Pursuant to Article 16 Paragraph (2) a service provider active on the commodity exchange may operate in the form of a company limited by shares, a cooperative, or a branch office.

Pursuant to Article 14 the amount of the subscribed capital of a service provider active on the commodity exchange may not be less than a) twenty million Hungarian Forints for service providers active on the commodity exchange operating in the form of a company limited by shares or a branch office, or b) ten million Hungarian Forints for service providers active on the commodity exchange operating in the form of a limited liability company or a cooperative.

We hereby draw your attention that - in absence of an express relevant provision in the Investment Services Act - the creation of a service provider active on the commodity exchange is not subject to authorisation and only the activities to be conducted by such are subject to authorisation, and thus the incorporation procedure related to the founding of the firm may be completed also prior to the issuing of its operating license, but naturally the company or cooperative may not commence activities that are subject to an official authorisation by an authority until the operating license has been issued.

General requirements for service providers active on the commodity exchange

Pursuant to Article 10 Paragraph (2), services related to the commodity exchange may be provided only in compliance with a) the personal conditions and b) the provisions for technical, information technology and security equipment as specified in this Act and in separate legal regulations, and with c) the provisions for organisational, operational, administrative, accounting, record-keeping and auditing procedures and system as set forth in the approved bye-laws.

Pursuant to Article 18 Paragraph (2) the accounting, record-keeping and information technology systems of a service provider active on the commodity exchange shall be suitable for the determination of its prevailing financial condition at any point in time, for the determination of the holdings and the amounts of the financial instruments and monetary assets transferred by the customer and due to the customer at any point in time, and for compliance with the data disclosure requirements as specified in the legal regulations.

Documents required for the authorisation of the activities

Pursuant to Article 33, for a service provider active on the commodity exchange the following attachments shall be submitted with an application for the issuance of an operating license:

- Its articles of association or the amendment of its articles of association;
- Proof of payment of the initial capital as specified and a declaration together with the corresponding documentary proof, stating that the amount required for the payment of the initial capital originates from the personal lawful income of the person participating in the founding;
- Designation of the activity that the applicant intends to pursue and the organisational and operational rules that should also contain the applicant's systems for decision making and governance;
- The names, registered addresses and the scope of activities of the enterprises in which the service provider active on the commodity exchange holds ownership shares, indicating also the percentage of its ownership share;
- A description of its accounting policies and accounting system;
- The draft rules for its business records;
- The draft rules for its auditing arrangement, to contain a description of the audit organisation and process, as well as the rules for process-integrated, ex-post managerial controls.
- The draft general terms and conditions of contract for the activity to be pursued, the draft business rules, the draft rules for the prevention of money laundering, the draft filing rules, the draft internal audit rules and the draft rules of administration;
- Copies of official documents providing proof of compliance with the personal conditions;

- A detailed description of compliance with the material and technical conditions as specified in this Act and in separate legal regulations;
- Certified statement by the auditor stating that the information technology system of the service provider active on the commodity exchange is suitable for compliance with the requirements specified under Article 18 Paragraph (2);
- Proof of payment of the administrative service fee specified in a separate legal regulation (HUF 50,000 for a procedure to issue a license for activities to provide services on the commodity exchange, pursuant to Regulation No. 12/2002 issued by the Minister of Finance);
- For a service provider active on the commodity exchange that operates in the form of a branch office, a certified statement from the regulatory authority having jurisdiction over its registered address stating, that it holds an operating license to engage in the activity;
- For a person in an executive position with a service provider active on the commodity exchange that operates in the form of a branch office, a presentation of his/her decision making and managerial powers;

With regard to foreign applicants further rules are stipulated under Article 33 Paragraphs (2)-(3). Thus, in an application for authorisation for an activity specified under Article 9 Paragraph (1), in addition to the documents listed under Paragraph (1), a foreign applicant shall also indicate the locations where it pursues the activities and shall also designate the decision making powers of the persons in executive positions and of the body, without the approval of which the individual decisions shall be invalid;

Furthermore, a foreign applicant shall attach to its application for authorisation for an activity specified under Article 9 Paragraph (1), a certified statement from the supervisory authority having jurisdiction over its registered address, stating that there are no grounds for the exclusion of a person in an executive position, who is not a Hungarian citizen, from filling the position or from discharging the duties associated therewith.

Personal conditions

For service providers active on the commodity exchange the Investment Services Act specifies a person in an executive position (Article 4 Paragraph (2) Section 70), the manager of a business unit (Article 23), the head of internal audit (Article 19 Paragraph (2)) and the auditor (Article 97).

Person in an executive position:

A person in an executive position with a service provider active on the commodity exchange shall submit a declaration stating that he/she is not subject to any of the grounds for incompatibility as listed under Article 25 Paragraph (1) of the Investment Services Act.

Business unit manager:

- An original official certificate of criminal history (good-conduct certificate) shall be submitted as proof of a clean criminal record;
- Employer's letter(s) of reference shall be submitted as proof of at least two years of relevant professional experience.

(Article 22 Paragraph (1))

Pursuant to Article 24 Paragraph (1) acceptable professional experience may include time spent as an officer, civil servant or employee in an investment or financial field of specialty with

- an investment enterprise;
- a financial institution;
- a stock exchange or a commodity exchange;
- an organisation performing the activities of a clearing house;
- an investment fund manager;
- a venture capital fund manager;
- the Magyar Nemzeti Bank (National Bank of Hungary);
- the Government Debt Management Agency Private Company Limited by Shares (ÁKK Zrt) or the Treasury;
- an administrative authority;
- a service provider active on the commodity exchange;
- the Central Clearing House and Depository; or
- a Central Contracting Party.

Article 24 Paragraph (2) states that professional experience obtained abroad shall be eligible for consideration if the professional experience was obtained at an institution equivalent to an institution specified under Paragraph (1) or at an international financial institution.

Head of internal audit:

Pursuant to Article 19 Paragraph (2) an investment enterprise shall notify the HFSA of the identity of the person heading its internal audit function.

Auditor

The applicant shall submit the contract signed with the auditor and a declaration stating that the auditor appointed by the applicant meets the conditions specified under Article 97 Paragraph (1) of the Investment Services Act;

Pursuant to Article 97 Paragraph (1), to discharge the duties of the auditor, the service provider active on the commodity exchange shall appoint an auditor who or which holds a valid auditor's license and who or which complies with the provisions of the Act IV of 2006 on Companies and

- Is certified to audit financial institutions or investment enterprises;
- Has no direct or indirect ownership in the service provider active on the commodity exchange;
- Has no close relative with a direct or indirect ownership in the service provider active on the commodity exchange;
- Has no outstanding debt owed to the service provider active on the commodity exchange;
- Has no close relative with outstanding debt owed to the service provider active on the commodity exchange; and
- An owner that holds a qualified influence in the service provider active on the commodity exchange has no indirect or direct ownership in the audit firm.

Authorisation for the Transfer of Positions

General Rules for the Transfer of Positions

Pursuant to Article 140 Paragraph (1) of the Investment Services Act an investment enterprise or a service provider active on the commodity exchange may, with the exceptions as detailed below and upon prior authorisation by the HFSA, transfer its outstanding positions of contractual liabilities to another investment enterprise or to a service provider active on the commodity exchange. Pursuant to Paragraph (4) of the referenced statutory provision, the license issued by the HFSA shall not substitute for the license to be issued by the Hungarian Competition Authority pursuant to a separate legal regulation.

It is an essential exception from the above that an investment enterprise may not transfer its positions of contractual obligations to a service provider active on the commodity exchange (Article 140 Paragraph (2) of the Investment Services Act), and accordingly, an investment enterprise may take over the contractual liability positions of other investment enterprises and of service providers active on the commodity exchange, while a service provider active on the commodity exchange may only take over the contractual liability positions of another service provider active on the commodity exchange (Article 140 Paragraph (3) of the Investment Services Act).

Pursuant to Article 141 Paragraph (1) of the Investment Services Act, transfers of contractual liability positions of investment enterprises and of service providers active on the commodity exchange are governed by the rules of the Civil Code (Act IV of 1959) for the assumption of debt.

Pursuant to Article 141 Paragraph (7) of the Investment Services Act, the rules of the Civil Code on assignment are to be applied for the rights vis-à-vis the customer of the investment enterprise or of the service provider active on the commodity exchange that makes the transfer.

Particular Rules for the Transfer of Positions

Obligation to Inform the Client

Pursuant to Article 141 Paragraph (2) of the Investment Services Act, in the course of the transfer the investment enterprise or service provider active on the commodity exchange that makes the transfer shall inform its clients, prior to the entry into force of the contract providing for the transfer, of the following:

- 1.) The intent to make the transfer;
- 2.) Pursuant to the provisions of Article 141 Paragraphs (3)-(6) of the Investment Services Act, the legal consequences if the client makes a statement or fails to make a statement (or makes an incomplete statement) and the legal consequences of the acceptance by the receiver;

The time available to the client to make a statement, and;

It is also necessary to designate a cut-off date following which, upon acceptance of the person and business rules of the receiving investment enterprise or service provider active on the commodity exchange, the monetary assets and funds owned by or due to the client are transferred into the management of the receiving investment enterprise or service provider active on the commodity exchange, and following which those assets are subject to the provisions of the business rules of the receiving investment enterprise or service provider active on the commodity exchange (Article 141 Paragraph (6) of the Investment Services Act), and in addition to this:

- 3.) The entity making the transfer shall advise its clients as to where, from which point in time, and in what form the business rules of the receiving entity are available for inspection.

Statement Made by the Client

Statement of Rejection by the Client:

If the client rejects the person or the business rules of the investment enterprise or of the service provider active on the commodity exchange that takes over the contractual liability positions, then within his/her statement to be sent in writing to the investment enterprise or service provider active on the commodity exchange that makes the transfer he/she shall:

a) Designate a different investment enterprise or service provider active on the commodity exchange, and;

b) Shall indicate the number of the securities account or safe custody account maintained there, as well as of the account used to transact investment-related cash-flow (Article 141 Paragraph (3) of the Investment Services Act).

Pursuant to Article 141 Paragraph (4) of the Investment Services Act the investment enterprise or service provider active on the commodity exchange that makes the transfer shall allow at least 30 days for the client to make the statement as specified above.

If a client fails to make a statement or makes an incomplete statement:

If the client fails to make a statement within the deadline allowed for making such a statement as specified above, or if he/she sends a statement to the investment enterprise or service provider active on the commodity exchange, which is incomplete, missing some mandatory content elements that are required for a statement of rejection, then the client shall be deemed to have accepted the person and the business rules of the receiving investment enterprise or service provider active on the commodity exchange (Article 141 Paragraph (5) Sections a)-b) of the Investment Services Act).

Acceptance of the person and of the business rules of the receiving investment enterprise or service provider active on the commodity exchange

Upon acceptance of the person and of the business rules of the receiving investment enterprise or service provider active on the commodity exchange and as of the cut-off date indicated in the information sent to the client as specified above, the monetary assets and funds owned by or due to the client are transferred into the management of the receiving investment enterprise or service provider active on the commodity exchange, and are subsequently governed by the provisions of the business rules of the receiving investment enterprise or service provider active on the commodity exchange.

Burden of Expenses and Fees

Pursuant to Article 141 Paragraph (4) of the Investment Services Act the expenses and fees incurred as a consequence of a transfer of positions may not be deferred to the client.

Attachments to the Application for an Authorisation to Transfer Positions

The following documents are necessary to be submitted as attachments to the application by the entity making the transfer and by the receiving entity for a prior authorisation of a transfer of positions:

- A contract under private law, without deficiencies, about the transfer of the business positions between the involved investment enterprise(s) and/or service provider(s) active on the commodity exchange, the examination of which shall focus in particular on the protection of the interests of the market and of the client, on whether or not adequate information was sent to the clients about the transaction, on the future business intentions of the entity making the transfer and of the receiving entity, on the completeness or the partiality and the entirety and coverage of the business positions to be transferred (the parties should avoid indicating a specific execution date without

alternatives, primarily because the contract is subject to official approval by an authority, which cannot be dated in advance);

- A time schedule related to the contract that reflects the practical course of the hand-over and the take-over of the positions;
- The draft letter of information to be sent to the clients by the entity making the transfer, about its intention to make the transfer.

We hereby draw your attention that following the transfer of positions the entity making the transfer and the receiving entity shall electronically send to the HFSA the mapping of the property and the vouchers certifying the transfers, in order to enable an accurate identification of the transferred positions.

Authorisation for the Acquisition of Qualified Influence in an Investment Enterprise

The concept of qualified influence

Pursuant to Article 4 Paragraph (2) Section 11 of the Investment Services Act, “*qualified influence* is an indirect and direct relationship with an enterprise on the basis of which the person holding the influence

- a)* Holds an ownership stake (share) of at least ten percent in the enterprise or can exercise at least ten percent of its voting rights;
- b)* Can appoint or dismiss at least twenty percent of the members of the decision making, executive or supervisory organs and bodies of the enterprise;
- c)* Can exert decisive influence on the operations of the enterprise on the basis of its articles of association or an agreement.”

General rules for the acquisition of qualified influence (general requirements, constraint of prior authorisation)

Pursuant to Article 37 Paragraph (3) of the Investment Services Act: “In order for a person or entity to be eligible for a qualified influence in an investment enterprise,

- a)* His/her activities or his/her influence on the investment enterprise may not threaten the independent, reliable and circumspect governance of the investment enterprise by its owners;
- b)* His/her business activities and the nature of his/her contacts or the structure of his/her direct and indirect ownership stake in other enterprises may not hinder the supervisory activities;
- c)* He/she shall be of good business reputation.”

Article 37 Paragraph (4) of the Investment Services Act provides additional support for Paragraph (3) Section a) by providing examples and setting forth: “The activities or the influence on the investment enterprise of the applicant are of particular threat to the independent, reliable and circumspect governance of the investment enterprise by its owners, if

a) The execution of its voting rights has been suspended by its competent supervisory authority within five years prior to the submission date of the application;

b) Holds (has held) a qualified influence, or is (was) a person in senior position in an investment enterprise, financial institution or insurer

ba) The insolvency of which could be avoided only with measures taken by the competent supervisory authority, and who was found to be personally responsible for the emergence of this situation in a conclusive resolution by a court or by an authority; or

bb) That had to be liquidated and who was found to be personally responsible for the emergence of this situation in a conclusive resolution by a court or by an authority;

c) Who has gravely or regularly violated the provisions of this Act or some other legal rules governing the management of the investment enterprise, and this was established by a competent supervisory authority, some other authority or court in a conclusive resolution dated not longer than five years ago.”

Article 37 Paragraph (1) of the Investment Services Act states that “the acquisition of a qualified influence in an investment enterprise is subject to prior authorisation by the HFSA.”

Article 37/B Paragraph (1) of the Investment Services Act specifies for existing holders of a qualified influence that they shall also obtain a prior authorisation from the HFSA if they wish to modify their qualified influence to exceed twenty, thirty three or fifty percent.

Particular rules for the acquisition of qualified influence

Establishing the percentage of the qualified influence

Pursuant to Article 37/A Paragraph (1) of the Investment Services Act: “When establishing the percentage of the qualified influence, voting rights are calculated on the basis of all participations that are connected with voting rights pursuant to the provisions of the investment enterprise’s articles of association, independently of any provisions that may restrict the exercise of such voting rights.

(2) When establishing the percentage of the qualified influence, in addition to the share held by the applicant, the voting rights pursuant to paragraphs 3) and 4) below are also to be considered.

(3) When establishing the percentage of the qualified influence consideration shall be made of the following:

a) Voting rights held by an investment fund manager or an undertaking for collective investment in transferable securities, if the investment fund manager or the undertaking for collective investment in transferable securities exercises the voting rights connected to the managed securities on the basis of instructions given directly, indirectly, or in any other way by the applicant or by another enterprise controlled by the applicant;

b) Voting rights held by an investment enterprise or a credit institution, if the investment enterprise or the credit institution exercises the voting rights connected to the managed portfolio on the basis of instructions given directly, indirectly, or in any other way by the applicant or by another enterprise controlled by the applicant;

(4) When establishing the percentage of the qualified influence the following voting rights connected to the share are to be considered as voting rights held by the applicant:

a) Voting rights that can be exercised by the applicant and a third party on the basis of an agreement that enables the parties to the agreement to exercise voting rights in a coordinated way;

b) Voting rights that the applicant may exercise on the basis of an agreement for a temporary transfer of voting rights;

c) Voting rights that the applicant may exercise on the basis of an agreement related to a share placed with the applicant as collateral;

d) Voting rights that the applicant may exercise on the basis of a beneficial interest (usufruct) in the share;

e) Voting rights that can be exercised by a controlled enterprise of the applicant on the basis as specified under a)-d) above;

f) Voting rights that the applicant may exercise as a custodian in its own judgement, in the absence of specific instructions from the depositor;

g) Voting rights that may be exercised by a third party in its own name, to the benefit of the applicant, on the basis of an agreement with the applicant; and

h) Voting rights that the applicant may exercise as a proxy in its own judgement, in the absence of specific instructions from the principal.

The following are to be excluded from the above when establishing the percentage of the qualified influence. Pursuant to Article 27/A Paragraph (5) of the Investment Services Act: “When establishing the percentage of the qualified influence, the voting rights of an enterprise controlled by the applicant need not be considered, if the applicant and its controlled enterprise, when acquiring the share, declare the following:

a) That they will not exercise the voting rights, or that the voting rights will be exercised by a third party independently of the applicant and its controlled enterprise, and that the share will be sold within one year from its acquisition date;

b) That the voting rights may be exercised on the basis of specific instructions issued on paper or electronically by a third party that is independent of the applicant and its controlled enterprise;

c) That the applicant will not take part in making any decisions for the appointment or dismissal of the members of the investment enterprise's decision making, executive or supervisory organs.

A further exception set forth in Paragraph (6) of the referenced legal regulation is as follows: "When establishing the percentage of the qualified influence the voting rights of an investment enterprise or credit institution operating as an enterprise controlled by the applicant need not be considered if the investment enterprise or the credit institution has a license to engage in portfolio management activities, and if it can exercise the voting rights related to its managed portfolio

a) on the basis of instructions given on paper or electronically;

b) independently of the applicant."

Particular conditions for issuing a license – mandatory attachments to an application for an authorisation

Pursuant to Article 37 Paragraph (2) of the Investment Services Act the following are to be attached to an application for the authorisation of an acquisition of qualified influence:

„*a)* The identification details of the applicant;

b) Proof of the lawful origin of the funds necessary for the acquisition of the qualified influence;

c) Documentary proof dated not earlier than thirty days prior to the submission date of the application that the person or entity has no outstanding debt owed to the tax authority, customs authority or social insurance organisation with jurisdiction over its person;

d) Proof, that his/her other ownership interests and activities pose no threat to the operations of the financial institution;

e) For natural persons an official certificate of criminal history dated not earlier than thirty days prior to the submission date of the application, or an equivalent official document from the applicant's personal jurisdiction;

f) A declaration by the applicant that he/she meets the conditions specified in Paragraphs (3) and (4);

g) If the applicant is not a natural person, its articles of association in effect on the submission date of the application and documentary proof dated not earlier than thirty days prior to the submission date of the application that its incorporation (registration) in its home jurisdiction has actually occurred, that it is not subject to a bankruptcy, liquidation or final

settlement procedure, and that the persons filling its senior positions are not subject to any exclusion criteria;

h) A declaration by the applicant that the acquisition of the qualified influence does not threaten the governance of the investment enterprise from a head office located in the Republic of Hungary;

i) If the applicant is not a natural person, a detailed description of the applicant's ownership structure;

j) The declarations specified under Article 28 Paragraph (1) Sections *t)* and *u)*;

k) Consent from natural persons that become closely related to the investment enterprise as a result of the acquisition of the qualified influence, to the management of their personal details for the purposes of supervision on a consolidated basis or for supplementary supervision; and

l) A declaration by the applicant in a private document of full probative value, stating that the applicant consents to the verification, at organisations contacted by the HFSA, of the veracity of the contents of the document attached to its application for the authorisation,"

The following are to be attached with regard to Section *j)* of the referenced legal regulation and pursuant to Article 28 Paragraph (1) Section *t)* of the Investment Services Act: in the case of an investment enterprise subject to supervision on a consolidated basis or subject to supplementary supervision, a presentation of the system for information transfer related to the supervision on a consolidated basis or to the supplementary supervision, and declarations by the persons closely related to the investment enterprise stating that they will make available to the HFSA all data, facts and information that may be necessary for the supervision of the investment enterprise on a consolidated basis or for its supplementary supervision. Pursuant to Article 28 Paragraph (1) Section *u)* of the Investment Services Act, declarations by the persons closely related to the investment enterprise stating that they approve of their personal details, provided to the investment enterprise, to be managed and forwarded for the purposes of performing the supervision of the investment enterprise on a consolidated basis or its supplementary supervision in compliance with this Act.

Pursuant to Article 37/B Paragraphs (1)-(2) of the Investment Services Act, if the applicant wishes to modify his/her qualified influence so that it exceeds twenty, thirty three or fifty percent, then in addition to those listed under Article 37 Paragraph (2) of the Investment Services Act the applicant shall also present in his/her application for the prior authorisation the following:

a) The percentage of his/her qualified influence at the time when the notification is made;

b) As well as the percentage of the qualified influence that he/she wishes to acquire.

It is the practice of the HFSA to require, within the proof of the lawful origin of the funds necessary for the acquisition of the ownership, also the continuous availability of the funds, during the period from their generation to the acquisition of ownership. As proof of the lawful

origin of funds, a balance sheet may be accepted for a business organisation while a natural persons may provide proof of lawful origin by sending a copy of his/her personal income tax return.

If the entity acquiring the ownership is a foreign legal entity, a non legal entity business organisation or a natural person, then of course as certification for no debt being owed to the state tax authority, the customs authority, the office of rates and duties and the social insurance organisation we can only accept official documents from the authorities of the country involved.

In order to certify that the other ownership interests and business activities of the applicant pose no threat to the secure operation of the investment enterprise or to the supervisory activity, the involved natural person or the responsible manager of the legal entity or of the business organisation that is not a legal entity should make a declaration in a documentary form.

In order to certify that the incorporation (registration) of the applicant in its home jurisdiction has actually occurred, and that it is not subject to a liquidation or final settlement procedure, a certificate of incorporation not older than thirty days is to be submitted while in order to certify that the applicant is not subject to a bankruptcy procedure a declaration by the responsible manager of the investment enterprise is to be submitted.

The clean criminal record of a natural person is to be certified with an official certificate of criminal history, attached in the original or in a copy certified by a notary public. A declaration about the absence of other grounds for exclusion is to be made in a documentary form.

Refusal of an application to authorise the acquisition of a qualified influence or the increase of a qualified influence (refusal to grant license)

The HFSA shall refuse authorisation for the acquisition of a qualified influence or for an increase in the percentage of a qualified influence, if the applicant or the holder of the qualified influence does not meet the conditions set forth under Article 37 Paragraphs (1)-(4) of the Investment Services Act, i.e., if the applicant or the holder does not meet the aforesaid general and particular conditions, including also compliance with the general provisions contained under Article 37 Paragraphs (3)-(4) of the Investment Services Act (or the attachment of a corresponding declaration).

Consultation with counterpart supervisory authorities

Article 38/A of the Investment Services Act prescribes the following: “If the applicant

- a) Is an investment enterprise with a license to engage in activities in an EEA member state;
- b) Is a credit institution with a license to engage in activities in an EEA member state;
- c) Is an insurer with a license to engage in activities in an EEA member state;
- d) Is a reinsurer with a license to engage in activities in an EEA member state;

e) Is an undertaking for collective investment in transferable securities with a license to engage in activities in an EEA member state;

f) Is a parent organisation of an enterprise listed under a)-e);

g) Has a controlled enterprise listed under a)-e);

then the HFSA may engage in consultation as per Article 171 with the supervisory authority with competence over the registered address of the investment enterprise, the credit institution, the insurer, the reinsurer and the undertaking for collective investment in transferable securities.

Silence by the authority: consent by the authority

Article 39 Paragraph (1) of the Investment Services Act sets forth that if the HFSA fails to refuse to grant a license within the period specified under Article 38 Paragraph (1) (the deadline for administration: *sixty working days*, for the rules for the calculation of other procedural deadlines see the summary of the common procedural standards for authorisation procedures) for the acquisition of the qualified influence or for an increase in the percentage of the qualified influence, then the license shall be deemed to be granted.

Deadline for the completion of an authorised transaction

In this regard Article 39 Paragraph (2) of the Investment Services Act provides as follows: “If the acquisition of a qualified influence or an increase in the percentage of a qualified influence is authorised, the applicant shall complete the transaction within six months.”

Administrative service fee

Pursuant to Article 3 and Article 14 of Decree No. 12/2002 (of February 20) by the Minister of Finance on the administrative service fees payable for administrative proceedings conducted by the Hungarian Financial Supervisory Authority, an applicant shall pay fees in the amount of twenty thousand Hungarian Forints for an application to authorise the acquisition of a qualified influence – or using the earlier terminology, the acquisition of an influencing stake in an investment enterprise – or the amendment of a qualified influence.

Reporting obligations of an investment enterprise with a change in its ownership structure due to the acquisition or amendment of a qualified influence

An investment enterprise shall report to the HFSA, within two working days of learning about the change, the identification details of the person holding a qualified influence in the investment enterprise, the percentage of his/her share and any changes thereof. (Article 39 Paragraph (4) of the Investment Services Act)

Reporting obligations related to the acquisition or reduction of a qualified influence

A person who has acquired a qualified influence in an investment enterprise, or has amended the percentage of his/her existing influence as per Article 37/B Paragraphs (1) and (3) (has increased or reduced it by stepping across the specified limit levels), shall notify the HFSA in writing within two working days of the acquisition of the qualified influence. (Article 39 Paragraph (5) of the Investment Services Act)

Authorisation Guidelines for the authorisation procedures conducted pursuant to Act CXX of 2001 on the Capital Market

Authorisation of the Activities of Investment Fund Managers

The rules governing investment fund managers are contained in Part eight of Act CXX of 2001 on the capital market.

We draw your attention, that the creation of an investment fund manager does not require a license of foundation – due to the lack of an express provision in the Capital Market Act, and only the activities to be performed by such are subject to authorisation, so the incorporation procedure can be carried out at the court of registration even before the license is issued, but of course the corporation may only commence its activities, which are subject to official authorisation, once the license has been issued.

Investment fund managers may perform the following activities:

Pursuant to Article 229 Sections a)-e) of the Capital Market Act, investment fund managers may perform only the following activities:

- a) Investment fund management;
- b) Securities lending;
- c) Taking and transmission of orders for the investment notes of the investment fund managed by the investment fund manager;
- d) Portfolio management activities;
- e) Investment advisory services.

Pursuant to Article 229 Paragraph (2) investment fund managers are obliged to perform the investment fund management activities as specified under Paragraph (1) Section a).

Rules of Organisation / Subscribed Capital

Pursuant to Article 235 Paragraph (1) investment fund managers may operate in the form of a company limited by shares or as a branch office.

Pursuant to Article 235 Paragraph (3) the subscribed capital of an investment fund manager may not be less than one hundred million Hungarian Forints, with the derogations contained under Paragraph (4) and Article 242/C.

Article 235 Paragraph (4) also states, that if an investment fund manager manages private pension fund assets in an amount reaching or exceeding two billion Hungarian Forints, then its owner's equity may not amount to less than two hundred fifty million Hungarian Forints plus one percent of the managed private pension fund assets in excess of two billion Hungarian Forints. If the owner's equity of an investment fund manager reaches one billion Hungarian Forints, it is no longer obliged to further increase its owner's equity if managed private pension fund assets continue to increase.

General Requirements for Investment Fund Managers

Pursuant to Article 230 Paragraph (7) the procedures, systems and solutions employed by the investment fund manager shall ensure that the securities and other money market instruments, monetary assets, stock exchange products and real estate properties held in the individual funds and portfolios are managed separately from each other and separately from the securities, other money market instruments, monetary assets, stock exchange products and real estate properties owned by the investment fund manager itself, and shall ensure the retrieval of the details (subject, date and time, contracting counterparty) of all completed transactions.

Pursuant to Article 230 Paragraph (8) the accounting, record-keeping and information technology systems of an investment fund manager shall be suitable a) for the determination of its prevailing financial position at any point in time, b) for the determination of the portfolios of the investment instruments, monetary assets, stock-exchange products and real estate properties comprising the individual managed funds and portfolios at any point in time, c) for a continuous verification of compliance with the provisions contained in the legal regulations and in the fund manager's own bye-laws, and d) for compliance with the data disclosure requirements prescribed in the legal regulations.

Documents Required for the Authorisation of the Activities

As a consequence of Article 230 Paragraph (3) the following documents are to be attached to an application for an authorisation to perform investment fund management activities:

- a) Certification of the personal, material and technical conditions as specified in Annex No. 11 and necessary for performing the activities;
- b) The Operational Rules, prepared with the content as specified in Annex No. 12;
- c) The Rules of Procedure, as specified in Annex No. 13.

Personal Conditions

1. The professional employed to be in charge of the activity shall have a clean criminal record, with at least five years of professional experience, and may not be subject to any of the exclusion criteria specified under Article 357.
2. The professional employed to perform portfolio management activities and to trade in investment instruments and stock exchange products shall have a clean criminal record, with at least two years of professional experience, and may not be subject to any of the exclusion criteria specified under Article 357.
3. The professional employed to be in charge of the back office shall have a clean criminal record, with at least two years of professional experience in portfolio management, investment fund management or with a financial institution, and may not be subject to any of the exclusion criteria specified under Article 357.
4. For Sections 1-3 above, professional experience shall include time spent in a legal relationship for work with a European investment fund manager or an investment enterprise for investment fund management functions; with the Magyar Nemzeti Bank (National Bank of Hungary), the HFSA, the ministry, the regulated market, a stock exchange, a clearing house, the Government Debt Management Agency Private Company Limited by Shares (ÁKK Zrt) and the Treasury for functions concerned with credit institution/insurer/pension fund investments and custodian services; and with a real estate trader or a foreign equivalent for real estate fund management functions.

In addition to all of this, the persons designated above shall also declare, that they are not subject to any conflict of interest criteria as specified under Article 242.

Material Conditions

Entities performing investment fund management activities shall possess adequate office space and communication systems (telephone, fax, electronic mail address).

Technical Conditions

An entity active in investment fund management shall possess a) a system for record-keeping that ensures compliance with the requirement for separated management and record-keeping as prescribed in the Capital Market Act, and b) a system for the record-keeping of portfolios that is suitable for presenting the changes in the assets of the managed portfolios on an up-to-date basis in a way that ensures compliance with information disclosure requirements and for meeting the requirements of internal audit and audits performed by the HFSA.

The following are the mandatory content elements of the Operational Rules of an entity active in investment fund management (see Annex No. 12):

- Rules for the prevention and handling of conflicts of interest;

- Rules for the separation of investment fund management activities from the other activities performed by the entity active in investment fund management;
- Rules for the separation of the activities of the front office from those of the back office;
- Rules for the setting of decision making powers within the organisation;
- Rules for the retention of data;
- Confidentiality rules;
- Rules for access by investors to the people performing the investment fund management activity.

The following is a more detailed elaboration of the above points for the preparation of the bye-laws:

1. Rules for the prevention and handling of conflicts of interest

A conflict of interest may emerge for the investment fund manager if the interests of a client or of a fund managed by the investment fund manager are in conflict with its own economic interests. The contents of this part of the rules depend on the other activities in addition to fund management that the fund manager requests to be authorised for. Prevention and handling can be ensured using an information system. The fund manager can use it to track its contractual relationships with its counterparty and their contents.

2. Rules for the separation of investment fund management activities from other activities

In addition to Section 1, these activities are also to be separated from each other.

3. Rules for the separation of front office and back office activities

The Capital Market Act does not specify the contents of these activities, which are therefore to be specified on the basis of industry practices. In the course of separation the process for the acceptance, execution and clearing of orders is to be split into two to meet the requirements of the Capital Market Act.

4. Rules for the setting of decision making powers within the organisation;

These rules are found in the Articles of Association, in the Statutes of the Board of Directors based on the Articles of Association, in the Organisational and Operational Rules prepared on the basis of the aforesaid, and in the internal instructions prepared for their implementation. This condition can be verified if these documents are attached.

5. Rules for the retention of data

The wording of the Act leaves a broad interpretation for data, so data may be both electronic and printed. The rules for the retention of data shall therefore extend to the management of printed documents, recorded telephone conversations, and computerised data.

6. Confidentiality rules

The wording of the Act is also broad in this regard, so data subject to confidentiality may include electronic or printed data, as well as verbal information. These rules cover the rules for the management of printed documents, of data recorded electronically (by telephone and using computers) and of data obtained in verbal communication.

7. Rules for Access by Investors

This includes the postal address, telephone number, fax number and the electronic mail address of the investment fund manager, the deadlines for the acceptance of orders and the timing of their execution.

The following are the mandatory content elements of the Rules of Procedure of entities active in investment fund management (Annex No. 13):

- Rules for asset valuation principles;
- Rules for the principles of counterparty risk management;
- Rules for the principles of the assignment or delegation of the activities;
- Rules on how and how frequently information is to be provided to investors;
- Principles and rules for performance measurement;
- Professional qualification requirements for employees;
- Rules for investments made by senior officers and employees;
- Distribution rules.

Pursuant to Article 230 Paragraph (5), in addition to the above documents the investment fund manager shall also attach the following:

- a) Its organisational structure;
- b) The names of its senior executives and certificates of proof that the conditions under Article 356 Paragraph (1) are met;

Pursuant to Article 356 Paragraph (1) of the Capital Market Act, to be eligible for a senior executive position with an investment fund manager a person:

- Shall have an academic qualification;
- Shall have at least three years of professional experience obtained in the finance profession or in a management role in a financial or economic function;
- Shall have a clean criminal record;
- May not be subject to any of the exclusion criteria as specified under Article 357.

c) Its business plan (which should contain a textual analysis of the results that the firm intends to achieve from the given activity in the market during the coming three years, showing the planned revenues and expenses, and all of these shall be supported with numeric data).

If an investment fund manager applies for license to provide some investment service, then pursuant to Article 3 Paragraph (3) of the Investment Services Act, regarding this activity it shall be subject to the provisions that govern investment enterprises, and the authorisation of the activity shall be subject to the provisions of Article 28 of the Investment Services Act, as described in the Authorisation Guidelines for the authorisation of investment enterprises. In this case the fund manager shall also prepare money laundering regulations.

It is also a condition – pursuant to Article 230 Paragraph (6) – that if an applicant applies for an authorisation to engage in portfolio management activities, it shall then attach to its application for authorisation a certificate from the Investor Protection Fund that it has also submitted an application to join the Investor Protection Fund and has paid the corresponding joining fee.

Further documents to be attached include the articles of association, a copy of the application for incorporation, and the proof of payment of the subscribed capital, as well as the voucher certifying that the fees for administrative services as specified in a separate legal regulation have been paid (pursuant to Decree No. 12/2002 by the Minister of Finance the fees for a procedure to issue a license to perform investment fund management activities amount to HUF 100,000).

Special Provisions for Investment Fund Managers managing European Investment Funds

Pursuant to Article 242/A Paragraph (1), in addition to the activities specified under Article 229 Paragraph (1), fund managers managing European investment funds may also engage in the following activities:

- a) Safe custody and record-keeping of collective investment securities;
- b) Custodian services for collective investment securities.

Pursuant to Article 242/A Paragraph (3) a fund manager managing a European investment fund may receive a license to engage in the above activities and in investment advisory activities, if it has a license to engage in portfolio management activities.

The HFSA shall establish in a resolution that the investment fund manager meets the higher level statutory requirements for investment fund managers managing European Investment funds.

The documents to be submitted in the procedure are as follows:

- During the procedure the fund manager shall attach to its application its adequately amended procedural rules and its operating rules.
- Pursuant to Article 242/G Paragraph (1) the fund manager shall prepare risk management rules;
- Pursuant to Article 242/A Paragraph (6) a fund manager managing a European investment fund shall specify in its bye-laws – within the framework specified by the law – the reporting obligations of its employees and the system of record-keeping by the fund manager with regard to transactions completed for securities issued by the fund manager.

Article 242/A Paragraph (5) specifies a requirement stating that if a fund manager managing a European investment fund applies for authorisation to engage in activities as specified under Paragraph (1) Section a) or b) (safe custody or custodian services for collective investment securities), then it shall attach to its application for the authorisation, a certificate from the Investor Protection Fund, of its submission of an application to join the Fund and of its payment of the fees for joining.

The investment fund manager shall submit a declaration stating that the fund manager meets the requirements set forth under Articles 242/C-242/D.

Authorisation of the Activities of Venture Capital Fund Managers

Venture capital fund managers may engage in the following activities

Pursuant to Article 296/A Paragraph (2) a venture capital fund manager may engage exclusively in the following activities:

- a) Venture capital fund management as specified in the law; and
- b) Advisory activities related to the activity designated under section a) above.

It is to be emphasized, that the latter advisory activity is not identical to investment consulting or to consulting as designated under Article 5 Paragraph (2) Section d) of the Investment Services Act.

Organisational rules and subscribed capital

Pursuant to Article 296/C Paragraph (1) venture capital fund managers are governed by the provisions of the Act on Business Associations, branch offices are governed by the provisions of the Act on Branch Offices, with the derogations contained in this Act (Capital Market Act)

A special rule concerning organisational form and capital requirement is contained under Article 296/C Paragraph (2), stating that a venture capital fund manager may operate exclusively in the form of a joint stock company or a branch office. The subscribed capital of a venture capital fund manager may comprise only a monetary contribution.

We hereby draw your attention that – in the absence of a relevant express provision in the Capital Market Act – the creation of a venture capital fund manager does not require a license of foundation, so the registration procedure related to the foundation of the company may be completed even before the operating license is issued, but of course the firm may only commence activities that require license by the authority, once the license has been issued.

Documents required for the authorisation of operations

Pursuant to Article 296/D Paragraph (1) the applicant shall submit the following documents with an application for the authorisation of venture capital fund management activities:

- a) The articles of association and its amendment;
- b) Documents certifying the payment and the availability of the subscribed capital in full;
- c) A copy of its share register;
- d) Its organisational rules;
- e) Names of the business associations where it holds a stake, indicating the percentage of the share;
- f) Proof of payment of the administrative service fee as specified in a separate legal regulation (pursuant to Decree No. 12/2002 by the Minister of Finance, HUF 200,000 for a procedure to issue a license to engage in venture capital fund management activities);
- g) The name and license number of its auditor;
- h) A certificate by the auditor stating that the information technology system of the applicant, its accounting policies and accounting system are suitable for ascertaining its prevailing financial situation at any point in time;
- i) A certificate about the clean criminal record of the person in the senior position and the document certifying the academic qualification of the person in charge of the venture capital fund management activities;
- j) Its business plan (to contain a textual analysis of the results that the firm wishes to achieve from the specific activity on the market during the coming three years, with an indication of its planned revenues and expenses supported with numeric data); and
- k) Other documents certifying compliance with the rules contained in this Act.

Personal conditions

In addition to the documents specified under section i) above, the persons in senior positions with the venture capital fund manager shall submit declarations stating that they meet the condition contained under Article 296/B Paragraph (2) – that a person in a senior position with a venture capital fund manager may serve as a person in a senior position with a maximum of three other venture capital fund managers founded pursuant to this Act –, and that they are not subject to a conflict of interest as contained under Article 296/B Paragraph (3). (A person in a senior position with a venture capital fund manager may not serve as a person in a senior position with a business organisation providing investment services or supplementary investment services to the venture capital fund manager.)

Pursuant to Article 296/B Paragraph (5) at least one person from among the senior officers of the venture capital fund manager shall have professional experience of five years.

Pursuant to Article 296/B Paragraph (6) professional experience shall include:

- a) Time spent as the owner, senior officer or employee of an enterprise registered in Hungary or abroad and engaged in the investment of capital, or of an enterprise engaged in closely related advisory or asset management activities (venture capital or private equity fund manager, advisor, investment or holding company);
- b) Time spent as a person in a senior position with a target company of the capital investment of an enterprise specified under section a), on the basis of the designation of an enterprise under section a).