

Increased minimum share capital
requirement for limited liability companies
Legal newsletter



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Deloitte Legal Szarvas, Erdős and Partners Law Firm provides its clients with a monthly newsletter on the most recent changes and newly adopted regulations in economic law and the most notable legal cases.

The new Civil Code entered into force on 15 March 2014 and we have described the resulting changes in several editions of our newsletter. However, a deadline relevant for limited liability companies (Kft.) that is worth mentioning again is fast approaching.

Transitional rules

Under the transitional rules, private limited companies already existing at the time of the entry into force of the Civil Code are, as a general rule upon amending their articles of association for the first time after the entry into force of the Civil Code, they shall pass a decision on the continuation of their operation and amend their articles of association in such a way that it complies with the provisions of the Civil Code here is, however, an important exception to this general rule.

Probably the most substantial amendment to the Civil Code regarding limited liability companies is that their minimum share capital is now once again HUF 3 million. In this respect, **a two-year grace period was granted by the legislator to companies existing at the time of the Civil Code, allowing them to comply with this obligation before 15 March 2016.** Currently, if a limited liability company that had existed before the entry into force of the new Civil Code has a share capital below this amount and wishes to modify its articles of association for any reason whatsoever (e.g. in the case of a new managing director or amendment of registered seat), it will not yet be required to raise its share capital concurrently. However, if it does decide to do so, then the provisions of the previously effective Companies Act will continue to apply to its articles of association as well.

As a result, even today there are a number of limited liability companies whose share capital is below HUF 3 million and whose articles of association are not in line with the provisions of the Civil Code.

The grace period is nearing its end

For companies already in operation at the time of entry into force of the Civil Code, **the deadline for capital increase and for ensuring compliance with the new Civil Code will pass on 15 March 2016. Companies with a share capital below HUF 3 million shall increase their share capital to HUF 3 million before this date;** at the same time, they shall pass a decision on continuing operation under the Civil Code and shall amend their articles of association accordingly. Should they not wish to do so, **they have the option to transform the company into a different legal form, merge with another company, or terminate the company without succession.**

How can share capital be increased?

The simplest way of increasing share capital is cash contribution to the company. It is important to note in this regard that the company may decide to set a deadline longer than the one year specified in the Civil Code for paying the amount of the cash contribution not paid before the request for the registration of changes is filed; in fact, the Civil Code does not limit the extent of this payment deadline. **The only limitation is that the company may not pay dividends to its members as long as the sum of unpaid profits and the cash contributed by the members is less than the amount of the share capital. Another important obligation in this respect is that the members are liable for the company's debt up to the extent of their cash contributions not yet paid up.**

Under the provisions of the previously effective Companies Act, **the rules allowing share capital to be increased by using assets in excess of share capital** (essentially the capital reserve or the profit reserve) **remain practically unchanged.** However, to be **able to do so, the company shall prepare an interim balance sheet,** which may result in the process becoming longer and more expensive.

Of course, **the required amount of share capital may be provided through in-kind contribution. A special form of this is the debt-to-equity conversion in which a loan previously granted by a member to the company is converted into capital.** In practice, such a debt-to-equity conversion is performed as an in-kind contribution of receivables: the member provides the loan as receivables due from the company in the form of in-kind contribution where the title to the receivables is transferred by the in-kind contribution to the obligor (i.e. the company) and thus these receivables cease to exist.

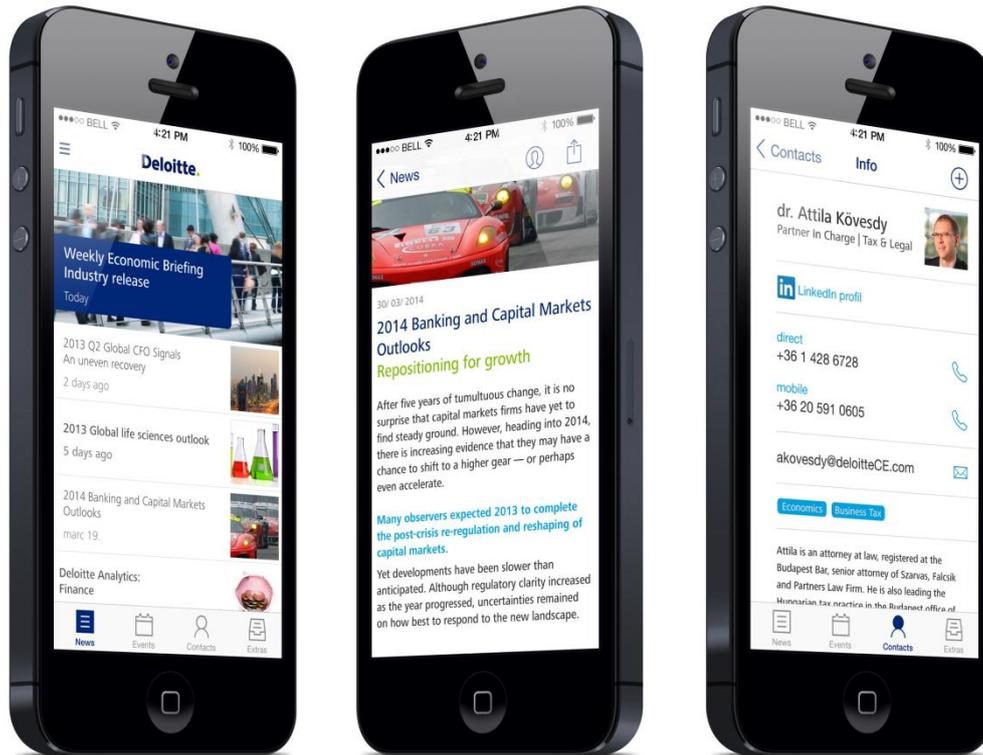
Procedural costs

The registration of mandatory amendments effected to ensure compliance with the Civil Code is exempt from duties and fees, provided that it involves only the decision to continue operation in accordance with the provisions of the Civil Code, or only the increase of the share capital in accordance with the new provisions of the Civil Code. The fees for the registration of any other changes are subject to the general rules.

Penalties

In case of a failure to ensure compliance with the Civil Code, the competent registry court may eventually decide to order the entity to be liquidated in a judicial oversight procedure. This is why the above deadline should be taken seriously and the necessary steps should be taken.





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