

## Business Advice Series Part Ten: Typical mistakes investors make in Hungary

### Don't lose out when divesting stake

**What should an investor pay attention to when he disposes of his business or share of a business in Hungary? In previous installments in this series the central themes were questions about the founding or acquisition of a firm from the legal or taxation viewpoints, operational problems, crisis management and restructuring - themes which affect investors again and again. At the end of the "life" of a business there is either the voluntary or involuntary liquidation of the company or (from the perspective of the investor) a separation from the business - as a rule by means of a disposal.**

Even in this last phase a few ground rules apply, especially from the tax viewpoint or to limit possible losses.

#### **Tax and liability**

There are two main themes here: 1), the aforementioned tax and 2), questions of liability or more precisely liability after divestment. From a tax perspective attention should be paid to where you must pay tax on any profit from the sale. The applicable tax laws can vary enormously from country to country. The aim should be to move the business or the part of it being disposed of to a jurisdiction where taxes are lower. It can make sense to contribute the to-be-disposed-of business into a foreign firm. Insofar as it (only) concerns a part of a business, then demerging that part and then contributing it into a foreign firm in a low-tax jurisdiction is a possibility.

Demerging can have turnover tax benefits in particular: disposing of the assets rather than the share of the business is liable to turnover tax. Disposing of a business or a share of a business however is not subject to turnover tax. Incidentally, it can also have other tax advantages, namely with land acquisition tax. Anyone selling land owned by a company must bear in mind the 10% land acquisition tax (*illeték*). By hiving off the land into a separate company he can achieve a tax-free sale of the land by the subsequent sale of the company (which now owns the land). As a result any "departure" from Hungary must also be well-planned from the tax angle.

The second important point is the issue of post-divestment liability. You don't want to end your involvement in a country but still worry for years about possible claims for damages being made against you. But it cannot be avoided completely - the liability of a departing member of a personal company such as a Bt. runs for five years and covers all events before your departure. Of course incorporated companies such the Kft. or Rt. are unproblematic. In these cases only the company is liable (with its entire assets) for any possible claims, and not the individual shareholders. By disposing of an "awkward part of the business" the whole company itself cannot avoid liability. An old company or a (hived off) new company are equally liable for existing contractual or legal claims.

If you observe the above rules you have every chance of departing from Hungary unscathed. Naturally there are many other themes besides those touched upon in this series, and of course it is crucial to get the experts involved who have full knowledge of all the relevant jurisdictions.

*The 'Business Advice Series' points out the recurrent pitfalls of doing business in Hungary and gives advice aimed at making your business more successful.*

## **Conclusion**

This series has endeavoured to cover the typical mistakes made in investment activity in Hungary. The key points were:

- 1 Before you start: Check, check, check
- 2 Be correctly established from the legal and taxation viewpoints
- 3 In Hungary “The law isn't like it is at home - or is it?”
- 4 In everyday business, tax is your Achilles heel
- 5 Mistakes in dealings with the authorities
- 6 We simply didn't notice it - Controlling (case study 1)
- 7 Lack of decisiveness in crisis management (case study 2)
- 8 After the conflict - stay the course (case study part 3)
- 9 Restructuring - if you do it, do it right
- 10 Don't lose out when you divest

Without doubt the amount of regulation in Hungary will increase. An important trend in Hungary is the - still too slow - move towards a service economy. A service economy will be even more strongly shaped by its staff - it is a “people business.” Future questions will emerge from this area, and the distinctive social intelligence of the Hungarians - with all its attendant strengths and weaknesses - will no doubt play a significant role internationally.